Housing in the Seventies

Working Papers 1

1973
1974
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National Housing Policy Review

Duane McGough

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National Housing Policy Review

U.S. Department of Housing
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Note to Reader

The U.S. Department of Housing and Urban Development (HUD) commissioned the papers contained in this volume with the understanding that research and data would be current as of the spring and summer of 1973. All papers in this volume, except as noted, were completed and submitted to the Department during that time. Readers are advised that certain information may be dated, therefore, and they should consider the analysis and conclusions of the author in that context. In some cases, which are noted in the volume, research was continued beyond the summer of 1973 and was completed in the spring or summer of 1974; those instances occurred where the Department concluded that a small amount of additional research would produce especially worthwhile results. In other instances, which also are noted in the volume, authors published their work separately; citations to those publications are included herein.

The papers in this volume have been edited by professional editors for syntax, style, and format; the style conforms to that of the *U.S. Government Printing Office Style Manual: 1973.* As that style permits, authors' individual treatment of footnotes, references, charts, tables, and like material has not been changed. Because of space limitations, appended material has been deleted in cases in which it consisted solely of material that had been published elsewhere, such as excerpts from books, reports, or the *Congressional Record;* in all such cases, an author's note advises the reader of the deletion and provides the citation to the deleted material.

Authors of the papers in this volume were advised of the intention of the Department to publish the papers and were provided with copies of the edited manuscript for review and for correction of incorrect or incomplete data. The authors' affiliations are current as of the spring of 1975. The views of individual authors are not to be construed as necessarily representing the views of the organizations with which they were associated at the time of publication of this volume or were associated at the time of writing of the paper; in some instances, authors state in a note the specifics of the disclaimer attached to that paper.

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Introduction

In the winter of 1973, President Nixon, in a major address to the Congress on Federal community development and housing policies, called for "the development of new policies that will provide aid to genuinely needy families and eliminate waste." [1]

Responding to this directive, James T. Lynn, Secretary of Housing and Urban Development (HUD), instituted the National Housing Policy Review, to serve as a wide-ranging study of Federal, State, and local housing programs; an analysis of their efficacy; and a series of recommendations for effective policies to meet the future housing needs of the Nation.

Contributing to the Review were housing experts within HUD and other Federal Government agencies, members of the academic community, and consultants from private research organizations and foundations. Together they contributed more than 150 studies and analyses covering the entire spectrum of housing and housing-related activities. Secretary Lynn designated a top-level task force to review and monitor the work. The task force was headed by HUD's Assistant Secretary for Policy Development and Research, Michael H. Moskow, and included William Lilley III, Deputy Assistant Secretary for Policy Development; Rudolph G. Penner, Deputy Assistant Secretary for Economic Affairs; and James B. Hedlund, Administrative Assistant.

Study teams, interdisciplinary in approach and composition, were organized; after they completed their data gathering and analysis, chapter teams organized and analyzed their material as well as that produced by other outside contractors. This material was rewritten entirely and published subsequently in October 1973 as the final product of the Review bearing the title *Housing in the Seventies.* As demand for copies of the study increased after the initial publication, that report was republished in a more permanent and accessible format in 1975. This volume, labeled *Housing in the Seventies: Working Papers,* reprints the bulk of the contractor papers prepared for the National Housing Policy Review, for which there also has been a steady demand since the completion of the Review.

In soliciting the contractor papers that went into the Review, every effort was made to obtain as wide a scope of viewpoint, opinion, and theory as possible. Accordingly—and predictably—the findings of the experts represent a decidedly nonmonolithic philosophy.

The papers included in these volumes form a large and representative—but by no means exhaustive—sample of the contributions by contractors made to the National Housing Policy Review. They were selected for publication because, taken together, they represent a composite view of the current thinking among scholars with regard to the Nation's housing policies—past, present, and future. They also are indicative of the wide diversity of opinion, noted above, among these housing experts. Included here are several papers within each of the Review's general analytical areas; in many cases they represent sharply divergent conclusions about the same subjects. It should be noted that some information in these papers may be dated, because of the time lapse between preparation and publication.

Some contractor papers were omitted from these volumes (either at the author's request or because they were duplicative of papers published herein); nevertheless a list of all contractor papers appears at the end of Volume 2. Any of these papers can be purchased from the National Technical Information Service (NTIS) of the U.S. Department of Commerce, Washington, D.C. 20036 or read in the HUD Departmental Library in Washington, D.C. Information on how to purchase individual papers from NTIS is included in the list of papers at the back of Volume 2.

Many of these papers are of a highly technical nature and may prove somewhat inaccessible to the lay reader. Each of them represents the views of the author exclusively and not necessarily those of the Department of Housing and Urban Development, the National Housing Policy Review, or other Federal agencies.

[1] State of the Union Message on Community Development, Mar. 8, 1973.

1 Legislative History

Evolution of Federal Legislative Policy in Housing: Housing Credits

By Milton P. Semer, Julian H. Zimmerman, John M. Frantz, and Ashley Foard
Semer and Zimmerman

Introduction

The gradual evolution of what has become a major and continuing housing-oriented role on the part of the Federal Government in the national credit markets had its origin in the fact that the free market, unconditioned by the considerations and mechanisms of public policy, failed to respond appropriately or adequately to the housing needs of the Nation. This fact reached its dramatic and overwhelming demonstration in the virtually complete collapse of the entire housing economy, including its home building and home financing sectors, during the Great Depression of the early 1930's.

No government could have failed to respond to a disaster of such magnitude, and the Government did respond. The trauma of the Depression brought about sweeping changes in every aspect of American political and economic activity, and not least in housing. New institutions were invented, new policies evolved, new procedures instituted, and entire new concepts developed.

Naturally, this did not all happen overnight, and not even in a few years' time. It has been over 40 years since the Federal Government took its first major steps to intervene directly in an effort to rescue and rehabilitate the housing economy. Twenty Congresses have sat during that time, and every one of them, without exception, has looked into housing problems and enacted housing legislation. The mere volume of resulting laws is formidable in itself. (The published laws relating to the Department of Housing and Urban Development alone occupy more than 1,000 pages, and these do not include obsolete legislation or the current legislation relating to housing programs of the Federal Home Loan Bank Board, the Veterans Administration, or the Department of Agriculture.)

This report will present an overview of the development of legislative policy with respect to the broad problems of housing credit. Because the purchase of a home is usually the largest and most important long term investment that the average man may make in a lifetime, and because almost no housing—for owner occupancy, sale, or rental—is built for cash, housing credit is the single most important factor in the efficiency, stability, and productivity of the home building industry and the residential real estate market.

This report is designed to trace briefly the considerations which led to each major new declaration of legislative policy affecting housing credit; to follow the major ways in which they have evolved in the years since; and to indicate which have succeeded and which failed, and why. Operating statistics and program data have been kept to a minimum, both in the interest of simplicity and clarity and to avoid adding to the already considerable length of the report. Enough figures have been included, however, to give the reader a sense of the orders of magnitude of the various programs and techniques discussed.

Since housing legislation has been the work of many Congresses, and of vastly more numerous Congressional committees and individual members, it need surprise no one that it has grown more complex as it has covered more and more subjects and been adapted to one crisis or problem after another. For the Depression was only the first of the great crises that have shaped national housing policy. After it came the war, and the postwar housing shortage; the Korean war; and a series of booms and recessions, of inflation and credit crunches. The multitude of spot decisions that were made led to some degree of overlapping, some inconsistencies of both goals and policies, and some outright contradictions. These too are noted.

Because of the tremendous bulk and complexity of the material covered, the treatment given the subject here is necessarily both selective and highly condensed. If it were not, this paper alone would have been the work of many more months, if not years, and would have extended to several volumes. The authors hope, however, that the materials included are comprehensive enough to afford the reader a general perspective on the role the Federal Government plays today in the generation and flow of credit in the housing market, and the steps by which it has reached that role from its status as a nonparticipant more than 40 years ago.

Generating Housing Credit Through Influencing the Flow of Savings—The Federal Home Loan Bank System

The President's Conference on Home Building and Home Ownership in December 1931 is often cited as providing the impetus for the original basic home financing legislation of the United States, especially that establishing the Federal home loan bank system. Essentially, the President's Conference was a factfinding body that identified the weaknesses and inadequacies of housing and home financing in the United States, as distinguished from an organization developing specific recommendations for home financing legislation.

The Federal Government's leadership in establishing a forum for consideration of these problems at a national level was of great historical significance. Although the documents produced by the conference did not directly call for increased or new Federal involvement in the national housing credit market, the fact appears to be that the President's initiative in calling such a conference and the reverberations of its discussions had much to do with the pioneering legislation which was shortly to follow. The conference highlighted for the Nation the existing inadequacies of home construction and rehabilitation, the need for further research and distribution of information on the subject, the crucial problems of building and loan associations and other lenders arising from the Great Depression then existing, and the flaws in foreclosure, zoning, and other State and local laws.

The Federal Home Loan Bank Act of 1932

Even before the convening of the Conference, President Hoover announced his intention to recommend to the Congress what he called ". . . a system of Home Loan Discount Banks," with four purposes:

1. To take pressure off sound home mortgage lending institutions and permit them to recover;

2. To stimulate home construction and increase employment;

3. To prevent repetition of the mortgage industry's collapse in the face of economic difficulty; and

4. To create a structure for the promotion of homeownership.[1]

In contemporary terms, it is instructive to note that the President considered as a sufficient basis to invoke Federal participation the fact that new home construction had then fallen drastically below a level of 200,000 units per year of "normal times"—as contrasted with a general agreement in the private and public sectors that the national need in the period of the 1960's and 1970's is a rate of new building on the order of 10 times that figure or more.

The Federal Home Loan Bank Act of 1932[2] authorized the establishment of a system of Federal home loan banks, roughly parallel to, and with functions in the field of, housing credit roughly analogous to those of the Federal Reserve system. Initially, the banks were to be capitalized by investment of Federal funds (originally intended to be appropriated funds, but later converted into capital subscription of the Reconstruction Finance Corporation), with the intent that the Federal capital would ultimately be retired by the investments of the member institutions—building and loan associations (later and now generally called "savings and loan" institutions) and, on a lesser scale, mutual savings banks, insurance companies, and similar major mortgage lenders.

The regional banks were to provide guidance, standards, and supervision. In addition, they were to provide an expanded source of credit to members by making advances on the security of mortgage loans held by them. To raise funds for this purpose—in addition to the provisions for members' subscription to capital stock in amounts fixed in relation to the volume of their business—the regional banks were given power to issue consolidated debentures in the private capital market. The security of these debentures was enhanced by making them all the joint and several obligations of all the banks—thus throwing behind each issue the underlying assets of the entire system.

Thus, taken as a whole, the system served:

- To provide national identity to a structure of home mortgage financing institutions;
- To introduce standards and criteria of sound performance;
- To provide the mechanism for a more dependable flow of mortgage funds;

[1] Press Statement of the President, Nov. 13, 1931.
[2] Public Law 304, 72nd Congress.

• To facilitate the flow of funds from areas of adequate to those of short supply.

Theory of Long Term Savings Institutions and Their Role in Home Financing

The Federal Home Loan Bank Act and the various pieces of perfecting and strengthening legislation that followed it did not seek to create an entirely new form of institution to provide funds for homebuilding and purchasing. Rather, they were intended to improve, rationalize, and strengthen institutional forms which had existed for at least a century, generally under the name of "building and loan association," and to reform their policies and practices so as to make them more responsive to the housing and economic needs of the country.

Underlying this approach were two closely related propositions: First, that encouragement of long term savings and habits of thrift was in the best interest of people generally—especially those who were heads of families—by virtue of encouraging individual responsibility, family stability, homeownership, and upward social and economic mobility of the industrious and provident. The corollary proposition was that long term individual savings are a peculiarly appropriate source of funds for home mortgage investment, as distinguished from the more volatile flow of funds in and out of the general investment markets.

In a simplistic way, it might be said that the objective of the system as it took shape and evolved was to provide for the ordinary citizen a way of investing his savings, with reasonable security and at a reasonable rate of return, to the end of accumulating resources that would permit him in due course to achieve homeownership.

In this light, the institutions intended to be served and strengthened were not considered to be "banks" in the ordinary sense, but were conceptually distinguished from commercial banks in a number of ways, of which the following were perhaps fundamental:

1. Funds of individuals in the hands of these savings institutions were not regarded as deposits in a custodial sense, but as investments in the institutions themselves—thus the special terminology that arose, referring to account holders as "members" or "shareholders," rather than "depositors," and to the funds themselves as "shares," rather than "deposits." Similarly, the earnings credited to shareholder accounts were referred to as "dividends" rather than "interest."

2. Consistent with this theory of individual savings as investments, the holders of accounts in savings and loan associations had no right to demand withdrawal. Instead, the associations had the power (consistent with regulations of the Federal Home Loan Bank Board) to impose a waiting period after an account holder made application for what was referred to as the "repurchase" of his shares in the association.

3. Checking privileges and other general banking services were considered to be outside the range of normal operations of these kinds of institutions.

4. The appropriate scope of investment activity for such institutions was deemed to be rather narrowly limited to the making of first mortgage loans on residential property.

5. Although participation of stock institutions owned and operated for profit of the stockholders was not ruled out, the thinking of the time placed heavy emphasis on encouragement of mutual institutions owned by their shareholders and operated for their common benefit.

Thus, the system of institutions which engaged new and significant forms of Federal support beginning in 1932 was conceived, broadly and simply stated, to have a dual function: First, to provide a means for accumulating the long term savings of individuals and families, and encouraging such savings; and second, plowing the capital thus accumulated back into housing in the form of first mortgage loans for the building or purchase of homes. While many variations and even idiosyncracies have developed within the system over the years, these conceptual threads have persisted throughout its history and have influenced its development along lines parallel to, but always distinguished from, the commercial banking system.

The Rescue Operation—HOLC

The Federal Home Loan Bank Act was designed to restructure the home savings and mortgage lending facilities of the Nation, and to rationalize their operations over the long haul. Before this could be done, however, there was an emergency situation to be dealt with of such immediacy and magnitude as to require other, more drastic short term measures.

In brief, the home mortgage lending industry was in a state of virtual collapse. New mortgage lending and new home building were almost nonexistent. The characteristic format of mortgage lending—a balloon-type loan for 5 years or less, at a high interest rate which had to be refinanced or paid off in full at the end of its term—had appeared to function reasonably well during boom times. Subjected to severe deflation and unemployment, it broke down. Lenders could not or would not refinance mortgages coming due; homeowners could not or would not pay them off. Values of both mortgages and the underlying security declined precipitously. Lending institutions with a large proportion of their assets in mortgages found themselves insolvent when the value of the mortgages evaporated. Vast holdings in junior liens—second, third, and even fourth mortgages—were wiped out as values fell below even the primary claim. Some 50 percent of all home mortgages in the country were in default. Foreclosures reached the astronomical rate of more than a thousand per day.

Less than a year after the establishment of the Federal Home Loan Bank Board, the Congress passed the Home Owners' Loan Act of 1933.[3] The act established a Home Owners' Loan Corporation, headed by a Board of Directors composed of the members of the Federal Home Loan Bank Board. HOLC's mission was to refinance home mortgages in default or process of foreclosure, and even to make loans to permit owners to recover homes lost through foreclosure or forced sale. To accomplish these purposes, it used Federal capital and funds borrowed in the private market on the security of federally guaranteed bonds. The original Federal Home Loan Bank Act had authorized the banks to make mortgage loans to individuals directly, as well as indirectly through the provision of credit to member institutions. This little-used authority was repealed by the act which established HOLC.

When HOLC's active lending program ended in 1936, it had made loans of more than $3 billion to refinance mortgages, pay delinquent taxes, and make essential home repairs, modernization, and improvements. In the course of liquidation of the Corporation's program in the years that followed, this investment was fully recovered, both for the Treasury and for the private bondholders.

HOLC, however, did more than stop a one-time panic and contribute to the restoration of confidence in mortgage lending as an economic activity and in mortgages themselves as valuable investments. In the course of carrying out its emergency mission, it pioneered the long term amortized mortgage, and demonstrated the feasibility of homeownership for people of only moderate means when financed through reasonable monthly charges related to income and credit rating. Thus it laid much of the basis for the complete restructuring of home mortgage finance that was to take place in the years that followed.

Rounding Out the System

In the same act that created HOLC, the Congress took another major step toward creating a modern, effective mortgage lending industry for the country. It authorized the Federal Home Loan Bank Board to provide for the "organization, incorporation, examination, operation, and regulation" of Federal Savings and Loan Associations, in order to ". . . provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes. . . ." (It is interesting to note that as recently as 1968 the authorizing statute was amended (among other purposes) to write into law the prohibition which had long existed in regulations against checking privileges on members' accounts (Public Law 90–448).) Charters were to be issued ". . . giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States."

As investment outlets, the new associations were virtually confined to making first mortgage loans on homes or "combinations of homes and business property" within a 50-mile radius from their home offices. Provision was made for initial capital subscriptions by the Treasury. Indeed, the Congress felt so strongly about encouraging growth of these new institutions that not only the associations themselves but the earnings of shareholders on their savings accounts were made exempt from income taxes. (This exemption was eliminated in 1942. (Public Law 834, 87th Congress).)

Each association was declared to be automatically a member on incorporation of the appropriate Regional Home Loan Bank. Provision was made for voluntary conversion of State-chartered member institutions to Federal status.

Thus the Board, which had been called into existence to create a reserve banking industry for mortgage lending and which had been used as the parent agency for HOLC, became the chosen instrument for a new and even more far-reaching reform—the effort to bring into existence and institutionalize sound and progressive

[3] Public Law 43, 73rd Congress.

home mortgage lending practices through a national system of local savings institutions built around federally chartered associations which were to serve both as leaders and examples.

Within a few years, the Federal associations, though only about a third in numbers of member institutions, held well over half the assets of member savings institutions nationwide.

Insurance of Savings and Loan Accounts

Nothing deepened the effects of the Great Depression on the financial community more severely than the catastrophic loss of public confidence—confidence in the integrity and stability of banks and savings institutions themselves, and confidence in the safety of private funds entrusted to their care. The bank holiday, banking reforms, and the establishment of the Federal Deposit Insurance Corporation did much to restore confidence in the commercial banking system. Perhaps no one thing did as much to renew confidence on the part of the small depositor as FDIC, which gave him the assurance of the Federal Government that, no matter what happened to the bank itself, his funds would be protected.

The analogy to individual savings in savings and loan associations was obvious, and indeed it seemed evident that such associations would be at a hopeless disadvantage in competing for individual savings unless they could offer comparable protection. In the National Housing Act (1934), the Congress took this logical next step, creating the Federal Savings and Loan Insurance Corporation in a now familiar format: The members of the Federal Home Loan Bank Board were to serve as the Board of Directors of the new Corporation, and initial capital was to be provided from Federal funds, to be provided, in this case by the HOLC.

Federal savings and loan associations were required to be insured by FSLIC; State-chartered member institutions were permitted to be so insured, upon providing satisfactory assurance to the Corporation that their operating and lending policies and reserve provisions met standards which the Corporation was empowered to establish. A premium was imposed of .25 percent of accounts of insured members, plus creditor obligations. In case of liquidation of an insured institution, the Corporation was required to be appointed conservator or receiver for Federal savings and loan associations, and authorized so to serve in the case of State-chartered insured institutions.

Recapitulation and Summary

The successive initiatives of the 3 years 1932–4 served to lay in the structural foundations of a complete overhaul of what is now called the "conventional" mortgage lending industry in the United States. Central to this overhaul were four major concepts and instrumentalities:

1. A specialized form of reserve banking system, tailored to the needs of family savings and home mortgage lending, and structured so as to maintain a flow of funds in times of short credit, as well as to permit a geographic flow of funds from regions with surplus funds for home mortgage investment to those where funds were in short supply;

2. A loosely integrated national system of local savings institutions primarily engaged in home mortgage lending, and built around a broad base of federally chartered institutions designed to illustrate the benefits of mutual ownership and serve as models of good practice and community service;

3. Federally underwritten insurance which guaranteed the safety of individual savings in Federal and insured member institutions; and

4. Overall, a Federal Home Loan Bank Board with broad regulatory, supervisory, and, within limits, disciplinary powers.

The institutional unity of the system was both strengthened and rendered more visible when the Board established a single Division now called the Office of Examination and Supervision to perform the functions of audit and examination both for the regulatory and supervisory functions of the Board and the Regional Banks, and for the protection of the insurance system. While serving the obvious purpose of efficiency and avoidance of duplication, this joint operation served as a continuous reminder to member and insured institutions both of a national purpose to strengthen and improve the savings and home mortgage lending system, and of a continuing Federal presence directed to the achievement of that purpose.

Nearly 40 years later, this basic structure is essentially intact. Over the years, as might be expected, a multitude of detailed changes has been made. FSLIC insurance coverage has increased in successive increments from an original figure of $5,000 for a single insured account to $20,000; concurrently, the insurance premium has been reduced, first to 1/8 and later to 1/12 of 1 percent. Restrictions on the investment powers of savings and loan associations have been progressively relaxed—in maximum mortgage amount; loan-to-value ratios; geographical coverage; and types of investments permitted. Within statutory guidelines, a wide variety of investments other than first mortgage home loans may now be made, and, in fact, savings and loan associations may now act as trustees for certain types of investment trusts—a function clearly falling in the category of "banking services" originally considered out of bounds for these institutions. But these are incidentals, however important. The central fact remains that the system is what it was designed to be: An organized structure for individual savings and home financing, characterized by a high degree of stability and providing by far the largest single (in the sense of organized or coherent) source of capital in the Nation for residential building and the movement of existing properties in the housing market.

The Federal Stamp

The record is clear that the earliest originators of the initiatives which led in logical steps to the existing Federal Home Loan Bank System —using that term in its broad sense—intended a far more limited and temporary Federal involvement than that which actually occurred.

The proceedings of the President's Conference of 1931 are replete with warnings against excessive Federal encroachment, and appeals for reliance on private endeavor with some degree of State and local regulation. It appears that President Hoover to some extent shared this view, while recognizing that Federal initiative and support were essential at least at the beginning. Indeed, he was to write, looking back on these events:

> . . . Nineteen years later, on Dec. 31, 1951, the eleven banks . . . had a total of over 4,000 member institutions with aggregate assets of more than $15,000,000. During that period the banks had made loans of more than $3,000,000,000, all repaid except for a current outstanding balance.
>
> Under the provisions for the absorption of capital by members, the government had been entirely paid off. As I had planned, *it had become in effect a private institution.* (Emphasis added.) [4]

It is difficult to avoid the conclusion that the former President's hopes and preferences here obscured his perceptions. For it seems abundantly clear that—whatever symbolic significance may be thought to attach to stock ownership—the Federal Home Loan Bank Board from its creation in 1932 was a Federal agency, and still is. So, too, was the HOLC during its temporary but indispensable existence. So, too, was and still is the Federal Savings and Loan Insurance Corporation.

In 1950, Congress further underlined the Federal character of the system by placing a billion-dollar line of credit (since raised to $4 billion (Public Law 151, 91st Congress)) to the Treasury (discretionary with the Secretary) behind the operations of the Federal Home Loan Banks, and a (mandatory) $750 million line of credit behind those of FSLIC.[5] This was done not because such emergency sources of funds were then needed or expected to be needed, but simply because the Congress thought it good public policy that they should be there if the need ever should arise.

The above discussion is not intended to consider one way or the other the merits of Federal involvement in housing credit, but rather to reflect the historical fact that under the impact of the Great Depression the Federal Government did in fact assume such an involvement on a theretofore unprecedented scale, and that the involvement continues to the present day. While the means and mechanisms adopted were financial, the motivations were social, as is reflected in President Hoover's own characterization of his purposes:

> . . . above all . . . [to promote] . . . home ownership, and employment on home construction.[6]

Generating House Credit Through the Reduction of Risk: The Mortgage Insurance System

Purposes of the System

The National Housing Act, enacted June 27, 1934, established the Federal Housing Administration to administer a new function of the Federal Government—the insurance of long term mortgage loans made by private lenders for home construction and sale, and the insurance of lenders against loss on shorter term loans for repairs and improvements of housing and com-

[4] Herbert Hoover, *Memoirs—The Great Depression*, p. 115.

[5] Public Law 576, 81st Congress.

[6] Op. cit., p. 111.

mercial properties. Its basic immediate purpose was to combat unemployment in the Great Depression, and its original long term purpose was to provide more and better housing through a general improvement in mortgage-lending practices and a general expansion of the residential lending and homebuilding industries.

As with the Federal Home Loan Bank system, the mortgage insurance program was brought into being by the urgencies of the Depression. It had resulted in the freezing of mortgage credit and an almost complete cessation of residential construction. Production of homes in 1933 dropped to 93,000 units, less than a tenth of the number built in 1925, and onsite construction throughout the country employed only 150,000 persons.[7] In addition to losses of jobs on the site, about an equal number were lost in the production of materials and equipment going into home construction.

At the same time, improvements to existing homes and other small buildings proved almost impossible to finance. Even apart from the depression condition, mortgage financing had been too cumbersome to be used extensively for the relatively small sums involved. Personal installment credit, on the other hand, failed to meet the credit needs in this field because the items involved in a modification job, such as a new roof or bathroom, could not be replevied. Manufacturers of the products used were generally not in a position to sponsor the needed credit because the materials involved came from a number of sources, and because labor (often self-employed) made up a large part of the total cost of the job.

As with much domestic legislation enacted during the Depression and recovery days, unemployment furnished the underlying impetus for the enactment of authority for the mortgage insurance and loan program. In the throes of the Great Depression, the executive branch and the Congress gave prime consideration to measures designed to reduce the massive unemployment existing throughout the United States. Where feasible, such efforts were directed to programs which could also help meet some additional critical depression needs. Legislation to restore the housing industry and promote home construction and repair work, with the resulting benefits to home buyers, builders, and lenders, was a natural mechanism for helping to solve not only employment but other vital social problems.

[7] H.R. Report No. 897, 81st Congress, 2nd Session, Committee on Banking and Currency on S. 2246, pp. 56-67.

In testimony before the House Banking and Currency Committee on May 18, 1934, the Federal Emergency Relief Administrator, Harry L. Hopkins, spoke first of unemployment:

> The building trades in America represent by all odds the largest single unit of our unemployment. Probably more than one-third of all the unemployed are identified, directly and indirectly, with the building trades . . . .
>
> Now, a purpose of this bill, a fundamental purpose of this bill, is an effort to get these people back to work . . . .
>
> . . . There has been no repair work done on housing since 1929 . . . .
>
> And, finally, we believe it is essential that we unloose private credit rather than public funds in the repairing of those houses and the building of new houses . . . .

Basic Statutory Functions Under the Original Housing Act

Home Mortgage Insurance: Section 203 of that act provides for the establishment of a "mutual mortgage insurance system" under which FHA could insure first mortgage loans made for the construction, purchase, or refinancing of one-to-four-family homes which would not exceed 20 years in term, or either $16,000 or 80 percent of the appraised value of the property.

The FHA was authorized to insure a mortgage loan only if made by a responsible lender able to service it. It had to contain provisions for periodic payments "not in excess of the borrower's reasonable ability to pay," and such provisions with respect to insurance, repairs, reserves, foreclosure, and other matters as FHA prescribed. The "project" with respect to which the mortgage was executed had to be "economically sound."

The interest rate on the loan could not exceed 5 percent per annum on the outstanding balance (or up to 6 percent under special circumstances).

The insurance provided gave the lender the right to receive in the event of foreclosure (and conveyance of the property to FHA and assignment to it of all related claims): (1) United States-guaranteed debentures (equal to the unpaid principal of the loan plus certain other allowances) maturing 3 years after the maturity of the mortgage; and (2) a "certificate of claim" (equal to the unpaid earned interest on the loan and foreclosure costs) payable only to the extent that FHA realized net proceeds from handling the property.

In return for this insurance protection, the Act required FHA to fix a premium charge of not less than .5 percent nor more than 1 percent per annum of the outstanding balance of the mortgage loan, which charge could be passed on to the borrower in addition to the interest on the loan. The FHA was required to classify the insured mortgages into separate groups "in accordance with sound actuarial practices and risk characteristics" and to set up a separate account for each such group. Whenever all the mortgages in a particular group account had been paid in full (or the money available in the account met certain requirements for payment), FHA was required to distribute the balance in the accounts for the benefit of the mortgagors, or homeowners. Hence the system was called "mutual" mortgage insurance.

Rental Project Mortgage Insurance: Section 207 of the original National Housing Act authorized FHA to insure mortgages on housing projects of Federal or State instrumentalities or private limited dividend corporations for persons of low income, if those projects were regulated as to rents, rate of return, and methods of operation. That program carried substantially the same insurance benefits as described above for home mortgages.

Repair Loan Insurance: Section 2 of the original National Housing Act authorized FHA to insure approved financial institutions against losses they might sustain as a result of loans for financing repair and improvements to real property. No such loan could exceed $2,000, or other limitations prescribed by FHA. The insurance to any one such institution could not exceed 20 percent of the amount of all its loans made for such purpose. This was changed to 10 percent by Public Law 486, 74th Congress, approved April 3, 1936. Thus, while the insurance payment was triggered by a default in the individual loan the outer limit of FHA liability was limited to a percentage of the aggregate of eligible loans made by the particular institution. This was an important safeguard since FHA did not initially process or approve the insurance of the individual loans.

Theory of FHA Mortgage Insurance System

Basically, the new mortgage insurance system was designed to protect lenders against loss on long term, amortized, high ratio mortgage loans. The protection was afforded through an FHA obligation to furnish, on default and foreclosure, insurance benefits up to the unpaid balance of the loan, with virtually no coinsurance by the lender. The system was to be self-supporting through the payment of premiums and fees to FHA that would establish an insurance reserve fund on an actuarily sound basis.

The Mortgage Instrument: The housing benefits of the new mortgage insurance system sprang largely from the government assumption of risk on this form of mortgage loan. Each of its features was important to the future of home finance.

Long Term Mortgage: Prior to the HOLC operation, it was customary in almost all cases for a home buyer to obtain two or three separate home mortgage loans, with the first mortgage being limited to what is today considered to be a very short term. Testimony [8] by Marriner S. Eccles, Assistant to the Secretary of the Treasury, given at the time the National Housing Act was being considered in the Congress, indicated that a 10-year mortgage was considered a long term mortgage by lenders at that time, and many home mortgages ran only 1, 2, or 3 years.[9] At the end of that short term, the home purchaser faced the expenses of refinancing and ran the risk resulting from changed market conditions. He faced the uncertainties of higher interest rates or even the unavailability of refinancing on terms he could afford, in which case he could lose his home and his equity investment through default and foreclosure. This characteristic of mortgage financing, along with the characteristics referred to in the next two paragraphs, contributed to the wave of foreclosures that came with the Great Depression and increased its impact.

Amortized Mortgage Loan: Generally, most of these earlier home mortgages were not amortized, and the payment of the entire principal or large balance ("balloon payment") fell due at the end of the short term of the mortgage. As it provided no system of regular level payments geared to the purchaser's ability to pay, the purchaser was either unable or lacked the inducement to make payments that would increase his equity and reduce his personal risk. That feature increased his dangers of default and loss.

Single First Mortgage With High Ratio Loan: The earlier first mortgage loans had such a low ratio of loan amount to value (State laws generally limited the ratio to 50 or 60 percent), that junior mortgage financing prevailed. Second and third mortgages bearing progressively steeper mortgage rates reflected their greater risks. Investment in these junior liens was considered

[8] National Housing Act (H. R. 9620 hearings before Committee on Banking and Currency, House of Representatives, 73rd Congress, May 18, 1934, pp. 1, 2.

[9] Ibid., p. 8.

speculative and interest rates up to 18 to 20 percent were common.[10] The speculative nature of this secondary financing reflected a risk to the home buyer as well as to the lender. His added interest cost and multiple financing charges increased the chances of default and loss of his property.

Relative Uniformity of Mortgage Requirements: The relative uniformity of the FHA mortgage requirements, quite apart from the Federal insurance itself, helped to encourage the flow of credit across State lines to areas of greatest shortage. For the first time, a home mortgage instrument was recognized and made marketable throughout the country on a substantial scale.

Cumulative Value of Long Term Low Ratio Mortgage: Almost all of the above benefits to homeowners were designed to have a corresponding benefit for homebuilders and lenders. The reduction of risk features for a purchaser reduced the risk and expense of foreclosure proceedings for lenders and provided more assurance of timely payment. The favorable financing terms for the home purchaser or owner broadened the housing market, bringing financing within the reach of persons of lower income and also benefiting builders and lenders.

Generation of Housing Credit Through Insurance Features of the System: Of course, the Federal insurance feature of the National Housing Act afforded the Federal financial backing necessary to the success of all the benefits of the Mortgage Insurance System. It was the key to generating additional credit for housing construction. Prior to mortgage insurance, the principal protection to the lender was the property covered by the mortgage. As this property, and the lender's rights to it in event of default, were wholly local, the mortgage loan did not lend itself to interstate transfers, or ownership by distant investors. With the Federal financial backup, the lender could look to the insurance as security, and the greatest risk of the mortgage investment was switched from the lender to the Federal Government.

Thus, along with the relatively uniform mortgage instrument, this novel insurance encouraged the flow of mortgage funds on a substantial scale from one part of the country to another where the need might be greater. Nonlocal lenders, such as insurance companies, could invest with confidence in mortgages originating in other areas of the country, relying primarily on the Federal insurance against losses in the event of default.

Actuarial Soundness—Lender Protection Without Loss to United States: Although the full faith and credit of the United States stood behind the FHA insurance obligation, there was an intent that the income to the FHA insurance fund would equal or exceed payments of insurance claims and other expenses. To accomplish this, the plan embodied in the Act had these prime characteristics:

Debenture System: Protection was afforded to the United States as well as to the lender through the unique authority to settle an insurance claim by furnishing long term obligations (debentures) to lenders, backed by the full faith and credit of the United States. Settling claims in debentures rather than cash permitted the FHA fund to avoid heavy cash withdrawals from the Treasury. In addition, a policy of orderly liquidation of acquired properties over a substantial period avoided the adverse effects of wholesale dumping of properties in an already distressed market. Taken as a whole, this plan was to permit the FHA to operate within its own resources even during a severe depression.

Premiums: The statutory authority for insurance premiums and fees was designed to enable the system to function on a sound businesslike basis, paying all administrative and other costs out of receipts and accumulating an adequate reserve against losses which might occur in the worst periods. Of course, in estimating the amount of reserve needed, consideration could be given to the advantages of the debenture system and other characteristics of the insurance. The administrative discretion given in the Act for determining the amount of the premium was considered adequate for adjustments to meet that objective. That is, the initial discretion to set premiums as low as .5 percent or as high as 1 percent was deemed appropriate because the system was too new to permit judgment to be made as to the precise rate.

Mutuality: The statutory plan of "mutuality" (returning to the homeowner, in effect, the unneeded portions of the premiums he had paid) was intended to assist in establishing an adequate insurance fund. As the future ratio of expenditures to receipts under the system was originally uncertain, the mutual feature enabled the premiums to be sufficiently high for soundness of the system, while at the same time assuring the borrower that his premium payments were not excessive.

[10] President's Conference on Home Building and Home Ownership, December 1931.

Mortgage Form: All of the features of the long term low ratio amortized mortgage loan which benefited the borrower, as described above, had a corresponding effect in strengthening the actuarial soundness of the whole insurance system. As they reduced the dangers of default and loss by the borrower, they reduced the degree of insurance risk to FHA and the amount of insurance claims that could be expected.

Individual Mortgage Transaction: Because the soundness of the insurance system was dependent on the soundness of the individual mortgage loans insured, the original act required each loan to meet the specific standards listed above. The FHA approval of each lender was a unique characteristic of the insurance system which entailed regulations and procedures as to his financial and other qualifications.

Intended Beneficiaries and Scope of Market: The several features of the mortgage insurance system that were intended to revitalize the housing industry and make home financing attainable for a vastly greater number of American families certainly benefited those of modest income more than others. However, the original system was not particularly concerned with the special housing needs of poor persons.

The mortgage insurance system was designed to help home purchasers and homeowners throughout the broad scope of the housing market, excluding only the abnormally expensive luxury homes where Federal assistance would be unwarranted. The originally authorized $16,000, 80-percent mortgage gave full insurance benefit to a $20,000 home. With today's costs, that home would be comparable to one costing 3 or 4 times as much. The repair loan insurance (as noted above) was not even limited to residential structures.

The only part of the original Act relating particularly to low income families was the embryonic authorization for mortgage insurance with respect to rental housing. Of course, its application was very restricted in any event, since it applied only to regulated projects of public bodies and limited dividend corporations.

Mortgage Insurance Benefits Having Indirect Credit Impact

The FHA mortgage insurance system embodies additional major features designed primarily to benefit the housing consumer but which have an indirect impact on general housing credit. These flowed from provisions in the original National Housing Act or from amendments:

Minimum Property Standards and Inspections: The importance of these standards is indicated by the title of the original act, which read as follows: "An Act to encourage improvement in housing standards and conditions, to provide a system of mutual mortgage insurance, and for other purposes." Pursuant to that language on standards, all housing to be financed with an FHA-insured mortgage must meet specific requirements formulated and promulgated by FHA. These are detailed and, in total, quite voluminous. They apply to the design of the structure, the quality of materials and construction, mechanical equipment, water supply, and sewage disposal. The location and condition of the site and, where appropriate, the subdivision planning must also meet specific FHA requirements.

Compliance with the minimum standards in the case of new home construction is obtained through inspections at three stages of construction. A more continuous supervision of construction is maintained, of course, in the case of new multiple units.

These various standards are designed to make the property more attractive and valuable to the home buying public in general, or to help assure preservation of the property over the life of the mortgage. In either case, the standards increase the value of the property as security for the mortgage by reducing chances of default and increasing recovery in event of default, foreclosure, and sale. Of course, this helps to make FHA-insured mortgages on such property attractive as investments, and to that extent helps to generate credit for housing. It also tends to encourage investment in conventional mortgages on the property in case of its subsequent sale or refinancing. Investment in housing in general is further encouraged to the extent that FHA standards affect the quality of construction of non-FHA housing in the locality or the quality of materials and equipment at the point of production.

Appraisals: In general, under the regular FHA mortgage insurance programs, the appraisal procedures have been a necessary and successful means of helping to establish the FHA-insured mortgage as a sound investment encouraging credit for housing. The original statute made appraisals necessary because maximum mortgage amounts were related to "appraised values." The appraisals are made by the FHA itself, generally through its own employees but sometimes through fee appraisers where essential because of workload.

Builders' Warranty: As supplemental to other construction compliance and with similar credit impact, a "builder's warranty" was required by the Housing Act of 1954. The act (Section 801) directed that the seller or builder of any new home assisted with an FHA-insured mortgage, or a loan guaranteed by the Veterans Administration, must be required to warrant for 1 year to the purchaser or owner that the dwelling is constructed in "substantial conformity" with the plans and specifications approved by the FHA or VA. This requirement grew out of investigations by the Housing (Rains) Subcommittee of the House Committee on Banking and Currency and the Teague Select Committee on Loan Guaranty Programs. It was determined by them that in many cases homes had not been built in conformity with the approved plans and specifications, sometimes leaving the purchaser or owner without legal recourse under his contract.

Although there had originally been strong opposition to the warranty as a mandatory requirement in the law, this opposition seemed to subside after enactment.

FHA Payment for Construction Defects: As further assurance that FHA-assisted property would meet construction standards, the Housing Act of 1964 (Section 121) authorized FHA to pay the owner of an FHA home any costs he incurred in correcting "substantial defects" in the home (or FHA could itself make the repairs) if such payment were requested within 4 years of the mortgage insurance.

Previously, the FHA had always correctly taken the position that it had no legal obligation, or even authority, to compensate homeowners for defects in FHA-assisted housing. The FHA standards and inspections were solely for purposes of assuring adequate security for the mortgage and no legal obligation in this regard ran to the homeowner. Actually, in cases where substantial defects occurred, the FHA often pressured the builder, frequently with success, to make adequate improvements. However, there remained a few "horror" cases, as where the builder was no longer in business or had no assets.

The above authority was extended (by the Housing and Urban Development Act of 1970, Section 104) in a broader form to existing housing, as distinguished from new construction, under the FHA Section 235 subsidized homeownership program discussed later. The construction defects covered include "structural or other defects which seriously affect the use and livability" of the dwelling. The Senate Banking and Currency Committee indicated in its report on the legislation that some FHA appraisers allowed blatantly defective homes to be sold to lower income families under the program when the purchasers understandably believed the Government was protecting their interests.

Cost Certification: The cost certification procedure was another protection against excessive mortgage amounts; this protection helped to preserve the investment quality of FHA-insured mortgages. The term "cost certification" refers to the builder's certification as to the dollar amount of his costs for specific items of construction, and related expenditures recognized by FHA. As first brought into the FHA mortgage insurance system for limited purposes by the Defense Housing and Community Facilities and Services Act of 1951 (Section 201), the cost certification requirement meant that the mortgage amount must be reduced, where necessary, to bring it within the builder's cost certification made after the completion of construction. Thus, the mortgage could not exceed 100 percent of the cost of physical improvements, so that the builder had to invest his land, time, overhead, and know-how. That act applied the requirement only to the new special mortgage insurance program (Section 908) provided in the act for rental housing in critical defense housing areas established during the Korean War. The same provision was soon applied to Capehart housing (Armed Services housing mortgage insurance, title VIII of the National Housing Act) by the Housing Amendments of 1953 (Section 10).

The above cost certification requirement was given little attention and is not well remembered. When "cost certification" is referred to now, it means a tighter and more stringent requirement enacted as part of the Housing Act of 1954 (Section 126).

That provision (Section 227 of the National Housing Act) is more specific, and sharper in defining the housing project costs to be allowed in the computation of cost. More importantly, it requires the mortgage to be reduced (after the construction and certification) to a fixed percentage of those costs—the same percentage prescribed by law as the maximum ratio of mortgage loan amount to value (or to replacement cost). Thus, where the law prescribes a maximum 80 percent ratio and the certified cost is $900,000 on a project where its estimated value had been $1 million, the mortgage has to be reduced to 80 percent of $900,000. This more onerous restriction was applied to all FHA multifamily projects.

This cost certification requirement was one of the principal responses of the Congress to the "FHA scandals" of national proportion that rocked the housing industry and Government agencies in 1953 and 1954. The World War II and postwar veterans housing of multifamily rental units (Section 608 housing) came into disrepute largely because of "mortgaging out" in a substantial portion of all projects under the program. That term means that excessively high values and mortgage amounts were authorized by FHA, resulting in the sponsor's walking away with possibly large amounts of leftover cash from the mortgage, after paying all his costs and with no money of his own in the project. At that time, there had been heavy pressure on FHA to get sponsors to undertake projects rapidly, and rising prices of land, materials, and labor had made it difficult to estimate future costs. Indeed, some of the cases of mortgaging out resulted from FHA's recognition of high costs during 1948, when the estimates were made, when actual construction took place during 1949, when costs had dropped.

Forebearance: In addition to the obvious benefit to the home purchaser, liberal forebearance procedures of the mortgage insurance system provided a direct accommodation to lenders with default problems. Also, the increased consumer demand for mortgage assistance, resulting from these favorable terms for the borrower, further increased the attractiveness of home mortgages for investment.

Originally, any concession by FHA to forebearance, which the lender requested for the borrower, was done administratively. When, on request of the lender, FHA found a default on an insured home mortgage to be due to circumstances beyond the control of the mortgagor, it could approve an extension of time for curing default and a recasting of the amortization.

Notwithstanding FHA's foreclosure procedures, considerable concern developed in the Congress over the plight of home purchasers faced with foreclosure through no fault of their own. Special attention was given to unemployed wage earners in depressed areas, or others who had been employed in industries curtailing production. Various bills had been introduced on the subject. In response, the most effective forebearance procedure was authorized by the Housing Act of 1959 (Section 114(a)). To avoid foreclosure, the FHA was permitted to accept a home mortgage in default, along with the property securing it, and pay the insurance benefits to the lender. Thereafter, the lender had no connection with the mortgage, and FHA was free to carry out such foreclosure arrangements with the homeowner as it determined best.

The Housing and Urban Development Act of 1965 provided for "moratorium" relief to "distressed mortgagors" who were homeowners with FHA insurance or VA guaranty in an area with a closed military installation, if the mortgages were in default because of the homeowners' inability to make mortgage payments. In such cases the FHA or VA was authorized to assume the obligations of those homeowners for a limited period.

Interest Rates and Discounts: Although the FHA maximum interest rates on mortgages are intended as consumer protections, the administrative increases or decreases of ceilings within the statutory maximums also can affect housing credit generally. The interest rate ceilings have also been one of the factors in providing uniformity in mortgage terms that has helped to generate credit for housing. Until the statutory interest rate maximums were suspended and left to administrative discretion under temporary authority beginning in 1968 (Public Law 90–301), the original statutory ceiling for regular Section 203 mortgages had been virtually unchanged.

Throughout FHA's history, its maximum interest rate ceilings have undoubtedly prevented excessive rates and abuses that would have occurred otherwise at certain times and in certain places. Also, it is fair to say that these FHA maximum rates have been kept at or below market interest rates on noninsured mortgages.

In times of severe credit shortages, however, when market interest rates are unusually high, lenders on FHA mortgages have resorted to charging substantial discounts in addition to interest rates. Actually, the amount of the discount, which is charged as a lump sum, plus the amount of the interest, often constituted the price which had to be paid to get the mortgage funds at the particular time and place. Generally, the amount of the discount was the amount the originating lender would otherwise lose in selling the mortgage in the secondary market. The FHA did not permit the lender to require the borrower to pay the discount, so the lender charged the seller or builder of the dwelling. Naturally, this tended to increase the sales price of the house, because the increase was not effectively prevented through the appraisal process.

At times, discounts were so large in connection with FHA-insured and VA mortgages that the Banking and Currency Committees became very alarmed, and fully investigated the subject. Of course, the Congressional concern grew out of consumer complaints and publicity concerning the problems. As a result, the Housing Act of 1950 directed the FHA and VA to issue regulations, applicable uniformly to all classes of lenders, which would limit the charges and fees imposed upon the builder or purchaser in connection with construction or sale of housing.

These regulatory controls were adopted and were almost completely unsuccessful. In the case of VA, a maximum 1-percent discount was imposed which curtailed use of the program so extensively that Congress modified the statute in the Housing Amendments of 1953.

Basically, however, the controls were unsuccessful because they were inconsistent with the economic facts of life, and were impossible to enforce. There was no practical means of preventing a discount to be paid to the lender by a builder in the form of some collateral benefit not overtly tied to the mortgage transaction. The controls were repealed by the Housing Act of 1954 (Section 813).

Amazingly, the Congress (in Section 605 of the Housing Act of 1957) required the FHA and VA again to impose discount controls in a form that would vary them by areas and mortgage terms. Those controls were equally ineffective and soon repealed (Section 6 of the Emergency Housing Act of 1958). In reporting that bill, the Senate Committee on Banking and Currency said that the complication of the controls reduced investment in FHA mortgages, particularly for low income families.

Equal Opportunity: As with many requirements adopted for purposes other than credit expansion, the application of equal opportunity requirements to housing has had a direct effect on the availability of mortgage credit.

Through the earlier portion of FHA history there was no involvement or concern with equal opportunity for the purchase or occupancy of housing. In fact, race was not regarded as a factor in any mortgage insurance operations except as to the effect of changing racial patterns in the locality on the value of the proposed housing. The first real response to heavy pressure for some action in this area was the administrative decision in 1950 not to insure any more mortgages on real estate subject to covenants against ownership or occupancy by members of certain races.

The first step of sufficient magnitude to affect FHA housing production or credit was President Kennedy's 1962 Executive Order (E.O. 11063) on Equal Opportunity In Housing, which applied to all new FHA or VA housing and related properties which could be covered (in the view of the Department of Justice) without Constitutional objection, in the absence of legislation dealing specifically with the subject. There was strong objection from the industry on the ground that the Government-assisted housing would be shunned by lenders and purchasers alike, who would shift to conventionally financed housing which was not then subject to equal opportunity requirements. Some objective observers also felt that the FHA production would be greatly reduced to the detriment of home purchasers who would otherwise receive the FHA consumer benefits not available under conventional financing. Others felt the Executive Order was not sufficiently enforceable to prevent the unscrupulous from profiting at the expense of those who would comply.

There may have been some adverse effect on FHA operations from the Executive Order, at least initially. However, it did not reach any significant proportions as some predicted, or convince anyone in hindsight that the policy of the Order was wrong. Even at present, experts cannot measure the effect of the Order on the FHA market at that time, but generally content themselves with the conclusion that increasing availability of credit offsets any possible adverse effect the Order may have made on FHA operations.

As to enforcement, the old reliable threat of withholding future mortgage insurance from the violators of an FHA regulation proved to be a reasonably adequate enforcement mechanism.

Presumably, if a sponsor was set initially on large-scale avoidance of equal opportunity requirements, he would not follow the mortgage insurance route in the first place.

The special concern of FHA's being singled out for regulation came to an end with the enactment of Title VIII of the Civil Rights Act of 1968 (the "Fair Housing" law), which, through a staggered application, covered all housing (and related transactions) as to both sale or rental, excluding only a single-family house sold or rented by the owner without any use of a broker or similar agent, and units in certain rooming houses. That act contains specific enforcement mechanisms.

Although the credit impact of the issuance of the Executive Order on Equal Opportunity cannot be quantified, it constituted at that time a typical example of two program policies that have divergent, if not inconsistent, objectives—production versus another social purpose. Although the application of equal opportunity regulations to housing has been resolved by statute, similar policy conflicts exist with respect to production versus other consumer benefits such as low interest rates and high property standards. More frequently, the conflicting social objectives have not been adverse to production but to other features of the mortgage insurance system generally considered basic. Thus, looseness of property standards and mortgage terms to enable FHA construction to proceed in outlying areas is inconsistent with the objectives normally sought by FHA. That is, quality is sacrificed to obtain quantity.

Whenever volume production, or another desirable objective, is in conflict with another social purpose, there are generally some persons with extreme views who would support one to the exclusion of the other. In general, however, there continues to be acceptance of a modification of the traditional mortgage insurance system to accomplish a special social purpose if production and other basic features of the insurance are not substantially thwarted.

It must be emphasized, of course, that the Fair Housing Law of 1968 presented a quite different relationship of civil rights objectives to housing production, because the law applies to virtually all housing. Instead of restricting any portion of production, the overall effect of the law tends to increase the volume of production by broadening demand. By making new homes and rental accommodations available to minority families, which have the most urgent need and an increasing ability to purchase or rent new units, a substantial segment of the population is brought into the market for new FHA (as well as other) homes and apartments, especially in metropolitan areas.

New Special Forms of Ownership

Cooperatives: Special mortgage insurance terms were authorized for housing cooperatives by the Housing Act of 1948. These terms permitted mortgages on new housing cooperatives to be up to 95 percent of replacement cost where the cooperative members were primarily veterans. The mortgage could be on (1) a project of a management type of cooperative (a nonprofit cooperative ownership housing corporation, the permanent occupancy of the dwellings of which are restricted to members of the corporation), or (2) a project of a building cooperative (a nonprofit corporation organized to build homes for transfer to the members' individual ownership).

The basis for this provision was a belief, expressed by the House Banking and Currency Committee in reporting the bill, that veterans' organizations in particular could use the cooperative as a means of joining together to produce housing with cost reductions not otherwise attainable. The original concept was a "consumer cooperative" which could eliminate or reduce expenses of private sponsors' profits. Reliance was placed on the success of cooperative ownership in other fields.

In the Housing Act of 1950, the above authority was expanded into a new separate program called the Section 213 program. That was conceived by cooperatives and veterans groups, and put into recommended legislative form by the Housing and Home Finance Agency.

Section 213 contained further liberal terms, including, for the building cooperative, the terms of the regular FHA single-family program where that would be advantageous. This legislation contemplated the sale of the mortgages to FNMA under its special assistance operations. That was on the basis that lenders generally were not yet ready to invest in this still-unfamiliar form of ownership.

This legislation was enacted in an era of strong pressure for cooperatives taking a dominant role in the future of housing throughout urban areas of the country. The major thrust of the Housing Bill of 1950 (S. 2246) as proposed by the executive branch that year (after House Committee action the previous year on Section 213, but prior to enactment of Section 213) was a massive new direct loan program for cooperatives and other nonprofit corporations building housing for moderate income families. The effort of the Administration to obtain enactment of that program may have been as great as any effort ever put forth by the executive branch to establish a new housing program. That program was defeated by a few votes in the Senate.

The Section 213 program, with the FNMA secondary market assistance, soon prospered. Builders were reluctant, however, to deal with consumer-originated cooperatives, and the typical cooperative was initiated by a developer who lined up the requisite number of members prior to insurance. Within 3 years, about $225 million of insurance had been written under the program, but few Section 213 mortgages were sold to secondary market purchasers other than FNMA.[11]

Gradually through the years, Section 213 mortgages became more marketable, and special

[11] President's Advisory Committee on Government Housing Policies and Programs, pp. 41, 42, 1953.

assistance for them, as such, under FNMA eventually became unnecessary and ceased. Section 213 operations constitute probably the best example of FNMA serving as an instrument for getting the private secondary market to accept a new form of homeownership or a new special purpose insurance program.

Limited Dividend and Nonprofit Corporations: From the very beginning of the mortgage insurance program, there was concern over providing such liberal credit advantages to sponsors of housing projects that it might result in excessive profits to them. This danger was seen in terms of the management period, rather than the construction period discussed above. Thus, Section 207 of the original act authorized mortgage insurance for rental structures only if held by public bodies or certain types of limited dividend corporations.

A few States had already enacted limited dividend laws applicable to housing construction. These provided for a maximum profit or dividend, about 6 percent annually on the amount invested, and for regulating the corporations as to operation and management. Relatively few housing units were provided under those laws in the early 1930's, and some Federal assistance was given to them by the Reconstruction Finance Corporation.

The limited dividend system was successful at controlling profits during management, but never offered much prospect of being extended to a substantial amount of housing during those early years. An annual profit of 6 percent was not sufficient inducement for private enterprise, whose scale of operations was needed to increase production in volume. In future legislative authorizations for FHA rental housing insurance, specific use of the term "limited dividend" corporations or trusts, if used at all, was used along with nonprofit or other corporations having similar mortgage insurance advantages. The Section 207 program was soon broadened to cover all private profit corporations regulated as to rental and other matters of operation. Special provisions for public bodies and limited dividend corporations were retained only to the extent of authorizing a larger dollar amount for an insured mortgage.

The next use of a concept for reducing or removing the operating profit margin in FHA rental housing was the housing cooperative under the Section 213 program discussed above, which was successful in that purpose and in providing a volume of production. Through consistent amendments during the life of FHA, the housing cooperative has been given—with respect to mortgage insurance for both single-family homes and multifamily structures—at least all of the advantages of other forms of profit-motivated ownership. In addition, it has been given the special advantages accorded nonprofit and limited dividend corporations.

In general, the rental housing programs of FHA have followed the Section 207 pattern of regulating rentals and other operations but permitting reasonable profits.

Originally, the special mortgage insurance program for families displaced from their homes by governmental action (Section 221, enacted in the Housing Act of 1954) was restricted to nonprofit sponsors.

The special mortgage insurance program for the elderly (Section 231, enacted in the Housing Act of 1959) provided special advantages for public and nonprofit owners, namely a maximum mortgage amount that could equal 100 percent of "replacement cost." Corporations operating for profit were made eligible but then the mortgage amount could not exceed 90 percent of development cost. With the demand for housing elderly persons, and FNMA special assistance where needed, that program prospered and is a significant part of all FHA volume.

In the more recent "rent supplement" program enacted in 1965 and the Section 236 program enacted in 1968 (which are discussed later under a separate heading), the project owner must be a limited dividend corporate or other entity, a cooperative, or another private nonprofit corporation. These programs include specific subsidies which in effect pay part of the rentals of the tenants, and therefore restrictions on operating profits are especially appropriate. Under these programs, limited dividend sponsors have become numerous because some profit is authorized for them in contrast to the other eligibles, the cooperatives and nonprofits.

Of course, it would be naive to imply that the profit motive is not involved in projects of nonprofit corporations. The profit of the construction contractor is always present, together with such management, financing, and other fees as may be involved. Actually, as indicated in connection with cooperatives, the nonprofit corporation may have been originated by the builder or others seeking profit through related transactions. On the other hand, many nonprofit mortgagors are church groups or other organizations having no self-serving motives in building for elderly or other needy persons.

The FHA has pioneered in bolstering the opportunities of cooperatives, limited dividends, and nonprofit corporations building rental and other housing. Undoubtedly, the social objectives of their operations under FHA programs will be of continuing concern to the Congress in considering further housing legislation.

Condominiums: The extension of FHA mortgage insurance to the new form of ownership known as "condominiums" constituted one of FHA's most successful ventures. Condominiums had existed for some time in Puerto Rico and a few Spanish-speaking areas of the United States on a limited scale. The FHA insurance program was first made applicable to this form of ownership as late as the Housing Act of 1961. The condominium concept is similar to that of a cooperative except that the individual unit, generally in a multifamily structure, is actually owned by the occupant and can be separately encumbered by a mortgage or can be separately sold. Each owner of a unit owns a share in common areas of the building and grounds such as hallways and parking space, and participates in building-maintenance payments. This form of ownership has distinct advantages for the home purchaser who does not want to be responsible (as comortgagor) for lack of payments by his neighbors on a blanket mortgage covering a whole multifamily structure.

The new mortage insurance provisions treated the individual unit in a structure like a single-family structure. Thus, when the buyer of the unit gives a mortgage covering that unit, the same mortgage terms are applied as in the regular FHA insurance program for single family homes. As to the blanket insured mortgage, covering the whole structure until such time as the individual units are sold off, mortgage terms are applied similar to the terms applicable to a multifamily structure under the regular insurance program.

The only important problems with condominiums were technical ones under State laws. That is, such laws as those on property taxes and title records and insurance were not framed so they could be applied separately to individual units in a structure. As a result of model legislation submitted to the States by the Housing and Home Finance Agency, almost all States adopted adequate legislation in this regard within 2 or 3 years.

The success of this mortgage insurance operation contributed in no small way to the rapid rise of condominium building throughout the United States—a boom that is still continuing and that is, of course, not limited to FHA housing.

Selected Use of New Underwriting Concepts

The original National Housing Act contained two basic underwriting concepts: (1) The property or project with respect to which the mortgage is executed must be "economically sound," and (2) the maximum mortgage amount cannot exceed a percentage of "appraised value." These two requirements are still effective with respect to the regular basic FHA mortgage insurance, that is, the program for one-to-four-family dwellings under Section 203, and the program for multifamily projects under 207 (excluding certain special purpose housing).

No one can question the merits of these two concepts for underwriting purposes. However, the application of them in FHA became very controversial and continued so for several years in the late 1940's and the 1950's. It was contended by groups favoring FHA mortgage insurance for special social purposes that FHA consistently used its underwriting procedures in an unreasonably conservative manner in order to defeat those purposes and avoid the burdens of new or unfamiliar activities. This view was shared by many in the Congress and by some non-FHA offices in the National Housing Agency and later in the Housing and Home Finance Agency. It was true that although the term "economic soundness" in mortgage insurance originally had no different meaning from the usual sense that those words are used, they came to be words of art encompassing the elaborate minimum property standards and established underwriting procedures of FHA.

Accordingly, when proposed special FHA programs were developed in the Executive Branch, or sometimes in the Congress, care was taken to avoid the term "economic soundness" in order to assure that the class of housing intended to be assisted with mortgage insurance would go forward as intended. Generally, the term "acceptable risk" was substituted. The special FHA programs are discussed later under a separate heading.

For similar reasons, "replacement cost" was generally substituted for "appraised value" in these new programs, as indicated above in the cooperative housing program. This substitution of terms had a more substantive meaning, however, than the one substitution above. Because "replacement cost" is only one of the three limitations normally used in determining "value," a maximum mortgage amount computed on the basis of replacement cost alone usually results in a higher maximum amount. "Value" is the lowest of (1) replacement cost, (2) prevailing sales price of similar real property, and (3) capitalized value based on "estimated net return" and "estimated fair return."

As a later supplement to substituting "replacement cost" for "value" in special insurance programs, the Congress began injecting into such programs a provision that required "replacement cost" to include "an allowance for builder's and sponsor's profit and risk of 10 per centum of all" the other items of cost except land, unless the agency certified that the 10 per centum was unreasonable. It was first applied by the Housing Act of 1956 (Section 107(a)) to the FHA Section 220 special insurance program for housing in urban renewal areas.

The provision was adopted because the Congress felt that assurance of that large a sponsor's return was extremely important to the entire urban renewal program, which had been floundering because of difficulties in getting housing underway on urban renewal sites as planned. Section 220 was the only feasible instrument for doing that, and sponsors had not been very interested in it. In reporting the Housing Act of 1956, the House Committee on Banking and Currency said the profit margin being allowed sponsors under Section 220 was not sufficiently high to attract them, and was unreasonably low. (The FHA had allowed a percentage, based on local custom and project size, that had varied between about 5 percent and 10 percent.)

Clearly, the above new underwriting standards were designed to force FHA into a more liberal insurance system for the special purpose programs. At the same time, however, the changes certainly were not intended to be used as justification for unsound or "bad" loans. The term "acceptable risk" preserves the connotation needed for keeping the mortgage insurance system on an actuarially sound basis. In general, the FHA programs using the new terminology have been so operated, particularly the Section 213 program discussed above, which has had one of the best records in accumulating a reserve of insurance funds sufficient to cover possible insurance claims in the future.

In any event, to determine that a loan is reasonably sound, the underwriter must ultimately find reasonable expectation of mortgage payments. In the case of rental property, this means reasonable prospect of project income adequate for those payments, taking into consideration all relevant factors over the life of the mortgage. This was often the controlling factor.

Growth of the Mortgage Insurance System

Insofar as Federal legislation was concerned, the FHA mortgage insurance system was a viable program from the beginning. The system would have grown and prospered, although in a truncated fashion, if the National Housing Act had never been revised (except as to extensions and changes made necessary by inflation and the passage of time). The program got underway with surprising swiftness, considering the novelty of the system and the enormous number of institutions and agencies throughout the United States which were involved.

Perhaps the most important delay factor was the need for State legislation to make FHA-insured mortgages legal investments for banks, State savings and loan associations, insurance companies, and other State-regulated financial institutions or other public or private investors. State laws generally restricted these investments to 50 percent or 60 percent of the value of the property securing the mortgage, and frequently limited the eligible term of the mortgage. At that time all States except New York and New Jersey met in regular session only once every 2 years, and those sessions were in even years in almost all States. However, a number of States had begun holding special sessions to help meet depression problems, including the enactment of enabling legislation to permit participation in Federal programs. Accordingly, within 2 years, most of these State law problems were removed by specific State legislation. Similar Federal legislation authorizes investment by national banks in FHA mortgages.

During 1934, the FHA insurance was all on Title I (Section 2) repair and rehabilitation loans amounting to $27 million. In 1935, total FHA insurance amounted to $297 million, including home mortgage insurance of $93 million and mortgage insurance on rental projects amounting to $2 million.[12]

Major changes in the legislative authority for the basic mortgage insurance program which affected its growth were:

[12] Allan F. Thornton: "The Economic Impact of Federal Housing Administration Insurance Programs" (HUD Library 332-72-T36) pp. 17 et seq.

1. Amendments making eligible for mortgage insurance a multifamily project with a profitmaking sponsor.

2. Liberalization of the maximum loan-to-value ratio of an eligible mortgage, which permitted increasingly lower downpayments by the purchaser or sponsor.

3. Lengthening the maximum loan period of the eligible mortgage, which permitted smaller monthly amortization payments.

4. Increasing the maximum dollar ceilings of the individual mortgages, especially in the case of home mortgages.

Other legislative changes in program scope and mortgage terms had appreciable effects on volume and growth. Also, of course, other Federal legislation and administrative actions had major impacts on the size of FHA operations, such as actions affecting the secondary market of residential mortgages and monetary controls of the Federal Reserve Board.

The legislative changes affecting mortgage insurance followed no pattern through the years other than that of broadening its scope and liberalizing its terms. The changes were often spasmodic, but there were recurring justifications or reasons behind similar enactments. The liberalized mortgage terms enacted through the years increased the volume of FHA-assisted housing, and generally each amendment changing those terms increased volume appreciably.

Economists are inclined to express these changes in terms of countercyclical steps. At times, a major motive behind the legislation, particularly on the part of some officials of the executive branch, was the desire to expand those Federal activities that could spur the economy in times of recession. Just as housing construction usually is affected more quickly and severely than any other industry by adverse economic conditions or shortages of mortgage funds, steps which will increase housing production can have a more immediate and substantial effect in providing or maintaining employment and bolstering a lagging economy. Because of the Government's ability to affect production through its administration of residential mortgage insurance, it has been a prime target for manipulation in times of recession.

As a matter of political reality, however, the reason FHA programs have been repeatedly made more liberal, encompassing additional techniques and objectives, has been the desire, both in the executive branch and the Congress, to bring adequate housing to more American families. This generally has meant liberalized provisions to reach more families with lower income.

Of course, large segments of the increased FHA volume built up through the years has been under new special mortgage insurance operations, discussed later, which were established for the benefit of special groups or for special purposes.

The development of the above changes in the FHA legislation may be viewed more specifically:

Multifamily Rental Housing: The National Housing Act Amendments of 1938 completely rewrote the insurance provisions relating to multifamily housing projects (Section 207), particularly to cover mortgages on rental housing built by profit motivated sponsors. As a result, mortgage insurance for rental housing became for the first time a substantial part of the mortgage insurance system. Individual mortgage ceilings were prescribed, including an 80 percent loan-to-value ratio and a $5 million maximum. The part of the property attributable to dwelling use could not exceed $1,350 per room. The maximum mortgage term was 25 years. The insurance was similar to that for home mortgages except that advances on the mortgage were insured and, in case of default, the lender need not foreclose but could, if he wished, transfer the mortgage to FHA and receive the insurance benefits (which would be reduced slightly in view of the shift of the foreclosure burden to the FHA). As previously indicated, the sponsor was regulated as to rents and other operations.

The 1938 act also provided for a program known as Section 210, which authorized insurance of a relatively small mortgage (not over $200,000) covering multifamily dwellings or not less than 10 single family dwellings. The unique character of this provision was the authority to insure advances on a mortgage covering a single family home. The Section 210 authority was little used and was repealed the following year.

Undoubtedly, there were countercyclical motives behind those multifamily provisions, as well as other provisions of the 1938 Act, but they served chiefly to extend FHA mortgage insurance to the whole scope of residential construction. The mortgage insurance operations for rental housing got underway almost immediately. However, they did not reach a volume of $100 million annually until 1947, when there was a sudden increase to $360 million for that year. In 1950 they were up to more than $1 billion for that year. The annual volume varied drastically until, in 1962, it was again up to more than $1 billion.

Liberalization of Mortgage Terms and Volume Operations: The 1938 Act also substantially liberalized terms of eligible home mortgages, both for the purpose of fighting a substantial recession and to make adequate housing available to more families. (From 1938 until the Housing Act of 1956 (Sec. 102), a higher maximum mortgage amount was authorized for new construction than for existing construction): The ratio of loan-to-value was increased from 80 percent to 90 percent for a mortgage of $5,400 or less on a new house, which was not an unrealistic figure at that time or for almost a decade later. A mortgage could be up to $8,600 if it did not exceed the sum of 90 percent of $6,000 of the appraised value and 80 percent of the value between $6,000 and $10,000.

In all such cases the dwelling had to be for occupancy by the owner, who must have paid 10 percent of the value in cash or its equivalent. The maximum term for those mortgages was increased from 20 to 25 years.

With the help of the above provisions, the total FHA insurance volume tripled by 1940 from the 1935 level, reaching an annual volume of almost $1 billion,[13] notwithstanding continued recession conditions.

During World War II years, the overall production of housing was curtailed due to the war effort requiring scarce materials and labor to be used only for priority purposes. Normally, no housing could be built except with specific Government approval. However, war housing could be built with the allocation of scarce material if so approved by the Government. The special FHA war housing programs (Sections 603 and 608), discussed later, provided mortgage insurance for private war housing on liberalized terms. As FHA administered the priorities system for private war housing in nonfarm areas, the portion of private housing built during those war years with mortgage insurance was abnormally high, reaching about 75 percent at one time, in contrast to a typical percentage of about 20–25 percent in other periods.

After World War II, FHA suspended commitments under its war housing programs and resumed operations under the regular Section 203 and Section 207 programs. The enormous postwar backlog of demand by veterans and other prospective buyers started an expansion of housing production, even without FHA assistance.

Shortly, in 1946, the Congress enacted the Veterans Emergency Housing Act of 1946, which contained an array of drastic measures to provide quick housing construction, especially for returning veterans. The Sections 603 and 608 programs were revived, with increases in mortgage limits and with use of more liberal underwriting standards.

The Housing and Rent Act of 1947 repealed most of the above 1946 Act, but enacted additional provisions including authority for FHA to finance the manufacture of prefabricated houses.

Total FHA operations expanded greatly during the above period of veterans housing construction, reaching a volume of $3,341,000,000 in mortgages and loans insured during 1948.

The Housing Act of 1948 further liberalized FHA programs for lower and moderate income families. The maximum dollar amounts on home mortgages were moderately raised, and FHA was authorized to raise the maximum loan-to-value ratio to 95 percent for certain lower cost homes. In the case of multifamily units, a mortgage could be eligible up to 90 percent of value and $8,100 per unit. In the case of nonprofit cooperative ownership housing primarily for veterans, the mortgage could be up to 95 percent of replacement cost.

During the 1950's, the annual volume of FHA insurance reached $4.3 billion. The credit represented by the mortgages covered, together with a rapid expansion of other home mortgage and consumer credit, greatly disturbed the Federal Reserve Board and other Federal offices concerned with inflation and Federal debt management. About half of the rapid expansion was due to FHA and VA mortgage insurance and guaranty.[14] In large part, that was due to the liberal mortgage insurance operations under the veteran insurance programs, the 1948 Act, and also liberal terms provided under the 1949 Wherry Act insurance program for military rental housing. Those liberal FHA operations accounted for the growth in multifamily units insured from 1,526 in 1946, to 126,729 insured in 1950.[15] Other factors that encouraged production, however, were the end of price controls, ample funds, and the purchase of mortgages by the Federal National Mortgage Association in 1949

[13] See President's Conference on Home Building and Home Ownership, supra.

[14] Ibid.

[15] Ibid.

and early 1950 on an unprecedented scale. On the demand side, housing production was encouraged by new family formations resulting from the large number of returning World War II veterans.

The general inflationary pressures which were meanwhile making themselves felt, largely because of the Korean War, led Congress to authorize the President (in the Defense Production Act of 1950) to control real estate credit, including specific authority to regulate and reduce loan amounts, loan maturities, and increases in the amount of downpayments on loans. The President gave this authority to the Housing and Home Finance Administrator with respect to Government-aided housing, and to the Federal Reserve Board with respect to new construction otherwise financed. That authority was used and the resulting increases in downpayments and reduction in long terms were effective in sharply reducing the volume of FHA operations as well as other housing starts. The controls were gradually removed by the Congress until, in 1953, they ended.

The volume of FHA operations did not increase dramatically during the 1950's, but there was a gradual increase, to an annual $6.3 billion volume by 1960.[16] The statutory changes liberalizing and expanding the mortgage insurance system during the 1950's were made principally in the new cooperative housing program described earlier, and in new special programs (discussed later) carrying liberal mortgage maximums and underwriting standards. The additional programs were enacted to assist Korean war housing in 1951, housing in urban renewal areas in 1954, housing in outlying areas in 1954, housing for displaced families and servicemen in 1954, trailer courts in 1955, military (Capehart) housing in 1955, nursing homes in 1959, and rental housing for the elderly in 1959.

Although the 1950 changes in FHA mortgage terms were made mostly in new programs, there were some significant changes made by the Housing Act of 1954 that further liberalized the regular Section 203 and 207 FHA insurance programs. They followed a recessionary condition in the general economy, and quickly stimulated FHA construction, particularly of moderate and higher priced homes. That act increased the maximum home mortgage amount to $20,000, and permitted a loan-to-value ratio as high as 95 percent on the value up to $9,000 in case of new construction. The maximum multifamily mortgage was increased to $2,000 per room, or $7,200 per unit if less than 4 rooms per unit. A per-room limit was adopted in the Housing Act of 1950 to discourage a tendency that had developed under the "per unit" limit for builders to build "efficiency" or one-bedroom units. Modest adjustments upward were permitted for elevator structures and high cost areas.

The Housing Act of 1957 further increased that maximum mortgage amount for the regular Section 203 home mortgage program so that the mortgage could cover 97 percent of the value of a new house up to $10,000, with adjustments downward on the remainder of a $20,000 valuation. A further small relaxation was made by the 1958 act "to stimulate residential construction" (Public Law 85–364). Such changes in those 1957 and 1958 acts helped increase production in the moderate price range.

During the 1960's, the most important new legislative responsibilities given to FHA were those relating to subsidy operations. However, important relaxation in FHA mortgage terms was made by the Housing Act of 1961 as one of the efforts of the Kennedy Administration to fight the recession beginning in 1960.

Under the 1961 Act, the maximum amount of an eligible home mortgage was increased to $25,000, and the portion which could be covered by a 97 percent ratio of loan to value was increased to $15,000. The maturity of the mortgage could be 35 years in the case of new construction. In addition, the special FHA program for displaced families (Section 221, discussed later) was broadened to apply to low and moderate income families generally. Thus, in a sense it was made part of the general mortgage insurance operation, rather than a program for a special group. The changes in that program permitted insurance of a mortgage up to $15,000 in a high cost area with only 3 percent downpayment, including closing costs, and with up to a 40-year term. Upward adjustments were also made for rental housing mortgages under the program.

These changes, with provisions in the 1961 Act liberalizing other special FHA programs, helped boost FHA operations to over $7 billion during 1963. They remained at more than $7 billion during the 1970's and exceeded $8.5 billion in 1965.

The Housing and Urban Development Act of 1969 increased the maximum home mortgage amount to $33,000 and made a modest increase in the mortgage ratio for higher cost homes. The mortgage maximums for the regular rental housing program were increased substantially (as

[16] Allan F. Thornton, supra.

were all FHA mortgage ceilings for rental housing). Consequently, such ceilings are now left almost entirely to administrative discretion because they are as high as $28,050 per large unit in a high cost area where elevator construction is necessary, and all ceilings may be increased by 45 percent when FHA finds cost levels so require.

The above amendments through the years show that the continuing trend of almost all FHA legislation has consisted of more and more liberalization of mortgage and other insurance terms (whether to benefit more consumers or increase credit or production). Little further liberalization is possible, so that this particular source of benefit has been almost exhausted. Incentives, if any are desired, to spur additional credit and production must come from other directions.

Extension of FHA Insurance into Blighted Areas: Of importance to the whole mortgage insurance system (but in terms other than volume) was the enactment of Section 223(e) of the National Housing Act (as part of the Housing and Urban Development Act of 1968), which gave legislative sanction to waiving or relaxing FHA property standards to permit mortgage insurance for housing in blighted areas of central cities.[17] Of at least equal importance was earlier administrative action taken in the same direction by the Federal Housing Commissioner. He forcefully directed his field officers to insure properties in blighted areas wherever possible to do so under the law. The new Section authorized mortgage insurance in an "older, declining area" where conditions prevent compliance with one or more regular eligibility requirements. The area had to be "reasonably viable" and the property "an acceptable risk," giving consideration to the needs of "families of low and moderate income in such areas." The insurance of a mortgage under this new authority was made the obligation of a "Special Risk Insurance Fund" established for a broader purpose contemplating heavier than normal losses.

The background of the above actions was a long history of only small FHA involvement in slum or blighted areas, except, of course, where areas were being rebuilt or improved through urban renewal or similar actions. The practice of excluding these areas, often referred to as "declining," had been criticized for years by certain private organizations and by many members of the Congress.

[17] The provision was substituted for an earlier one (Section 203 (1) added by Section 302 of the Demonstration Cities and Metropolitan Development Act of 1963) which waived economic soundness in riot threatened areas.

The field instructions of the Federal Housing Commissioner, together with the above provisions, made a substantial change in FHA operations in blighted areas. For the first time, many such areas in large cities were benefited by mortgage insurance, including several which had been affected by riots, such as Los Angeles and Detroit. Of course, that meant looser FHA property standards insofar as those areas were concerned. It should be mentioned, however, that the FHA instructions did not relax the credit standards applicable to a home purchaser.

This new authority and practice was not limited to FHA subsidy operations but applied to all insurance in the affected areas. This was significant from the standpoint of identifying reasons for abuses and defaults constituting some of the recent FHA "scandals" in Detroit and elsewhere, because properties subject to excessive defaults and foreclosures included much housing under nonsubsidy programs where the looser standards of the above new section were applied.

Open-End Mortgages: As one step in keeping up with innovations emerging in the private mortgage market, the Housing and Home Finance Agency recommended and the Congress enacted authority to insure "open-end mortgages." This was done as part of the Housing Act of 1954 (Section 126). An open-end mortgage is one which provides that the outstanding balance can be increased in order to advance additional loan funds to the borrower for improvements or repairs of the home covered by the mortgage without the necessity of executing a new mortgage. That avoids the expense of a new title search, recording, and other mortgage costs, while permitting the borrower to get funds for repair or improvements at the relatively low rate of interest established in the original mortgage.

Under the provision in the 1954 Act, an added insurance fee has to be prescribed in the open-end mortgage. The original principal amount of the mortgage, and the maximum amount otherwise controlled by statute, could be exceeded if improvements added an additional room or other enclosed space.

One basis for proposing this legislation was the absence of adequate incentive for extending mortgage credit to rehabilitation work. Many States had enacted laws permitting open-end mortgages, and in other States those mortgages could be valid without specific authorization. There had been little use of this type of instrument throughout the country, however, and application of mortgage insurance did not increase its use extensively. The low mortgage interest rate proved unattractive to lenders for use in connection with the small dollar amounts involved in individual repairs and improvements.

Cash Payment of Insurance Claims: The Housing and Urban Development Act of 1965 authorized FHA, at its option, to pay insurance claims (under any of its programs) in cash rather than debentures. Similar authority had been granted in 1961 with respect to certain special purpose programs. Payments in cash constitute an added advantage to lenders that helps encourage housing credit.

The authority to pay claims in cash was not intended to undermine the basic concept of debenture payments previously discussed. The Committee on Banking and Currency stressed in its reports on the 1965 bill that the authority to issue debentures instead of cash was not repealed, and that FHA could use that authority if it determined that discontinuance of cash payments would be desirable.

Also, an important question presented to FHA is whether it elects to agree in its insurance contract to pay claims in cash, or retain in the contract the option to pay in cash or debentures as the circumstances warrant at the time of payment. At present, the FHA retains the option in its programs to choose the method of payment at the time of payment.

Present Posture of the Basic Mortgage Insurance System

Because such a large portion (some 23 percent) of all FHA mortgage insurance is being written under programs involving subsidies, it is difficult properly to appraise the current posture of the basic mortgage insurance system in the terms of volume operations. Because of the effect of outstanding commitments under the FHA subsidy programs, the production incentive impact is enormous, and clearly the overall FHA operations remain higher ($14.8 billion and 830,500 units insured in fiscal year 1972) than they would without subsidies. The 1971 volume was $15 billion, higher than any previous year, and equal to nearly 10 percent of all cumulative FHA business since 1934. On the other hand, a substantial but unknown volume of additional units would have been built under the nonsubsidy program if the subsidy operations had not existed.

The overall mortgage insurance programs are being used for a large portion (over 1.6 million units in 1972) of all housing construction and home sales throughout the country. Of the 2.1 million housing starts in the country last year (excluding almost 600,000 mobile home shipments), about one-fourth of these were assisted with FHA mortgage insurance. FHA-insured repair and rehabilitation loans also remain high—about $900 million last year.

It must be noted that the very recent trend of FHA operations is down, but because of factors which, viewed historically, can be regarded as quite temporary. It is reported that FHA mortgage insurance applications in the first quarter of 1973 amounted to 139,790, which is down from 293,909 in the same period of 1972.[18] Of course, the current suspension of the FHA subsidy programs abnormally affects the overall volume of applications. Also, due to the shortage of mortgage funds during the last few months, housing starts in the whole market have fallen substantially.[19]

Although the recent FHA "scandals" are generally associated with the FHA subsidy operators, they have brought the whole mortgage insurance system under critical review for various reasons and purposes. First, the regular insurance programs are properly subject to review and criticism insofar as they were directly involved in the scandals. As previously indicated, the lowering of property standards was a major factor in mortgage defaults and foreclosures of housing in blighted areas financed with mortgage insurance under the regular programs with the looser authority permitted in 1968. Similarly, the bad management or personnel practices applied to housing under the regular programs, as well as to subsidy operations. Although that obviously points to the need for corrections throughout the system, it does not logically discredit the merits of the FHA insurance system itself. If the system were responsible in any way for the current type of evils, the fact would have emerged years ago.

Questioning of the more fundamental aspects of the system has come largely from private groups, particularly certain segments of the lending industry, which challenge the need for any FHA in view of the broadened scope of home lending by savings and loan associations and the rising volume of business being done by private mortgage insurance companies—matters with no direct relation to the recent scandals. Possibly some of the force of that attack has waned, but the issue remains. There has always been a small group which has opposed the use of FHA mortgage insurance for any "social pur-

[18] *Wall Street Journal* (May 14, 1973) citing FHA as source.

[19] *Time Magazine* for June 11, 1973, p. 79, reports housing starts have fallen from an annual rate of 2.5 million in January of this year to 2.1 million in April.

pose," such as those initiated after 1950, and which believes that mortgage insurance will continue to be corrupted if linked with other Government operations.

Those who suggest private mortgage insurance companies or other existing institutional types as a substitute for the basic FHA system overlook primarily two of its features: (1) its many consumer benefits of importance to the Congress and the general home buying public, discussed elsewhere; and (2) the value of the Government financial backing represented by the insurance, together with its debenture feature, which makes it possible to have an insurance obligation that will withstand any depression, and with the least potential loss to the Government.

Accomplishments of the FHA

Reform of Residential Financing: With the leverage of the mortgage insurance obligation, the FHA greatly benefited the entire field of housing and home finance. That was a major factor in generating mortgage credit on an adequate, permanent basis. The scope of this encompassed mortgage financing techniques, and practices by lenders, builders, architects, and producers of building materials, and affected State mortgage laws and building codes.

The most important contribution of FHA to home financing was the assistance it gave to the general acceptance and use of its uniform long term, low downpayment, amortized mortgage, which had been pioneered some time earlier by the HOLC for its special purposes. With a standardized mortgage instrument that all States recognize, and on which banks and other institutions can lend, mortgage funds can now move freely across the country to where they are needed. This one feature of the system materially affects the volume of credit for housing, as large-scale nationwide investors, such as insurance companies, have become regular purchasers or direct investors in FHA mortgages.

The soundness of the FHA mortgage loan with its low downpayment and amortization, and without a second mortgage, made the investment more attractive.

The FHA system helped change the whole investment approach of lenders toward residential mortgages. Under the greater financial risks previously existing, lenders had to contemplate and allow for substantial costs resulting from foreclosures. Under the FHA system, they could look to sounder loans and the Government insurance backup.

Volume of Production and Credit: Throughout its history, FHA has helped generate credit for mortgages and loans under its insurance programs totaling 164 billion dollars, which can be compared with a 1934 total national investment in home mortgages of $18 billion.[20] This FHA total includes over 11 million home mortgages totaling over $119 billion. About 40 percent of FHA home mortgages, or about 4.4 million, are on new construction. The total amount of FHA-insured mortgages includes of $23 billion, for 1.8 million units, under project mortgage programs. About 20 percent of all nonfarm starts in home construction have been under FHA home mortgage insurance programs.

The volume of FHA operations has meant that over 11 million families have been assisted in purchasing or building homes with the favorable financing terms and consumer protections of FHA insurance. The successive occupants of an additional 1.7 million units receive the benefits of adequate accommodations and at reasonable rentals made possible by favorable FHA financial assistance.

It is difficult to determine, at any given time, the volume of production that results solely from mortgage insurance. One study of the increasing residential construction during the post-World War II years estimated a stimulus of 375,000 to 500,000 additional units a year, or about $4 to $5.5 billion.[21]

As previously indicated, FHA programs have been successfully changed at times to increase credit which was needed to spur construction during recession as an aid to the housing industry and the general economy.

Channeling Housing Funds to Lower Income Families and Other Special Needs: From almost the beginning of FHA mortgage insurance, inducements in the form of special mortgage terms were designed to help channel funds to housing within the reach of lower income families who would not otherwise be able to purchase homes. For them, FHA insured a mortgage with a lower downpayment and a correspondingly higher risk than for higher income families borrowing with larger mortgages. Also, the fact that under the FHA insurance system the downpayments are generally lower than under other financing tends to channel credit to lower income families. These features of FHA mortgages have influenced other financing and have been followed to a large extent in non-FHA financing by institutions such as savings and loan associations.

[20] Allan F. Thornton, supra.

[21] *The Economic Impact of Federal Loan Insurance* (Washington: National Housing Association, 1961, p. 62).

The mortgage insurance programs for special groups (such as elderly, veterans, defense workers and servicemen, displaced families, and cooperatives) have carried special inducements to channel credit to them. In all cases, a controlling factor has been the low or moderate income character of these consumer groups as a whole.

Pioneering Consumer Benefits: The FHA has taken the lead in providing the additional consumer benefits discussed earlier. Some of these have had a substantial effect throughout the housing and home financing industries. Thus, maximum property requirements have set a norm for all housing. They have tended to standardize home equipment and materials and have enabled building codes and other requirements to be more nearly uniform.

Homeownership: Homeownership has been a guiding principle of FHA since its inception. The increased availability of home financing credit under its programs has helped increase not only the volume of individual homes, but the ratio of ownership to rental. In 1930, only 46 percent of families owned their own homes. The 1970 census indicated that this had increased to about 63 percent.

Establishment of Mortgage Banking Industry and Large-Scale Builders: Prior to 1934, mortgage bankers handled only an insignificant amount of business. The mortgage bankers now service FHA mortgages amounting to over $50 billion, as estimated by the Mortgage Bankers Association. Their function of channeling the flow of funds from national investors to builders and home purchasers was made practical by the FHA insurance protection of large-scale mortgage investments throughout the country, regardless of State variations in foreclosure procedures and expenses and other applicable State requirements. Concurrently with the development of the mortgage banking industry and its national credit services, many large-scale builders of homes came into existence throughout the country. Only a very few existed before 1934. Because of mortgage insurance, funds from large national investors became available on liberal credit terms. These large-scale builders were encouraged by the resulting prospect of sustained, stable production essential to their operations.

Consumer Credit for Repair and Rehabilitation: The insurance of institutions against losses on borrowing for repair and rehabilitation was the first FHA program to start operating, and is still continuing on a large scale. Over 30 million such loans have been made, amounting to more than $20 billion. This form of short term financing operates on a discounted loan proceeds basis, which results in a higher finance charge to the borrower than the interest charge on an insured mortgage. Yet it is a practical procedure for lenders and repair contractors everywhere, and affords the borrower a discount rate substantially lower than he would pay on relatively small unsecured loans without FHA insurance.

The only serious failure in this program occurred in the year 1953, and shortly before, when scandalous abuses occurred that constituted a part of the "FHA scandal" that year. Hundreds of homeowners throughout the country had been defrauded by promoters (called "suede shoe boys") of repair and rehabilitation jobs who took advantage of loose lending practices that FHA had not adequately controlled. It was also the year of greatest operations under the program. Therefore, the Housing Act of 1954 imposed new drastic safeguards, including a 10-percent coinsurance requirement on each loan (in addition to the previous 10 percent maximum on the portion of the institution's loans that could be insured). There were predictions that this would kill the program, but it continued at almost the same rate as the average of years immediately preceding that change.

It may be noted that experience during the priorities and credit control days following World War II made clear that any serious curtailment of this program will produce an enormous reaction from the thousands of suppliers and contractors who use it.

What FHA Mortgage Insurance Has Not Accomplished

Although the mortgage insurance system was adapted, through legislation and sometimes through administrative action, to meet emerging social problems, new forms of ownership, and new industry techniques, it failed in other respects to meet major problems in the housing field. Often, that was because the problems were beyond the scope of mortgage insurance rather than because of any weakness or failure in the mortgage insurance system itself.

Major failures were:

Neglect of Small Cities, Towns, and Rural Areas: Of course, nothing in the legislation—explicit congressional intent or regulations—restricts mortgage insurance to large cities. (There was even an early amendment, Section 110 of the Housing Act of 1954, which is still in effect, that attempted unsuccessfully to extend FHA insurance to a farm dwelling.) In practice, the FHA programs have operated largely in big cities and their suburbs, to the neglect of small towns, and rural areas. Several reasons can be given: (1) the failure of small town banks to learn and participate in the rather complex FHA procedures and requirements, (2) an FHA conservative view of the housing market in a small town or a one-industry small city, (3) a lack of interest by the FHA field office because of the remoteness of a small city or town in relation to the volume of housing involved, considering difficulties of inspections, etc., and (4) concentration during the 1960's on the emerging urban problems of the very large metropolitan areas. Some special purpose housing, such as housing for the elderly, has moved substantially into small communities.

Notwithstanding the real obstacles to providing FHA assistance in small places, those obstacles are not unsurmountable, as the Veterans Administration and the Farmers Home Administration have proven, using different legislative and other techniques, discussed later in this paper.

Incoherent Suburban Development: Perhaps FHA is most frequently criticized by professionals for producing "urban sprawl." That is valid to the extent that most FHA insurance on new construction has been on housing in the suburbs that was developed in an incoherent manner from the standpoint of overall community planning and the needs of all income groups. Often, recreational facilities have been inadequate or nonexistent. The usual criticism runs to the dreary scenic appearance and sameness of the housing.

In fairness, it is difficult to say that FHA caused this type of construction, because it frequently occurred in areas where building was done without FHA insurance. It does represent a lack of initiative by Federal and local officials to take whatever steps are required to compensate for the failure of local planning and other controls.

Failure to Produce Housing in Volume Through Mortgage Insurance for Rehabilitation: No greater effort has been put forth unsuccessfully by HUD and its predecessors than in their consistent and vigorous (but unrewarding) attempts to produce a large volume of adequate housing through mortgage insurance for rehabilitation. Successes have occurred on a small scale with very limited special legislative (such as Section 221(h) and the similar section 235(j) beginning in 1968) and administrative actions, but general legislative authority has not been effective.

Outstanding in this regard were the rehabilitation measures in the Housing Act of 1961 which had been proposed and heralded as one of the main features of that landmark legislation (Section 303(k) and Section 220(h) of the National Housing Act). They produced almost nothing. Apparently, very favorable financing terms are inadequate incentives for overcoming the basic obstacles inherent in rehabilitation jobs.

Lack of Minority Housing in Suburbs: It is obvious that, notwithstanding the application and substantial enforcement of equal opportunity requirements to housing occupancy and financing, the needs of minority families for housing in the suburbs are not being met in a meaningful way. Apparently, nothing FHA does causes this result, but the present mortgage insurance system, together with other Federal and local controls, are failing to meet these needs.

Decline of Central Cities: This is closely related to the above-mentioned failures with respect to suburban development and the needs of minority families. Generally, the FHA has produced housing in the suburbs that is unavailable to blacks and the poor and has facilitated the movement of whites with moderate or higher incomes to the suburbs. This has helped accelerate the decline of central cities. At the same time, the present FHA mortgage insurance system is inadequate for substantially meeting the problems of blight and deterioration in cental cities. In fact, FHA is being criticized for going too far administratively in liberalizing its programs in attempts to bring mortgage insurance to some areas which continue to deteriorate. Indeed, it has been one of the prime financial losers as a result of its unsuccessful efforts to operate in older blighted areas.

Generating and Stabilizing Housing Credit through the Secondary Market

To understand the role the Federal Government has come to play in the secondary market for housing mortgages, it is essential to bear in mind what the "secondary market" is, and what it does. In essence, the function is rather simple, although in practice it develops manifold complications.

Primary lenders of mortgage funds—those who originate mortgage loans—are necessarily limited in the scope of their operations by the funds they have available to lend. This inherent limitation, however, affects different kinds of lending institutions in different ways.

Savings and loan associations make mortgage loans primarily as investments, with the object of holding them to maturity. Their program of new lending, accordingly, is tailored to fit their sources of funds, which are principally amortization, prepayments, and interest on the loan portfolio, plus the net inflow of new savings. To meet temporary peaks of demand for funds, they can secure advances from the regional Federal Home Loan Bank on the security of loans in their portfolios.

Other types of mortgage lenders, however—such as mortgage banking institutions—do not accumulate savings directly, and normally do not originate mortgages to retain in their own investment portfolios. Rather, they make mortgage loans with the intention of disposing of them to other investors who want long term investments but are not themselves directly active in the housing market; such investors include banks, insurance companies, certain trust and retirement funds, etc. These "secondary" lenders buy mortgages from the primary lenders, thus restoring funds available for the making of new loans. Typically, the mortgage banker retains the loan for servicing on a fee basis for the secondary purchaser, since the latter normally does not engage in that sort of local real estate management.

When lenders of the latter type find their liquid assets fully disbursed or committed to current loans, they must perforce suspend new lending operations until a new supply of lendable cash is found. This, in simple terms, is the function of the secondary market. While such lenders as savings and loan associations are less dependent on the secondary market, they can and often do have recourse to it. The activity of the total residential mortgage market, therefore, is profoundly affected and even limited by the availability of this supply of backup credit.

There is a considerable history behind the Federal Government's recognition of, and its involvement in, the secondary market for residential mortgages.

The Federal National Mortgage Association recently observed:

> The secondary mortgage market is not a highly organized market in the sense that markets for stocks, bonds and agricultural products are organized. It has no common gathering place where buyers and sellers may meet to complete their transactions. It is an ill defined and poorly understood phase of the complex financial structure which comprises the market for residential housing mortgages. But while it is a nebulous sort of arrangement, the secondary mortgage market is very meaningful in a special sense to each of its participants.[22]

The above comments are true even today. But it is important to bear in mind that when the Federal Government first addressed itself to the problems of reviving and restructuring the home financing system of the country as a major part of the recovery effort, the secondary market for home mortgages, to all intents and purposes, did not exist. Even those relatively few mortgage lenders who relied partly on discounting mortgages (selling them at less than their remaining unpaid amount) to other sources of capital were in such dire straits that their portfolios were not salable at any price.

First Step: National Mortgage Associations (1934)

In early 1934, the President proposed a new, broad attack on the problems of the floundering housing economy.[23] The legislation proposed was to have four main thrusts.

- Initiation of an aggressive program of modernization and repair of existing structures of all kinds, but especially homes.
- Establishment of a system of "mutual" mortgage insurance.
- Establishment of a system of privately owned national mortgage associations.
- Establishment of a corporation to insure accounts in savings and loan associations and similar institutions.[24]

It appears to be generally supposed that this original proposal for the establishment of a new type of private mortgage association under Federal charter and regulation was primarily intended to provide liquidity for, and promote market acceptance of, the proposed new 80 percent, 20-year insured mortgage contemplated by the draft bill.[25] Examination of the contemporary record does not support this interpretation.

The authors of the new proposals were confronted with the fact that there were idle savings in large volume in the hands of "building and loan associations," banks, and insurance companies, while at the same time there was heavy unemployment in the construction industry

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[22] *Background and History—1970*, Federal National Mortgage Association, p. 5.
[23] Message of the President, May 14, 1934.
[24] Release of the National Emergency Council, May 14, 1934, pp. 3 et seq.
[25] See, for example, discussion in *Background and History—1970*, supra, p. 4.

as a whole, and most of all in the residential construction component of that industry. Yet funds for repairs and new construction were unavailable, despite the great need for such construction, because investors had come to view mortgages as virtually synonymous with financial disaster. At the same time, there was widespread geographical maldistribution of accumulated capital. The problem appeared to be to break through the barriers between the pools of available funds and the purposes for which they were urgently needed.[26]

In this context, the proposal to establish a novel form of national mortgage association was described as ". . . another important means of reopening the mortgage market . . . ," and of encouraging the flow of capital from areas of surplus to those in short supply.[27]

This part of the President's four-part approach was strenuously attacked by the United States Savings and Loan League in the hearings which followed.[28] Their main objections were the following:

1. That tax exemption for private, profitmaking institutions was a new and unwise precedent, and an unfair competitive advantage for these special federally sponsored businesses.

2. That they were not confined under the bill to investment in insured mortgages, but could—and presumably would—both make loans and purchase them on any sort of mortgage security. (On this point, Mr. Bodfish appears to have been technically correct. The sponsors of the bill had described the new associations as being "confined" to investment in insured mortgages (see sources cited, supra), and the President in his Message had said they would be "almost entirely" limited to such investment. However, the language of the draft bill did not, in fact, so restrict them.)

3. That they would compete directly with established mortgage lending institutions, thus weakening them rather than broadening the market.

4. That by reason of the requirement of $5 million paid-in capital in cash for the organization of a national mortgage association, they would as a practical matter be limited to a few large financial centers.

5. That because of the competition between existing savings institutions and the new mortgage associations, the assignment of regulatory and supervisory duties with regard to them to the Federal Home Loan Bank Board carried an unavoidable conflict of interest threat to the Board itself.

These major criticisms are detailed here not so much to consider their merits as to note that they all deal with the general operations of the market—not with a specific concern about providing a market for the new insured mortgage instrument, or encouraging its acceptance (although this subject was also discussed somewhat in the hearings).

That the Congress was responsive to these and other criticisms is indicated by the changes it made in the final bill agreed to. These included, among others:

1. The exemption from Federal income taxes was eliminated.

2. The authority to "lend" was dropped in favor of language permitting national mortgage associations to "buy and sell" mortgages. While they were not prohibited from purchasing uninsured mortgages otherwise eligible, language was inserted which prevented them from including any such mortgages held by them in the asset base from which their borrowing power in the private market was to be computed.

3. Authority to charter and regulate national mortgage associations was shifted from the Board to the new Federal Housing Administrator, who was to carry out the modernization loan and mortgage insurance provisions of the act.

Perhaps because of these changes, and perhaps for other reasons, the experiment embodied in title III of the National Housing Act was a failure. Although the capitalization requirements were later reduced and the borrowing restrictions relaxed, no private national mortgage associations were ever chartered under the new authority. Nevertheless, it is of historical interest and importance to note that as long ago as 1934, and contemporaneously with the establishment of the insured mortgage system, the Federal Government recognized the need for, and undertook (albeit unsuccessfully) to bring about, basic reforms and structural changes in the mechanisms governing the generation of housing credit and its movement through the market.

[26] See discussion in National Emergency Council Release, supra.
[27] Ibid.
[28] See Testimony of Morton Bodfish, hearings before the House on H.R. 9620, pp. 293 et seq.

Intermediate Stages

The RFC Mortgage Company: It would appear that Congress perceived fairly rapidly that the national mortgage association device was something short of a solution for the problems of "reopening the mortgage market," for in the following year it gave new powers to the RFC ". . . to assist in the re-establishment of a normal mortgage market." [29] Under this authority, the RFC Mortgage Company was organized, originally to invest in a wide range of mortgages, both residential and commercial, where funds were not available from private sources at reasonable rates.

Before the end of the year, however, the RFC Mortgage Company had begun to purchase FHA-insured mortgages on already-existing properties, and this activity continued through the life of the Corporation. A decade later, when the VA guarantee program was launched to aid in housing veterans and this new form of Government-backed mortgage was experiencing market growing pains, the Corporation was authorized to purchase VA-guaranteed loans as well.[30] In all, the Corporation during its active period purchased more than $250 million in FHA-insured mortgages and $140 million in VA-guaranteed mortgages.

The Corporation was dissolved pursuant to Act of Congress in 1948.[31]

Initial Organization of the Federal National Mortgage Association: In 1938, in an apparent effort both to breathe life into the national mortgage association idea and to expand Federal support for the mortgage market, a further initiative was undertaken. Congress amended title III of the National Housing Act so as to preserve (and even liberalize) the arrangements for organizing and chartering private national mortgage associations, but at the same recognized that such an association might be set up and operated by a Federal agency.[32] Thereupon, on application of RFC, the Federal Housing Administrator chartered the Federal National Mortgage Association (FNMA) (first, but only very briefly, titled the National Mortgage Association of Washington).

For the next several years, both FNMA and the RFC Mortgage Company were active in providing a secondary market for FHA-insured mortgages—FNMA purchasing FHA-insured mortgages on new residential properties constructed after a base date and insured after construction, and RFCMC on VA-guaranteed mortgages, older FHA mortgages, and certain other types not eligible for purchase by FNMA. The characteristics of and distinctions between mortgages eligible for purchase, respectively, by FNMA and RFCMC are too numerous and technical to be of relevant interest here. In any case, both corporations were entities of, and operated by, RFC.

For its first 5 years, FNMA had an active and fairly level role in the market, purchasing mortgages at a rate of about $50 million per year. Then followed 5 years of rapidly declining activity, the result of the defense and war emergencies and their impact on the economy.

During these years, residential construction (like other construction) was sharply restricted, except for that related to the defense effort, which was encouraged through a variety of devices. Basic building materials and skilled labor were subject to a system of priorities and allocations, and thus were available mainly for defense-related building. For the limited volume of residential construction permissible, mortgage funds were relatively abundant. In short, there was little function for a secondary market facility to perform, and its new purchases declined sharply, reaching a level of less than $100,000 in the fiscal year 1947. At the same time, market conditions favored sales of mortgages out of the portfolio (as well as amortization and prepayments), so that by the end of that year FNMA's outstanding portfolio balance had dropped to just under $5 million, or about 2 percent of what it had been 5 years earlier.

FNMA Takes Hold (1948–54)

In 1948, 14 years after the first unsuccessful Federal venture into the secondary market, a series of major developments occurred in rather quick succession that profoundly changed the whole picture, including the Federal role in it.

Pursuant to the RFC Extension Act of the previous year,[33] the RFC Mortgage Corporation was dissolved, and its assets transferred to RFC for liquidation. (Six years later, the residue of this portfolio was transferred to FNMA for management and liquidation by Reorganization Plan #2 of 1954.)

Shortly thereafter, in 1948, Congress enacted legislation which completely rewrote Title III of the National Housing Act.[34] For present

[29] Public Law 1, 74th Congress.
[30] Public Law 656, 79th Congress.
[31] Public Law 132, 80th Congress.
[32] Public Law 424, 75th Congress.

[33] Public Law 132, 80th Congress.
[34] Public Law 864, 80th Congress.

purposes the most significant changes were three:

1. The new law authorized the establishment (by name) of a Federal National Mortgage Association, and further declared that the already established FNMA was that Association.

2. The authority to provide secondary market support for VA-guaranteed mortgages, which had lapsed with the termination of the RFCMC, was extended to the newly ratified FNMA.

3. By dropping all the relevant provisions of the old title, the new law eliminated all reference to the organization and chartering of private national mortgage associations.

Thus FNMA finally and formally was recognized as the Federal Government's instrumentality for channeling credit (still either Federal or federally backed) into the secondary market for residential mortgages. Concurrently, three major forces were combining and interacting to enlarge greatly its role and impact in the housing economy:

- First, the war housing crisis was giving way, with hardly any gap between, to the postwar housing crisis brought on by returning veterans and the enormous increases in family formation and resulting housing needs that would be experienced for the next several years.

- Second, the rising housing demand and the relaxation of inhibitions on construction generally increased the demand for mortgage funds, which became generally tighter and began to rise in price.

- Third, the use of FNMA advance commitments as a leverage tool in FHA-insured residential construction became general, and the homebuilding and financing industries developed their own special accommodations to this mode of doing business.

Because of the importance of the last point, a word of explanation of the "advance commitment" procedure may be in order. Under this system (in the particular form in which it became most potent), FNMA would issue to a builder, even before a contemplated home or multifamily project had been built (or even started), a commitment to purchase the mortgage at a fixed price from an eligible mortgagee, upon completion and insurance of the mortgage by FHA. (Obviously, in order to work, this system required that the builder also have a conditional commitment from FHA.) Armed with this assurance, a builder could readily obtain construction financing (in many cases itself insured) on the basis of a commitment from an approved lender to make the mortgage loan. The latter commitment, in turn, was readily obtainable from a mortgagee because it was made on the basis of FNMA's promise to buy the mortgage upon execution and insurance.

Commonly, if not typically, the permanent mortgage was executed, endorsed for insurance, and conveyed to FNMA in a single closing meeting. Thus the private lender was only a nominal mortgagee, since he generally disposed of the mortgage at a previously determined price the same day he originated it. The lender's only actual financial participation was the provision in some cases of construction financing, and this was on the assurance of an immediate FNMA takeout on execution of the mortgage—and often, as noted above, the construction advances were also FHA-insured.

Under the combined impact of these stimulating forces, FNMA activity—almost nonexistent in 1947—accelerated at a striking rate, rising to nearly \$50 million in the fiscal year 1948; over \$400 million in 1949; and nearly \$1 billion in 1950. (Naturally, this volume required a corresponding increase in the Association's financing, with the result that its borrowing authority grew in successive steps from \$220 million at the time of its establishment in 1938 (Public Law 424, 75th Congress) to \$2.75 billion by 1950 (Public Law 475, 81st Congress).) Thus FNMA became a major factor in the generation and flow of housing credit, although its contribution was still essentially Federal credit, and the operation was described by its critics as a disguised form of direct Federal lending.

By 1950, the Congress became concerned at the enormous expansion and seemingly runaway character of FNMA secondary market activity, notwithstanding that it was generally recognized that this activity had contributed to the production of a significant volume of needed housing. It applied the brakes by providing that thereafter the Association was authorized to purchase "only those eligible mortgages which are guaranteed or insured at the time of the contract"—thus effectively eliminating the whole advance commitment machinery which had come into such widespread use. (Public Law 475, 81st Congress. The same concern played a considerable part in the decision to transfer FNMA from RFC to the Housing and Home Finance Agency, where it was hoped that its policies and operations could be more closely coordinated with those of related housing programs (Reorganization Plan of the President No. 22 of 1950).) Thereafter, FNMA activity dropped back to more moderate levels, although these were still very high compared to anything experienced in the early years.

The Charter Act—1954

In 1953, President Eisenhower appointed an Advisory Committee to review and evaluate the Federal Government's housing policies and programs.[35] That Committee recommended, among a great many other things, basic reforms in the secondary market structure, both as to the role of the Federal Government and that of the private financial community.[36] A basic element of the Committee's approach was the effort to design a secondary market facility which would derive capital from participating lending institutions and would finance itself in the private capital markets, rather than relying upon the Treasury.

The President's subsequent recommendations to the Congress [37] differed in important respects from the Advisory Committee's specific proposals, but they embodied this general concept much as the Committee had suggested. The Housing Act of 1954 [38] adhered closely to both the objectives and structures envisioned in the President's message.

Title II of the 1954 act was enacted with the short title of The Federal National Mortgage Association Charter Act. It provided for three separate and distinct types of operation, categorized as follows:

Secondary Market Operations: Under this category, the Association was to provide "a degree of liquidity" for mortgage investment, and thereby help improve the distribution and availability of mortgage funds by purchasing mortgages insured by FHA or guaranteed by VA after the enactment of the new law. These mortgages were required to be of such types and quality as generally to meet the investment standards of the private market.

The secondary market operations were to be capitalized by capital stock to be subscribed by the Treasury, and nonvoting common stock required to be purchased by lending institutions in proportion to their sales of mortgages to the Association. After such initial purchase by the seller, the common stock was to be freely traded in the market. For operating purposes, the Association was to finance itself in the private capital markets through the sale of obligations which explicitly were not in the public debt or guaranteed by the United States. Although the Association itself and its operations were exempted from Federal income taxes, the secondary market operations were required to make annual payments to the Treasury in amounts equivalent to the tax that a private corporation would have had to pay on the same operations.

The act also contained provisions which specifically contemplated that at some future time ("As promptly as practicable after all of the preferred stock of the Association held by the Secretary of the Treasury has been retired . . . etc." Section 303(g)) legislation would be proposed to the end that these secondary market operations would be transferred to the common stockholders and thereafter "be carried out by a privately owned and privately financed corporation."

Special Assistance Functions: In this category, Congress recognized that special types of insured or guaranteed mortgages authorized from time to time in furtherance of a particular public purpose (such as those designed to assist in financing military housing, or cooperative housing projects, for example) often experienced market resistance until they had stood the test of experience and had overcome the problem of the investor's unfamiliarity with them. Accordingly, it authorized the Association to purchase ". . . selected types of home mortgages (pending the establishment of their marketability)" when, and to the extent that, the President determined that such purchases were in the public interest.

In addition to such special-purpose support, special assistance was authorized for ". . . home mortgages generally as a means of retarding or stopping a decline in mortgage lending and home building activities which threatens materially the stability of a high level national economy," subject to the same Presidential control.

The special assistance functions were to be financed with funds borrowed from the Treasury, and all "benefits and burdens" of these operations were declared to inure solely to the Treasury.

[35] Executive Order 10486, Sept. 12, 1953.
[36] *Report* of the President's Advisory Committee on Government Housing Policies and Programs, December 1953 (pp. 11-13 and Appendix 4).
[37] Message from the President, Jan. 25, 1954, (H. Doc. 306, 83rd Congress, 2nd Session).
[38] Public Law 560, 83rd Congress.

Management and Liquidating Functions: Under this category, the Association was to segregate all its assets and liabilities acquired prior to the enactment of the Charter Act and pursue their orderly liquidation. These activities were initially to be financed entirely by the Treasury, but the Association was directed to substitute private financing on a nonguaranteed basis as rapidly as might be feasible and to repay the Treasury indebtedness.

With respect to each of these three major categories, the Association was directed to establish and maintain separate accountability, so that in effect FNMA became a holding company managing three separate corporate subsidiaries.

Partition of FNMA—1968

It would be beyond the scope of this review to track in detail the variations in secondary market activity, and their causes, from 1954 to 1968. Throughout this period, the Government's role in the secondary market conformed to the conceptual pattern established in the Charter Act.

It is sufficient to note here that both the secondary market functions and the special assistance functions took hold and performed much as had been envisioned in that legislation. Not surprisingly, the special assistance device responded to what might be called the general law of proliferation, and, by 1968, 15 distinct special assistance "programs," or subprograms, had been formally authorized—11 by the President, and four by the Congress by special legislation.

In response to changing policy considerations and varying market conditions, total FNMA participation in the market varied considerably during the period, although the overall trend was unmistakably up. In 1968, the year in which the next major transformation of the Government posture toward the secondary market occurred, total mortgage purchases reached a new high of almost $3.5 billion. Even the 2 years of lowest activity during the period (fiscal years 1956 and 1964) were at a volume—$315 million—that might well in earlier years have been considered a "sustained high level," and certainly were large enough to constitute a significant factor in the total residential credit picture.

In 1968, the Administration concluded and Congress agreed that the time had come to move forward with the conversion of the secondary market functions from a mixed-ownership Federal corporate activity into a privately owned and financed corporation, without waiting for the retirement of the Treasury-held stock, as had been contemplated by the Charter Act. This decision appears to have stemmed mainly from budgetary considerations, although it was also believed that the secondary market function would flourish better in an environment more intimately related to the private market. The Housing and Urban Development Act of 1968 [39] partitioned the FNMA as it then existed, changing it into two new corporations:

1. A federally chartered private corporation which, after a brief transition period, was to be privately owned, operated, and financed. This corporation was also to be known as the Federal National Mortgage Association.

2. A new, wholly owned Federal corporation to be known as the Government National Mortgage Association, which was to assume the functions of the former FNMA with respect to special assistance and the management and liquidating operations.

It is unnecessary here to review the details of the capitalization and financing of the new FNMA. It is sufficient to note that in due course all Treasury-held preferred stock was retired; the undistributed earnings and earned surplus of the predecessor corporation were distributed; and the new FNMA passed into the full ownership of its common stockholders. The act extended voting privileges to the common stock, which theretofore had been nonvoting.

Expanding the Federal Role in the Secondary Market

Partition itself did not materially alter the nature of the secondary mortgage market function in which the Federal Government was then engaged. It merely retained in Federal ownership and management those functions that were deemed to be peculiarly governmental in nature (the support of mortgages enjoying only a limited market, but directed to the achievement of specific public purposes, plus the orderly liquidation of mortgages acquired in earlier programs) while permitting the general secondary market functions to continue in private ownership and under the rubric of private enterprise.

In the 1968 Act itself, however, and again in the Emergency Home Finance Act of 1970,[40] the

[39] Cited supra.
[40] Public Law 91-351.

Congress ventured yet deeper into experimentation with the Federal role in the residential secondary market.

Mortgage-Backed Securities

The Housing and Urban Development Act of 1968 authorized the new GNMA to guarantee a new type of obligation to be insured in the capital markets by private lending institutions. These were to be in the nature of bonds or investment certificates secured by a pledge of pools of mortgages insured or guaranteed by FHA, VA, or the Farmers Home Administration. Such a guarantee was authorized to be extended to "any . . . issuer approved for the purposes of this subsection" by GNMA. Most significantly, the full faith and credit of the United States was attached to the GNMA guarantee of such mortgage-backed obligations.

The appeal of the Government guarantee was quickly demonstrated by the reception of these securities in the market, notwithstanding their novel character. By May 31, 1973 (less than 3 years later), more than $7 billion in mortgage-backed securities had been guaranteed and issued. This refers only to investment or trust-type certificates (the so-called "pass-through" securities), in which amortization on the underlying mortgages and interest is paid monthly to the certificate holder in accordance with a predetermined payment schedule. Also outstanding were approximately $2 billion in bond-type securities, which are issued in much larger denominations and provide serial maturities and semiannual payments of principal and interest. All of these securities were issued by either FNMA or FHLMC, and are not treated here on the theory that they are essentially merely financing tools for these corporations.

It should be recognized that in considerable part these investments are nonadditive in terms of the total supply of residential mortgage credit —that is, they are held by investors who in all probability would have put roughly similar amounts into mortgage investment in any case through some other channel, if the new securities had not been available. Such investors (who hold mortgage-backed securities in considerable volume) include savings and loan associations, savings banks, mortgage banks, and insurance companies. As of May 31, 1973, at least 75 percent of the outstanding securities were held by such investors.[41]

On the basis of available data, however, it can be estimated conservatively that something like 20 percent, or perhaps a little more, represents funds from investors who normally and previously had avoided the mortgage market because they are not equipped to service (or supervise the servicing of) mortgages, and because they do not like to be dependent on obligations secured by real estate, with the attendant potential problems not only of servicing but of the complications involved in possible natural disaster or in default, foreclosure, or even change of ownership. Investors in this category include retirement funds, trust funds, credit unions, and individuals. Individual investment for speculative gain in temporary ownership of residential property or in short term second mortgages is commonplace; however, investment by individuals in long term first mortgages is, relatively speaking, a rarity.

It can reasonably be concluded, therefore, that the new mortgage-backed securities have been instrumental during this relatively brief period in channeling something on the order of $1.5 billion from quite new sources of capital into housing mortgages—a volume quite sufficient to establish them as a significant factor in the secondary market for residential mortgages.

A Secondary Market—or Markets—for Conventional Mortgages

In the summer of 1970, the Congress detected (not for the first time) what it perceived as a "housing crisis," pointing to falling rates of housing production, acute housing needs, and high and rising mortgage interest rates in the context of an economy exhibiting both recessionary signs and price inflation. To attack these problems, it enacted the Emergency Home Finance Act of 1970, which was described as intended not only to provide an immediate stimulus to home construction but also to ". . . [create] . . . new secondary market facilities to broaden the availability of mortgage credit." [42]

To that end, the act authorized FNMA to purchase, hold, and sell "conventional" mortgages (defined as mortgages not federally insured or guaranteed, as previously required), subject to certain prescribed limitations as to maximum amount, percentage of value, etc.

However, the 1970 act did not stop with this broadening of the FNMA secondary market function. In addition, it created a wholly new Federal

[41] Source: Office of the Secretary Treasurer, GNMA.

[42] S. Rept. 91-761, Apr. 7, 1970.

corporation, to be known as the Federal Home Loan Mortgage Corporation, to be headed by a Board of Directors of the same membership as the Federal Home Loan Bank Board, and to be capitalized by the issuance of nonvoting stock to the Federal Home Loan Banks. The new corporation was to provide a secondary market not only for conventional mortgages, but also for federally insured and guaranteed mortgages. The terms and limitations of this operation were made identical to those applicable to FNMA, with the somewhat confusing explanation that this was done ". . . so there can be a parallel development of these institutions and so neither would have any competitive advantage over the other.[43]

The parallelism, however, was less than complete. For example, the Senate Committee had proposed that the new corporation be exempted from State taxes (except real property taxes), but that—like FNMA—it be subject to Federal income and other taxes. The act as finally adopted, however, exempted the Corporation from all taxes, both Federal and State (except real property taxes).

The demand for mortgage credit was sufficient to enable both these new secondary market operations to begin functioning rather promptly and on a substantial scale, in spite of what might be thought their somewhat redundant character. Presumably as the natural result of their established institutional relationships, the FHLMC under the Bank Board dealt primarily with savings and loan associations and similar lenders, while FNMA found its market mainly among mortgage bankers and related institutions. By fiscal year 1973, each of the new facilities was purchasing mortgages in a volume of roughly $1.5 billion annually.

Comments on the "Private" Character of FNMA

The FNMA created in 1968 is indeed, in a technical sense, "privately owned" and "privately financed." But it is worth observing that this may be something different from the image frequently projected both by it and for it—that FNMA has become simply a large private corporation, owned by its principal users and doing business in the market place. This image involves matters of semantics and rhetoric, as well as of law and finance. Clearly, the new (and present) FNMA is distinguishable from such a purely private corporation on at least four significant points:

1. Its charter was granted by Congress to accomplish purposes which, if somewhat vaguely stated, were public in character. Subject to constitutional limitations, that charter may be altered or revoked as Congress may determine.

2. In granting the FNMA charter and providing for the withdrawal of the Federal Government from an ownership position in the new corporation, the Congress nevertheless reserved important powers to the Secretaries of Housing and Urban Development and of the Treasury. These include the power of the Secretary of HUD to control the declaration of dividends and the volume of financing undertaken, and the power of the Secretary of the Treasury to control both the timing and the terms of the Association's financing program in the private market.

That the Congress was fully aware of what it was doing is made clear by the language of the Senate Committee Report, which observes in pertinent part:

> The Secretary [of HUD] would have general regulatory powers over FNMA *to assure that the purposes of the charter act are served . . .*
>
> The committee feels that adequate safeguards have been provided to assure that the privately owned FNMA *will continue the secondary market operations in a manner consistent with the best interests of the public* . . . one third of the board would be appointed by the Secretary and all would be removable for good cause by the President of the United States. Finally, *the Secretary's regulatory power over FNMA* would be sufficient to protect against abuse of the public interest. (Emphasis added.) [44]

These are hardly the terms of reference of any ordinary business enterprise.

3. The Congress may have intended its creature to swim in the waters of the private market, but it did not intend that it should sink. Thus it left in place behind the private FNMA—like its predecessor—a $2.25 billion line of credit to the Treasury in case of need. That this was deliberate and not a product of oversight is made clear by the fact that the same Act repealed a provision which had prohibited borrowings from the Treasury after all preferred stock held by the Secretary of the Treasury had been retired.

4. The prompt and all but unqualified acceptance of FNMA obligations in the private market reflected something more than recognition that the underlying security consisted of

[43] Ibid.

[44] S. Rept. 1123, 90th Congress, 2nd Session, May 15, 1968.

mortgages all of which were either insured or guaranteed by the Federal Government. It reflected also a market judgment—almost certainly correct—that the Federal Government's identification with and sponsorship of FNMA ran so deep that the Government would not, and could not, under any circumstances permit FNMA obligations to fail in the hands of private holders, thus destroying its credibility in the market. Thus these obligations were regarded as enjoying a de facto, even if not de jure, Government guarantee.

It is abundantly clear that FNMA is not an ordinary private business enterprise in the generally accepted meaning of the words. On the other hand, it is clearly not a Federal agency in the ordinary meaning and acceptance of that term. It appears, rather, to fall in that hazy and ambiguous in-between class of agencies—such as the Federal Reserve Board, for example—which are "private" in their formal ownership and mode of operations, yet so deeply affected by the public interest and so rooted in Federal sponsorship and policy as to have unbreakable, even if informal, linkages to the public sphere.

Special Assistance and the Budget Impact

Because of their very nature as wholly owned corporate activities of the Federal Government, the special assistance functions of FNMA (originally) and GNMA have from their inception had a very substantial impact on the Federal budget. It was inevitable, therefore, that special assistance should become an area of contention between conflicting policy objectives. To generalize and perhaps somewhat oversimplify, housing policy commonly looked toward furtherance of some specific housing objective (such as encouragement of cooperative housing, or of housing for low and moderate income families) or toward stimulation or stabilization of the housing economy at a high rate of production, or both. Budget policy, on the other hand, normally looked toward maximum feasible restraint on budget outlays and on the generation of new obligational authority that would create budget exposure.

The built-in tension between these two often incompatible objectives has had important practical consequences, both with respect to policy and levels of program activity, and with respect to procedures and methods of operation. Two examples may be cited.

Budget Control of Program Levels: Largely because of the dominant weight assigned to budget considerations, the special assistance authorizations available to the President have, throughout the entire period since 1954, greatly exceeded the funds that were made available for use through budgetary release. This in turn led not only to dissatisfaction in the housing industry and the Congress, but also was the motivating factor which led the Congress on several occasions to enact designated special assistance programs of its own, rather than waiting for Presidential action. These programs were, in substance, efforts to apply leverage to achieve a higher level of special assistance support than the Administration was willing to make available. These too, however, have been subjected to budget control, so that for such federally funded programs, budgeted levels effectively control the extent and character of operations.

Tandem Plans: Similar considerations led to the development of such devices as the so-called "tandem plans," which had the effect of reducing the immediate budget impact of special assistance support, while in all probability increasing the ultimate cost to the Government.

Under the tandem arrangement, GNMA issues a commitment to purchase a mortgage eligible for special assistance at a predetermined price which is more favorable than that available in the market (special assistance being unnecessary otherwise). This commitment is transferred to FNMA, and, when the mortgage is ready for delivery, GNMA pays FNMA the difference between the committed price and the price which FNMA would have paid in its regular market purchase program. Thus the immediate budget expenditure is reduced from the full amount of the purchase commitment to this difference—usually a few percentage points of the full amount.

Since the tandem plan is essentially a device for substituting one source of funds for another to achieve a budgetary (rather than a housing) result, it is not further considered here, beyond noting that this favorable effect on the budget has made possible higher levels of special assistance activity than otherwise would have been acceptable.

The growth of special assistance activity in the last few years has been in part due to the major effort to achieve a greater volume of low and moderate income housing, but to a significant degree it has been acceptable only because the tandem arrangement greatly ameliorated the budget problem.

The whole subject of Federal budget concepts and their impact on the generation or residential mortgage credit is both too technical and too complex to be examined here. It should be noted, however, that budget considerations are certain to exercise a restrictive effect on direct Government activity in the secondary mortgage market, so long as their budget treatment emphasizes immediate expenditures, with little or no consideration for long term costs, and draws no distinction between current expenses and outlays for long term capital investment.

Present Posture of the Government in Relation to the Secondary Market

Looking back over this long and complex history, it is difficult to discern any unifying concepts or institutional forms which have developed in such a way as to rationalize and provide coherence to the Government's role in the secondary residential mortgage market, other than the continuing recognition of the need for Government intercession to assure an adequate supply of mortgage credit.

Beginning in 1954 with the Charter Act, and for some years thereafter, it appeared that such a conceptual pattern was crystallizing. This pattern may be considered to rest on four general propositions:

1. That the Government should provide a facility to assure a dependable market for insured and guaranteed mortgages, in order to assure an ample supply and reasonable geographic distribution of mortgage credit, to help maintain stability in the mortgage market (especially during times of credit stringency), and to help keep the volume of insured and guaranteed mortgage lending at a level which would be sufficient to give effect to their influence on mortgage lending practices generally. This facility, however, should be financed in the private capital markets and should be limited to the purchase of mortgages of general market quality.

2. That the Government should also provide a facility for providing temporary support to new and innovative forms of residential mortgages designed to fulfill national housing objectives, pending the establishment of their acceptability in the private market, and also—in times of great need—to supply temporary bulges in the availability of mortgage funds to avoid undue shrinkage of housing production.

3. That the mechanisms of the Federal Home Loan Bank system, properly used, should prove competent to maintain adequate funds and stability in the conventional mortgage lending field.

4. That the Government's policies and activities in these areas should be housed in a single agency (later department), in order that they could be consistent and coordinated among themselves, with the general housing market, and with related Federal credit policies and programs.

As it developed, this pattern was but a temporary phase. It began to unravel in 1955, when the Federal Home Loan Bank Board was removed from HHFA and established as an independent agency, thus at once narrowing the Administrator's authority and responsibility for overall coordination, and eliminating any clear channel or mechanism through which such coordination might be brought about.

In 1968, mainly (as noted above) for budgetary reasons, FNMA as established in 1954 was partitioned, with the secondary market functions going into a new private corporation. Although efforts were made to retain some coordinating powers in the Secretary of HUD and the Treasury, the natural result of this move was to fragment further the secondary market functions and blur both responsibility and machinery for general oversight or the development of common premises and purposes.

In 1970, the Congress compounded an already confused situation by establishing two new secondary market facilities with identical authorities and stated objectives—one in the private FNMA and the other in a new subsidiary of the Federal Home Loan Bank Board.

Meantime, again for budgetary reasons, the operations of the remaining Government-operated secondary market facility (GNMA) were channeled to an increasing extent through the mechanisms of the private FNMA, while the mortgage-backed securities device had the effect of escalating practically every large mortgage lender in the country into a sort of self-contained secondary market, operating under color of the full faith and credit of the United States.

In short, it would appear that after almost four decades, the exact nature of the Federal Government's role in relation to the generation of housing credit through the secondary market is, if anything, more incoherent than ever. By the same token, the productivity and stability of the housing industry are no less dependent on the availability of credit in the secondary market now than in the past, and the continuing availability of such credit continues to depend, in critical degree, on this variety of government and government-sponsored or underwritten mechanisms.

Extension of Federal Credit Aids for Groups Having Special Housing Needs

The Federal programs previously discussed have dealt with measures to provide housing for the broad range of American families, especially those of lower income. The programs discussed under this heading are those designed to provide credit assistance, through mortgage insurance, direct loans, and other techniques for groups having special housing needs, such as veterans, farmers, the elderly, or families displaced from their homes by governmental action.

The programs discussed here do not include those designed initially to provide overt subsidies such as the various subsidy interest rate and grant programs (which are treated separately). For convenience, however, this part does cover those programs that started out on a nonsubsidy basis and were converted to subsidy operations later, such as the direct loan program for college housing.

FHA Mortgage Insurance for Special Groups

In addition to the gradual liberalization of mortgage terms under the regular FHA insurance operations, the Congress has enacted since 1941 a series of special mortgage insurance programs for particular categories of families having special needs. (As discussed above, the special assistance functions of FNMA's secondary market were also used for these programs.) It was in this way that the overall character of FHA was changed in the 1940's and 1950's from an agency that was concerned almost entirely with increasing the supply of adequate housing to an agency that became widely concerned with serving special public purposes in the housing field. The development of these new programs generally did not occur in FHA itself, but in other offices of the Housing and Home Finance Agency and the executive branch, and there was reluctance by some in FHA to assume responsibility for the new operations. At the same time, outside criticism developed in some quarters to special-purpose programs on the ground that they diverted FHA efforts from volume production and resulted in high risk insurance.

Generally, each of these new special programs was established as an almost independent operation with its own statutory provisions and insurance fund, in order to avoid adverse effects on the regular programs under Sections 203 and 207. The essence of each new program was a liberalization of mortgage terms beyond those in effect at the time under the regular insurance programs. The liberalization in all cases followed a quite regular pattern, so that it can be described categorically. Except as mentioned in connection with each special program, mortgage terms were liberalized in three ways:

1. The "economic soundness" test for the proposed construction was replaced with an "acceptable risk" test.

2. The maximum insurable mortgage loan was based on "replacement cost" rather than on the more conservative estimate of long range "value." This change and that under 1, above, are discussed above, under "Select Use of New Underwriting Concepts."

3. The maximum percentage or ratio of loan to "replacement cost" was made higher than the earlier percentage of loan to value. This sometimes took the form of raising the maximum dollar amount which could be included at a higher ratio. In some cases, also, the maximum term of the mortgage was lengthened to permit lower monthly payments. These programs are discussed briefly below.

World War II Defense and Veterans Housing: The first new special purpose program was enacted in March 1941, to provide mortgage insurance on liberal terms to builders providing sales housing for defense personnel in critical defense areas (Section 603 of the National Housing Act, added by Public Law 24–77th Congress, approved March 28, 1941). The program was extended to rental housing (Section 608) the following year, when most of the above-listed liberalizing features not already enacted were added (Public Law 559–77th Congress, approved May 26, 1942).

In some areas, particularly around military bases and new defense industries, there was such a shortage of housing that defense activities were being impeded. Priorities and allocation controls were being imposed on new construction during the war, and they contained requirements that the new housing under the program be made available to workers in defense industries and to certain categories of military personnel.

There was also a strong desire on the part of the executive branch and the Congress to get private enterprise engaged in the construction of needed war housing to supplement the large volume of direct Federal construction being undertaken for war workers under the Lanham Act (Public Law 849–76th Congress, approved October 14, 1940, and related "temporary shelter acts"). Almost $2 billion was appropriated for the direct construction (or conversions of existing structures) that provided nearly a million dwelling units.

After the end of World War II, one of the paramount domestic concerns of the Nation was the housing of returning veterans and the backlog of housing construction. Accordingly, as previously indicated, the Congress enacted the Veterans Emergency Housing Act of 1946, which reenacted the Sections 603 and 608 programs, making them applicable to housing for veterans of World War II instead of war workers, and on still more liberal terms. The same Act contained drastic measures to stimulate, and make possible, quick housing production. It made the priorities and allocation powers previously used for war purposes available for getting materials and equipment needed for use in housing and in the construction of housing, and for producing building materials. Premium payments were authorized to producers to speed up the supply of building materials. Allocated war assets in the form of materials and equipment needed in home construction and in the production of lumber and other scarce items were of tremendous value to housing production. A guaranteed market program was authorized for new types of building materials and prefabricated houses. Because of industry objection to many of the severe controls, most of these authorities were repealed the following year.

Scandals resulting from the loose application of insurance standards under the Section 608 program have been explained previously in connection with the enactment of "cost certification" requirements which effectively prevented the particular abuse of "mortgaging out."

Notwithstanding abuses, Sections 603 and 608 programs were successful in meeting the great housing needs of war workers and later returning veterans. In all, 690,006 dwelling units were insured under Section 603, and 465,674 under Section 608.

Cooperative Housing: The Section 213 cooperative housing program was discussed in this paper, under "New Special Forms of Ownership." Although it was made available broadly for a specific type of ownership, as distinguished from a special group of persons, it embraced essentially the same liberalized mortgage term provisions as discussed here. As explained, the cooperative housing mortgage insurance has been one of FHA's most successful ventures, having assisted the production of about 150,000 dwelling units [45] for moderate income families.

Korean War Housing: Early during the Korean War, the Housing and Home Finance Agency developed a very comprehensive package of legislative proposals encompassing the whole field of activities that should be undertaken by the Federal Government to provide or assist in providing defense housing and community facilities needed in "critical defense housing areas." This was enacted in about the same form as proposed, and was made effective for 2 years (Defense Housing and Community Facilities and Services Act of 1951).

That legislation included a liberalized form of home mortgage insurance (Section 903) and rental housing mortgage insurance (Section 908) similar to Sections 603 and 608 for World War II. The new authority was unique by retreating in one respect on liberalized terms, however. It returned to the "value" concept in establishing a mortgage ceiling instead of "necessary current cost." Concern had already developed over excessive mortgage amounts under the Section 608 program. However, the facts producing the famous "FHA scandals" of 1953 had not yet surfaced.

The vast use of new legislative authority contemplated under the 1951 Act never occurred. Only 65,703 units received mortgage insurance under Section 903, and 8,485 units under Section 908. Other programs authorized by the 1951 Act were little used, such as the programs for direct Federal construction of war housing and facilities similar to Lanham Act authority in World War II.

Housing in Urban Renewal Areas: The "slum clearance and community development and redevelopment program" (the Title I program) authorized by the Housing Act of 1949 had a slow start. It required State enabling legislation and participation by local governments, and the program actions at the local level were novel, enormous, and time-consuming. However, a specific and overshadowing obstacle developed to the execution of the typical redevelop-

[45] 1971 HUD Statistical Yearbook.

ment through housing construction. A redevelopment project had to be either "predominantly residential" before clearance, or the area had to be redeveloped for predominantly residential purposes after clearance. The regular FHA insurance programs were wholly inadequate to attract credit and sponsors.

The President's Advisory Committee on Government Housing Policies and Programs issued its report in December 1953, making major recommendations on HHFA programs, including those relating to slum clearance and redevelopment. That program was changed to the "urban renewal" program with a broadened scope that covered rehabilitation projects as well as clearance and redevelopment. Thereafter, a community was required to have a "workable program" for solving its overall development problems as a condition to urban renewal and related Federal aid. As part of this package of new legislation, a mortgage insurance program was recommended to generate housing credit and production in urban renewal areas.

The new program was proposed by HHFA as part of the Housing Act of 1954 and enacted as Section 220 of the National Housing Act. It applied liberal mortgage insurance terms to home mortgage and multifamily projects, both new and rehabilitated. (Although the substitution of "replacement cost" for "value" in determining maximum mortgage amount was not made until the following year in the Housing Amendments of 1955.) The Administration at that time stressed rehabilitation as a means of reducing the Federal outlays required for "bulldozer" clearance operations.

A basic feature of this Section 220 program was the new underwriting principle that the housing project be approved by FHA and go forward on the assumption that the urban renewal program would redevelop the area into a viable neighborhood. Accordingly, instead of the usual "economic soundness" requirement, the Housing Administrator was required to certify to the Federal Housing Commissioner that the urban renewal plan for the area conformed to the general plan for the locality as a whole and that there existed the necessary authority and financial capacity to assure the completion of the urban renewal plan. The Federal Housing Commissioner also had to determine that the housing would meet such standards and conditions as he imposed.

Great delay in many urban renewal projects again occurred because of internal agency controversy over implementing the Section 220 program. Often a housing project considered feasible by those administering urban renewal was not considered feasible for mortgage insurance purposes, or the price approved for the sale of urban renewal land to a housing developer was considered excessive by FHA. Conversely, the changes sought by FHA were often thought to be inconsistent with the urban renewal objectives. This problem was resolved by the firm administrative action of the Housing Administrator, who coordinated the two program operations and imposed joint procedural requirements.

The Section 220 program became generally successful in generating credit for housing production in urban renewal areas. The criticism of the program in later years stemmed from the fact that it produced housing for high income families and not for those displaced from the area. It was not designed for low income or displaced families as such, however, but to provide housing needed in the community and housing that would add to the city's tax base.

Prior to 1972, mortgage insurance under the program had been written for 72,665 dwelling units—a large figure considering the fact that all units must be constructed within urban renewal areas.

Housing for Families Displaced by Governmental Action: By 1953, experience had begun to show the magnitude of the urban renewal problems resulting from the displacement of families from project sites to be cleared. These problems became the chief basis for objection by local governing bodies, in those cases when disapproval occurred. The lack of adequate housing for the displaced was critical, and there was growing concern for the plight of those affected, who were generally poor or minority families, or both.

Accordingly, the President's Advisory Committee, in its report that year (above), recommended a special mortgage insurance program for displaced families, which was proposed by HHFA as part of the Housing Act of 1954 and enacted as Section 221 of the National Housing Act.

This new authority required that the housing involved be "programed" for each area on the basis of the number and income of families displaced by governmental action, and that they receive priority of opportunity to purchase or rent the dwellings. This governmental action included any Federal, State, or local government action. The city was required to have a "workable program" for community development, and the city or other local government had specifically to request the housing (this latter requirement was later repealed).

The liberalized mortgage insurance terms described above were granted in this program, except that the substitution of "replacement cost" for "value" was not made with respect to single family homes, nor with respect to multifamily structures until the Housing Act of 1959. Originally, program sponsors were restricted to nonprofit organizations, but profit sponsors were made eligible by the Housing Act of 1964.

The Section 221 program was split by the Housing Act of 1961 in order to: (a) Continue the special program for displaced families, but broaden it to cover all low income families (known as the 221(d)(2) program); and (b) establish a subsidized interest rate program (known as 221(d)(3), and discussed in the next paper, Subsidy Programs). The Administration at that time considered the (d)(2) part of the program as one primarily for the suburbs (the "workable program" was waived for it) and the new (d)(3) program as one primarily for the central city.

Also, Section 221 later became the base for a special subsidized interest rate program [Section 221(h) (and the similar Section 235(j) programs beginning in 1968) enacted in the Demonstration Cities and Metropolitan Development Act of 1966] to assist nonprofit corporations to buy and rehabilitate deteriorated housing for sale to low income families.

The credit and production incentive of all of the Section 221 functions was enormous—through calendar year 1971, 775,824 units with mortgage insurance at the market interest rate, and 194,232 units at the subsidized interest rate.

Housing for Servicemen: The Housing Act of 1954 also provided a special home mortgage insurance program for servicemen. It was designed to remove the incentive otherwise given to servicemen to retire and receive the housing benefits of the GI Bill. It had been claimed by the Department of Defense that many trained officers were lost to the service in that way in view of the inadequate housing near military installations. During the period that a house, assisted with mortgage insurance, remained occupied by a serviceman, the insurance premium was to be paid by the Secretary of Defense rather than the serviceman.

The mortgage insurance terms were liberalized, but "value" was used in determining maximum mortgage amount rather than "replacement cost." For servicemen, the program is similar to the regular home mortgage insurance program under Section 203, except for the benefits mentioned, which gives the serviceman advantages similar to those given a veteran under the home loan guaranty provisions of the GI Bill of the Veterans' Administration.

The insurance operations under this program have been very large—241,936 dwellings by the end of 1971.

Military Housing Insurance—Wherry Act and Capehart Act: During the late 1940's, the Department of Defense, especially the Air Force, became very concerned about the lack of adequate housing for its civilian and military personnel assigned to duty at or near military installations. The Air Force pressed the HHFA to develop some form of remedial legislation which would use private investment, because Defense had been unable to obtain appropriated funds from the Congress on a scale that would begin to meet the problem through direct Federal construction.

The HHFA prepared legislation for a mortgage insurance program with the liberal mortgage insurance terms discussed above. It was to be a rental housing program for a 2-year period, and the Secretary of Defense was authorized to lease Government land and sell utilities and services for the housing. The mortgages were to carry the low interest rate of 4 percent or less, and it was contemplated that the Federal National Mortgage Association would buy the mortgages.

As some protection to FHA, no mortgage could be insured unless the Secretary of Defense certified: That the housing was necessary for military personnel; that the installation was deemed a permanent part of the Military Establishment; and that there was no present intention to curtail activities substantially at the installation.

A draft of this legislation was picked up and passed quickly by the Congress (Public Law 211, 81st Congress), due in part to the interest of top congressional leaders in housing conditions around installations in their States or districts. One of these leaders was Senator Wherry of Nebraska, who sponsored the legislation and gave his name to the program.

The program soon operated in volume, and spawned another trade association consisting of Wherry Act sponsors, who obtained legislation beneficial to them in later years, including authority for the Department of Defense to purchase their projects.

The Department of Defense was not satisfied with the Wherry Act because, although it resulted in production of housing for their personnel, the housing was not sufficiently under its control and was too unlike public quarters which it managed.

Therefore, largely on the recommendation of the Department of Defense, but concurred in by HHFA and the Administration, the Congress substituted the Capehart Act for the Wherry Act (both were Title VIII of the National Housing Act). This was done by the Housing Amendments of 1955. It provided, among other things, for more liberal mortgage insurance (up to 100 percent of replacement cost).

Capehart housing is undoubtedly the outstanding example of a "Rube Goldberg" financing scheme authorized by housing legislation. During Senate Committee hearings, Committee members referred to it by that name. It was designed so that the Defense Department could have all of the controls and advantages of housing built by it, but without using its appropriated funds.

Under clear authority in the new provisions, the Department of Defense leased its land to builder-sponsors who then became mortgagors under the new FHA insurance program. Builder-sponsors were selected on a competitive bid basis and the Department of Defense used its own architect to plan the projects. Funds were obtained from private lenders who sold the mortgages to FNMA, which, in turn, obtained funds through borrowing from the Treasury under the FNMA special assistance program.

As soon as housing construction was completed in a Capehart project, it was acquired by the Department of Defense (by purchasing the stock of the builder-sponsor pursuant to prior agreement), which assumed payments on the mortgage notes insured by FHA. If the FHA did not agree that the housing was needed, it could nevertheless insure the mortgage if the Department of Defense guaranteed FHA against loss on the mortgage.

Through the above complicated use of Department of Defense and HHFA operations, the Defense Department obtained housing it could maintain and control as public quarters without using direct appropriations, but by using Treasury funds traveling over a very indirect route.

Over 205,000 dwellings were produced with the assistance of the Capehart military housing program. Authority to enter into further FHA commitments to insure these housing mortgages ended October 1, 1962.

However, one supplemental mortgage insurance program with liberal terms (Section 809) for military housing still continues. That is a home mortgage insurance program for civilians employed at research or development installations of the military departments, the National Aeronautics and Space Administration, or the Atomic Energy Commission. A special program of no more than 5,000 units was authorized (Section 810, enacted in the Housing Act of 1959) for military housing, but was not successful.

Housing for the Elderly: The Housing Act of 1959 established a new direct loan program for housing the elderly, which is discussed below under a separate heading. The same pressure by groups and the same interest in the Congress that resulted in the direct loan program also produced in the same Act a new FHA mortgage insurance program for rental housing to serve elderly persons. Several special advantages previously had been granted (by the Housing Act of 1956) to elderly housing under the regular mortgage insurance program for multifamily structures (Section 207).

The new program contained the several liberalized mortgage insurance terms discussed above. It contained a special advantage if the sponsor was a public body or nonprofit corporation—the mortgage could be up to 100 percent of replacement cost rather than the 90 percent otherwise applicable.

By the end of 1971, about 40,636 dwelling units had been insured under the program.

Nonhousing or "Fringe" Mortgage Insurance Programs

Nursing Homes, Hospitals, and Group Practice Facilities: The success of mortgage insurance as a means of accomplishing objectives desired by the Congress, by industry, or by others, finally led to various efforts to apply this method to a variety of projects not even involving housing. These included mortgage insurance on nursing homes, hospitals, and facilities for group medical or group dental practice. While those particular programs produced substantial results, they were widely criticized on the ground that they were inappropriate uses of mortgage insurance and that they diverted FHA from its basic housing mission.

The Housing Act of 1959 established a special mortgage insurance program (Section 232) for proprietary nursing homes, and nonprofit facilities were added later. Mortgage insurance programs for group practice facilities and hospitals were added in 1966 and 1968, respectively.[46] These facilities are not comparable to residential property as mortgage security; insurance of a mortgage on one of them is more in the nature of insuring a business. In the event of foreclosure, there is no group of prospective purchasers on a scale similar to that existing for housing.

The reason for placing the hospital program in HUD was largely political, because the House Banking and Currency Committee was more responsive to the program than the Committee on Education and Labor, which ordinarily would have handled such legislation.

Hospital programs are naturally in the domain of HEW, where the Hill-Burton hospital grant program is administered. Accordingly, HUD has used HEW to process mortgage insurance applications under the special mortgage insurance program for hospitals. This has given rise to policy conflicts at times, because the applicable FHA regulations, which are consistent with those for other FHA programs, vary in some respects from HEW regulations applicable to Hill-Burton projects. At the same time, there are complaints of inconsistencies between HEW policy decisions made in processing under the new program and decisions made by FHA in processing applications for mortgage insurance on housing.

Recreational Homes: The Housing and Urban Development Act of 1968 authorized mortgage insurance for recreational homes—those that need not be designed for year-round occupancy. A conservative maximum mortgage amount of 75 percent of appraised value was prescribed. Other mortgage and property requirements were provided on a liberal basis. Authority was given to suspend the program if it would adversely affect mortgage funds for other programs.

This program has been criticized as being an unwarranted extension of Federal financial assistance into an area which private enterprise alone should handle. So far, the program has remained suspended.

Trailer Courts: Since the Housing Amendments of 1955, the regular multifamily mortgage insurance program (Section 207) has been applicable to mortgages for the development of trailer courts. This program has been criticized because of its questionable objectives in terms of improving housing standards and the need for Federal involvement.

[46] Demonstration Cities and Metropolitan Development Act of 1966 and Housing and Urban Development Act of 1968.

Mobile Homes: The regular FHA repair and improvement loan insurance program (Title I) was extended by the Housing and Urban Development Act of 1969 to cover mobile homes used by the owners as their principal residences. As indicated, the Title I program insures financial institutions against losses on a coinsurance basis. A trailer loan under the program can now be as high as $15,000 (involving two or more modules), and for a term up to 15 years and 32 days if property and site standards are met.

Pressure for this program was resisted for years on the basis that (1) it was not a program consistent with the best objectives for improving the living conditions of American families, and (2) the security for the loan (the trailer) was inadequate, because it could quickly disappear. The experience of private enterprise proved the second reason to be at least partly unfounded, although problems do exist. The sale of mobile homes has skyrocketed like nothing else related to housing, as shown by the recent volume given previously in this report. At the same time, Federal involvement has been shown to be unnecessary for production. A high volume of production and sale occurred before the mortgage insurance program was put into effect. At present, about 6,000 trailers have been reported as being included by institutions within their Title I loans.[47]

Alaska Housing: The HHFA program for Territory of Alaska housing, under the Alaska Housing Act of 1949, was temporary and limited. It is worth mentioning, however, as possibly the best example of excessive credit granted on a programwide basis for a most worthy objective. It permitted a very belated use of FHA insurance in Alaska which became enormously successful in meeting a critical need. But the act also permitted such liberal extensions of credit (especially through a local public agency, the Alaska Housing Authority) that foreclosures on multifamily structures were scandalous, and the easy credit under the act even attracted fraudulent sponsors from distant points in the States.

Yield Insurance: The greatest failure to implement a program of HUD or its predecessors was under the "Yield Insurance" program authorized by Title VII of the National Housing Act. That authority, given in the Housing Act of 1948, is still on the statute books. A billion dollar insurance authorization was provided, but no insurance was ever written.

[47] HUD staff.

The purpose of the program was to encourage equity investment in rental housing, tapping funds of insurance companies and pension funds. At that time, some insurance companies had placed equity funds in rental housing developments. The program included the insurance of an annual return from a housing project (built with equity investment) which would equal a computed minimum amortization charge plus an annual return on the outstanding investment equal to fixed percentage.

The program was not a "mortgage" insurance operation, because outstanding obligations after completion of construction were prohibited. Later, however, to make the program more attractive, the authority was amended to permit nonmortgage borrowing against income.

At one time, real interest was shown by bond counsel and investment firms, and several sponsors took action in contemplation of using the program, but shifted instead to Section 207 mortgage insurance.

Direct Loans for Housing the Elderly and Handicapped

In the late 1950's, increasing pressure was put on the Banking and Currency Committees to enact a direct loan program for housing to serve the elderly. It was contended that the special but modest FHA-mortgage insurance terms for elderly housing at that time were far from adequate to help provide housing at rentals which the majority of elderly could afford. By that time, however, the Bureau of the Budget was strongly opposed to direct lending because of its budget impact, and the Administration opposed a direct lending approach.

Using the drafting service of HHFA, the House Banking and Currency Committee developed provisions for the direct loan program which became section 202 of the Housing Act of 1959. It was enacted as part of the same bill that included the new section 231 mortgage insurance program for the elderly, previously discussed.

Under the new section 202 authority, the Housing Administrator could make direct loans to private nonprofit institutions for the construction or rehabilitation of housing and related facilities for elderly persons (a later amendment added handicapped persons). The loan amount could equal 98 percent of the development cost of the project, the term of the loan could be up to 50 years, and the maximum interest rate was, in effect, fixed at the average annual interest rate on all interest-bearing obligations of the United States then forming part of the national debt. The borrower had to show that he was unable to obtain necessary funds "from other sources upon terms and conditions equally as favorable." The housing could not be of elaborate or extravagant design or materials. An initial appropriation of $50 million was authorized for a revolving fund for the loans.

The Agency established a task force for rapid implementation of the program. In 1965, when loans were being made under the program at an annual rate of about $60 million, the Congress lowered the interest rate on the loans to 3 percent (Section 105 of the Housing and Urban Development Act of 1965), which resulted in a loan volume of $100 million during the following year. The rate before the amendment in 1965 was 4 percent, and the House Committee said, in reporting the amendment, that the 3-percent rate would reduce monthly debt service on a typical dwelling from about $45 to $39. The program reached a peak of $130 million in 1968. The aggregate of loans under the program exceeded $574 million.

The elderly housing direct loan program was very popular with sponsors such as church and other eleemosynary organizations and builders. After the subsidy program for multifamily housing (Section 236 of the National Housing Act, discussed later) was enacted in 1968, the Department of Housing and Urban Development stopped making commitments under the direct loan program, as part of the executive branch policy of reducing or eliminating direct Federal loan operations. In this case, the Department contended that substantially all of the benefits of the direct loan program, and more, could be obtained under the subsidy program, with additional costs to sponsors of only relatively minor finance costs during construction.

A tremendous lobbying campaign to retain the direct loan program was carried on with the Department and the Congress. Subsequently, the Congress increased the amount of the appropriation authority for the program, and the Banking and Currency Committees attempted unsuccessfully to get the Department to revive the program.

Direct Loans for College Housing

A program of direct loans for college housing was authorized by Title IV of the Housing Act of 1950. It was developed quickly in the Congress as the result of an unusually effective effort by college and university presidents who testified for the program in 1949 and 1950, led by John A. Hannah, President of Michigan State College and President of the Association of Land Grant Colleges and Universities.

The support for the program was based upon the tremendous increase in college enrollment that started in the post World War II era, the lack of dormitory construction during the depression period and the war, and the desire to assist returning veterans. This group constituted a large part of college enrollment because the War had delayed their education, but they could now use the benefits of the GI Bill. At that time, the student enrollment of about 2½ million, about half of whom lived away from home, was overwhelming.

Under the new direct loan program, the Housing Administrator could make loans to public or nonprofit private "educational institutions of higher learning"[48] for new or rehabilitated dormitories or apartments to accommodate students or faculty members. The loan amount could equal 100 percent of total development cost, the term of the loan could be up to 40 years, and the maximum interest rate was the rate specified in the most recently issued bonds of the Federal Government having maturity of 10 years or more, plus .25 percent. The borrower had to show that he was unable to obtain necessary funds "from other sources upon terms and conditions generally comparable . . . ." The construction could not be of elaborate or extravagant design or materials. The borrower was also required administratively to offer the bonds in the private market; if no "equally favorable" bid were received, the Government would then purchase the bonds pursuant to its loan commitment. To obtain funds for loans, the Housing Administrator was given an initial $300 million borrowing authority.

In reporting the bill containing authority for this program, the House and Senate committees on Banking and Currency stressed its benefit to students, explaining how it could reduce dormitory rentals by more than one-half.[49]

The program started slowly because it was first suspended by the President and then limited to defense-related loans, in order to conserve building materials for Korean War purposes. Defense restrictions were removed on August 4, 1953, and in 1955 (Section 301, Housing Amendments of 1955), a significant change in a prerequisite for borrowing accelerated the use of the program. Instead of the borrower having to show, as previously, that he could not obtain funds from other sources on "generally comparable" terms, he now had to show only that he could not obtain funds on "equally as favorable" terms. This also avoided a troublesome problem of regulating on the earlier prerequisite.

Accordingly, the annual borrowing rate increased to over $300 million in 1955 and stayed above that amount most of the years until 1969, reaching a peak of $447 million in 1961.

In 1968 (Section 1705(b) of the Housing and Urban Development Act of 1968), the Congress enacted what was referred to as a second program of college housing aid in the form of an interest rate subsidy program to back up private housing loans to colleges. This came at a time when there was concern about the huge outlays of Federal funds advanced on college housing loans, and when there was continuing objection by the Bureau of the Budget (now the Office of Management and Budget) to direct loans in general.

The new grant authority was made available to reduce the annual debt service payments on a private market college loan to the amount of the annual debt service that it would have had to pay if it had borrowed under the Government's direct loan program. In other words, the college would end up with the same financial advantage under either program—the Federal lending rate was then 3 percent.

Of course, the initial Federal outlay under the new grant program was only a fraction of that under the direct loan program. The Department of HUD was authorized to enter into contracts with the schools to make these grants annually. Initially, the total annual grants in any year could not exceed $20 million.

As explained by the House and Senate Committees on Banking and Currency in reporting the 1968 Act (See House Report No. 1585, page 102), it was intended that the direct loan program generally would continue as before for those institutions which could not borrow in the private market at reasonable interest rates. It was expected that public institutions which had the advantage of Federal tax exemption on their bonds could borrow privately at sufficiently low interest rates so that, with the new interest rate subsidy, they could provide dormitories at sufficiently low rentals. The committee pointed to further vast increases in enrollment, due in part to returning Vietnam veterans.

[48] See Report of Senate Committee on Banking and Currency, No. 892, 81st Congress, 1st Session, on Housing Amendments of 1949, p. 55.
[49] Ibid.

In 1969, the volume of direct loans (plus loans with grant assistance) dropped greatly, due to the shift in operations under the new authority and a decision to stop further direct loans except where the applicant showed he was not able to obtain reasonable financing under the new grant program. The program soon recovered its volume.

By June 30, 1972, a cumulative total of almost $5 billion of college loans had been made, including over $1 billion of private loans receiving the grant subsidy.

New commitments under these programs were terminated January 5, 1973, along with other housing subsidy operations.

Department of Agriculture Farm and Rural Housing Program

Experience during the early years of FHA mortgage insurance showed that this program was not very effective in small towns and rural areas. Some critics blamed this result—or lack of results—on FHA, alleging indifference on the part of the agency to the needs of such areas. More dispassionate analysis, however, suggests that the reasons for this outcome lie in the nature and the mode of operations built into the program in its authorizing legislation.

The natural clients of FHA in the private market were the home builders and mortgage lenders to whom its services were useful and important. But in small towns and the open countryside, professional home builders operating on any considerable scale were virtually nonexistent, and home mortgage lenders few and scattered. Thus, small town banks, for example, did not engage in home mortgage lending on a sufficient scale to make it worthwhile to master the fairly elaborate and sophisticated forms and requirements involved in mortgage insurance. They were better suited to making farm loans for such purposes as seed, livestock, and farm machinery, which involved shorter terms and simpler processing, and which afforded higher yields and less onerous servicing problems.

Even Federal savings and loan associations in moderate-sized towns were not greatly attracted to rural areas, in spite of their then-authorized 50-mile radius of operations. In the first place, these smaller institutions were even less attracted to FHA-insured and VA-guaranteed lending than were their counterparts in the larger cities. In the second place, relatively small mortgage loans on scattered sites at locations remote from the home office were expensive to originate, difficult to service, and awkward to deal with if the property were resold or the mortgage went into default. In short, some different kind of approach was needed if the housing problems of small towns and open rural country were to be met—both the needs for farm houses as such, and those not located on farms but in populated rural areas.

An Early Approach—The Housing Act of 1949 (Direct Loans): Title V of the Housing Act of 1949 was an effort to develop such a new approach. That part of the major 1949 Act authorized direct loans for farm dwellings and service buildings, and also loans and grants to low income farmers for minor repairs to homes and farm service buildings to eliminate hazards to health and safety. (Actually, loans for housing could be made under the original Bankhead-Jones Act. This was never considered to be a housing program as such, however, because its major thrust was toward encouragement of ownership of farms of adequate size and equipment, and in this context housing was considered as merely an adjunct of the physical plant of the farm considered as a whole.)

While better adapted to its rural purposes, the Title V program still was restricted to specified types of loans on structures actually located on farms. In 1961, however, these concepts began a gradual process of enlargement. In that year, housing loans were authorized to owners of nonfarm building sites in rural areas (then defined by regulation as open country and towns of not more than 2,500 population).[50] In the following year the authority was extended to include loans to buy previously occupied dwellings and minimum adequate building sites.[51]

Introduction of the Insured Loan—1965: In these early stages, Farmers Home Administration, as noted above, made direct loans—i.e., loans of Federal funds, on which the Government was the mortgagee. In 1965, the Congress commented that, even with the availability of such loans, a "widespread housing credit gap continues to exist in rural areas despite efforts of the Federal Housing Administration to reach farther and more effectively into . . . [these] . . . areas . . . ."[52] The proposed new method, it was explained, would ". . . serve to reduce in some degree the inequality between urban and rural families in the field of housing *without increasing the strain on the Federal budget.*" (Emphasis added.)

[50] Public Law 70, 87th Congress.
[51] Public Law 723, 87th Congress.
[52] S. Rept. 378, 89th Congress, 1st Session.

The italicized phrase is worthy of note because it directs attention to the fact that farm housing loans, like other efforts at direct lending for housing purposes, was subject to the continuing stress between social objectives such as housing, on the one hand, and budgetary considerations on the other. Direct farm housing loans (like FNMA mortgage purchases from Federal funds) were budget expenditures in the year of disbursement, and hence (if conducted in significant volume) had an immediate and substantial budget impact.

The Congress was quite aware that an effort to expand substantially the level of rural housing activity would meet with resistance from the fiscal authorities of the Executive Branch unless immediate budget impacts could be avoided or at least greatly minimized. This consideration may be thought to be the moving factor behind the adoption of the "insured loan" approach.

The Housing and Urban Development Act of 1965 [53] authorized insured loans (described below) and established a Rural Housing Insurance Fund as a medium for financing them. While the 1965 legislation extended the direct loan authorization and established another revolving fund to finance it (thereby somewhat reducing its requirements for new appropriations), it was thus clear that emphasis was shifting from the use of direct loans to the new insured loan approach. This shift was confirmed and formalized in 1968, when the direct loan revolving fund was abolished and its assets and liabilities were transferred to the rural housing insurance fund.[54] Actually, the direct loan program was not terminated by the 1968 law, which transferred the loan authorization to the insurance fund along with the assets and liabilities of the direct loan revolving fund. However, it has since dwindled to a very minor part of the total program.

The Rural Housing Insured Loan System: Since the insured loan has become the predominant form of rural housing finance by the Farmers Home Administration, it is relevant to briefly summarize how it works, especially because it differs greatly from the Federal Housing Administration's mortgage insurance system. In simplified form, the major steps are as follows:

1. Rural home loans are made through some 1,700 County Supervisors, who are responsible for ascertaining such matters as the eligibility and credit-worthiness of the applicant, the suitability of the proposed site, the unavailability of private credit in the area at reasonable terms, etc.

2. The loan is secured by a note and mortgage. Farmers Home Administration retains the mortgage. The note, however, is packaged with other similar notes to provide the collateral given for a special type of Government-guaranteed security representing a sum equal to the sum of all the principal amounts of the underlying notes, in denominations of $100,000 or more. These securities are sold in the private capital markets at rates determined by conditions in the money market at the time of sale. Their maturities may be of varying lengths because they are not controlled by the maturities of the underlying notes. At maturity, this security may (at the election of the holder) either be repurchased by the Farmers Home Administration (which thus reacquires ownership of the package of individual notes) or be renewed or extended for an additional period.

3. The proceeds of the blanket security sales are deposited into the Rural Housing Insurance Fund, thus effectively substituting private investment capital for the Federal funds which supported the original loan commitment.

4. Farmers Home Administration retains the mortgages, continues as mortgagee, and services the loans.

5. Since the interest cost of the blanket securities exceeds the interest realized on the underlying notes, losses accumulate in the Fund which are restored annually by appropriations. (Limiting language in the appropriation act is also used to put a ceiling on the total volume of insured loans to be approved during the fiscal year, which otherwise would be limited only by the resources of the insurance fund.)

The foregoing description relates to the so-called block system of financing, which accounts for the largest part of the Administration's activity in the capital markets. A variation not so extensively used provides for the direct sale of actual blocks of notes, in packages totaling $25,000 or more, which may be purchased from the Administration under a similar guarantee as to principal and interest.

Summary and Comments: It may be observed that the farm and rural housing program has conformed to the pattern of other housing programs over time, in that by virtue of various amendments it has become more general in application, while at the same time being applied

[53] Public Law 117, 89th Congress.
[54] Housing and Urban Development Act of 1968, cited supra.

to particular and special needs, such as those for rental housing, for the elderly, for cooperative housing, etc. (It should be mentioned that the total housing program of the Farmers Home Administration includes a number of other facets, such as loans and grants to encourage self-help housing; loans to families whose property is damaged or destroyed by disaster; assistance for certain home improvements, etc. These are not detailed here because of their relatively small volume and specialized nature.)

At the same time, the Farmers Home Administration has been drawn progressively deeper into the gray area between the actual farm and the larger towns and cities where the FHA mortgage insurance programs are effective. Thus, the original provision extending the program from farms to rural areas and towns of not more than 2,500 population was changed by the 1965 amendments to include places up to 5,500 in population which were rural in character. This was again revised in 1970 to increase the applicable population limit to 10,000.[55]

The level of activity has responded strikingly to the combination of a wider field of application and the revised budget treatment made possible by the use of insured loans. Not until 1963 did the total activity in a fiscal year exceed $100 million. By the time the insured loan procedure was perfected and established in fiscal year 1967, the volume had tripled, to a figure of almost $425 million. By fiscal year 1971, it passed $1 billion, and, in 1973, exceeded $2 billion—a level projected to be maintained by the 1974 Budget.

Some Comparisons with FHA Mortgage Insurance: It has already been noted that the financing system involved in the rural housing insured loan program is altogether different from that in the FHA mortgage insurance system. There are also significant differences in the operating methods of the two programs which are worth noting:

Local Processing and Operating Relationships: FHA deals primarily—indeed almost exclusively—with approved mortgagees and with builders. Its local offices seldom have any significant degree of direct contact with the home buyer or owner. Even the application for mortgage insurance must be filed by the mortgagee. This is in direct contrast with the Farmers Home operation, in which the applicant comes directly to the agency's local office, and the development of an approvable loan is a process of face-to-face negotiation between the local officials of Farmers Home and the would-be home buyer. This format necessarily leads to a much closer understanding of and "feel" for the individual problems and circumstances of each applicant, and a much more flexible situation in which to work out a plan tailored to both his needs and his income and future prospects.

Servicing: In the mortgage insurance system, servicing of insured loans is a function of the mortgagee (or, in the case of a secondary holder, of a local private mortgage-servicing agency on a fee basis). FHA seldom becomes involved until the loan is in trouble, and is not effectively in a position to work out solutions until it accepts either assignment of the mortgage or conveyance of the property securing the mortgage.

Farmers Home, on the other hand, services its individual mortgage loans directly. This keeps the agency in constant touch with each homeowner under an insured loan, and provides the maximum opportunity to initiate corrective measures at the earliest sign that he is getting into difficulty. The avoidance of foreclosure and individual hardship is thus greatly facilitated, as well as the minimization of losses to the insurance fund.

Participation of Local Lending Institutions: In the FHA mortgage insurance system, most loans are originated by local lending institutions. Even if the mortgage is later sold to a secondary holder, it is common for the originating mortgagee to hold the loan on its books for servicing on behalf of the secondary investor. Cumulatively, this volume of business has an important effect in strengthening local lending institutions and enhancing their ability to contribute to the development of the local economy and the solution of housing problems in their areas.

By contrast, the Farmers Home insured loan system effectively substitutes private capital for Federal funds, but it derives this capital largely from the national capital markets. Thus its investors are generally not only remote geographically from the areas served, but equally remote in function from housing and even from mortgage lending as such. They have no reason to take any interest whatever in individual loans, since the basic security for their investment—ostensibly the groups of loans underlying their securities—is in fact the unconditional Government guarantee of their investment as to both principal and interest. Servicing of the individual loans, as noted above, is performed by the Farmers Home Administration, and the ultimate investor has little or no incentive to be con-

[55] Public Law 91-609.

cerned with whether such servicing is done well or poorly. This general format of operation obviously has little or no impact on the practices or mortgage lending capabilities of local lending institutions in rural areas.

The Veterans Housing Program

Early in 1944, with more than 11 million Americans in arms and the peak still a year away, committees of the Congress were engaged in postwar planning for World War II service people. The postwar readjustment of the young men and women then in uniform loomed as a major social and economic problem, especially to those in the Congress and the veterans organizations who remembered World War I and were determined that its harsh aftermath of neglect of ex-servicemen must not be repeated.

When the Congress was considering in 1944 what form of housing credit assistance should be provided for future World War II veterans to help them in their readjustment to civilian life, they were principally influenced by the following considerations:

1. Veterans generally would be young men (and women) who would be establishing households, but as a consequence of long service at military pay levels, most of them had been deprived of a normal opportunity to develop a substantial accumulation of savings.

2. During the war years, civilian workers generally had been employed at favorable pay rates, and because of their accumulation of savings they would be in a commanding position to compete for the limited supply of available housing in the immediate postwar years.

3. It was important that the postwar readjustment effort by designed to stimulate redirection of liquid capital—which had been accumulated during war years when normal investment outlets were restricted—into normal peacetime avenues.

4. Conventional—and even Federal Housing Administration insured Section 203(b) home purchase loans—at that time required equity payments that would preclude many future veterans from obtaining financing.

5. The veterans—with few exceptions—would be first-time home buyers lacking experience in real estate transactions, and should be protected somehow against paying excessive prices for housing.

Development of the Home Loan Guaranty Approach: The Congress sought an approach which would take all these considerations into account, and which in addition would involve a bearable public expense.

Among the alternatives for consideration were the making of direct loans to all eligible veterans, or the payment to each home buying veteran of some sort of grant. To be effective, loans or grants would at least have to equal the lender's probable requirement of an equity payment. With a potential eligible veteran population of 11 to 15 million, the cost of either direct loans or equity grants would have been tremendous and probably not acceptable from the standpoint of the Federal budget despite the popularity of the purpose.

From the Congressional Committee deliberations, after consulting leaders in the home mortgage sector and veterans affairs leaders, there evolved a new concept—that the government would provide a practical substitute for (or the equivalent of) a downpayment by protecting the lender against loss on 100 percent mortgage loans with a guaranty that would operate as to the top portion of the loan. In other words, the guaranty by the Federal Government would serve as the practical equivalent—from a lender's standpoint—of the cash equity investment (downpayment) called for under conventional mortgage lending standards.

Thus the resulting act—the Servicemen's Readjustment Act of 1944, more familiarly known as the GI Bill of Rights—introduced quite a new form of housing credit assistance for the special benefit of veterans. It authorized the Veterans Administration to guarantee lenders against loss on home mortgage loans, up to the lesser of 50 percent of the loan amount, or $2,000. (This figure quickly proved to be too small to be effective in the market, and in the following year it was increased to $4,000.)

Operation of the Guaranty: Under the guaranty concept, the percentage of loan guaranty stays constant throughout the life of the loan, so that as the loan debt is reduced, the amount of the guaranty payable is also reduced. Thus, a 60 percent guaranty (the present statutory percentage, substituted for the original 50 percent coverage in 1950 (Public Law 81–475)) on a loan of $20,000 ($12,000 guaranty) becomes a $9,000 guaranty when the loan is reduced to $15,000.

The lender's only risk of loss under the guaranty concept is the relatively remote possibility that between the time of loan origination and ultimate default and foreclosure, the value of the security might depreciate to the point where it would be less than the nonguaranteed portion of the remaining unpaid mortgage loan. Admittedly, this can happen—as in the case, for example, where the mortgaged property is destroyed by disaster, or in the occasional "ghost town" situation which can arise when a major military base is closed down. Statistically, however, such cases—however painful for those involved—are rare enough to be insignificant in the workings of a nationwide guaranty system involving millions of loans.

The investment of billions of dollars in guaranteed loans by prudent institutional investors is the best evidence that they—as well as the VA—consider such loans to be virtually riskless as a practical matter.

The authority of the VA to guarantee home loans was not restricted by a statutory dollar limitation, either on a single loan or on the total program. Consequently, whenever a lender is willing to accept the VA guaranty as a sufficient protection against possible future loss, the home loan is eligible for guaranty regardless of its amount, provided that amount is not more than the VA's reasonable value determination (described below) for the home, and that the borrower is a satisfactory credit risk and has (or can reasonably be expected to have) the requisite income to repay the loan in accordance with its terms.

Obviously, a $12,500 guarantee on a $62,500 loan provides only 20 percent guaranty coverage, and the full 60 percent coverage is not available on a loan of more than $20,833. In the larger as well as the smaller loans, however, that part of the total loan which is most vulnerable to loss is guaranteed. Thus, loans in the $40,000-and-over bracket are not uncommon in present-day VA experience. Only about 20 percent (in number) of the recent VA loan volume, however, involves loans in excess of $33,000.

Protecting the Veteran from Excess Costs: The concern of the Congress that veterans be protected against paying more for housing than it was worth resulted in a unique statutory stipulation—that no loan would be eligible for guaranty if the purchase price or cost of the dwelling or farm residence to be purchased or constructed with the loan proceeds exceeded the "reasonable normal value" of the property as determined by appraisal. This was later modified to "reasonable value" as determined by the Administrator, and made applicable to the maximum loan amount rather than the purchase price. (The Veterans Administration has found, since this change in the law, that 10.7 percent of the home loans guaranteed involve a cost or purchase price to veterans in excess of its "reasonable value" determination.)

Defaults: VA's guaranty is payable in cash. The law specified that in the event of default in the payment of any loan guaranteed by VA, the holder of the obligation shall notify the Administrator, who "shall thereupon pay to such holder the guaranty . . . " regardless of the condition of the property (if properly insured)—even including its total destruction.

Very early in the program, the Veterans Administration recognized that if the interests of the Government were to be protected when foreclosure of guaranteed home loans was in prospect, some measure had to be taken to prevent the holder of a defaulted loan from acquiring the security property at a foreclosure sale for a nominal bid (or for less than the nonguaranteed portion of the loan) and thereafter selling the property for a price substantially in excess of the nonguaranteed loan amount, resulting in a windfall to the lender at the expense of the Government. It was also recognized that large investors in mortgage loans were reluctant or unwilling to manage and dispose of properties acquired in foreclosure sales as a result of defaulted loans.

To protect the financial interests of the Government and to overcome the investors' potential problems, the Agency provided in the loan guaranty regulations for the establishment of what is called an "upset price" or "specified amount"—that is, the current value which the mortgage holder must attribute to the foreclosed real estate in the accounting incident to the settlement of the VA's guaranty liability.

This practice fully protects the lender, and at the same time protects the VA from having to make excessive payments on account of the guaranty.

VA will pay the lender the difference between the outstanding indebtedness (including accumulated interest and other charges) and the "specified amount," so long as this difference does not exceed VA's guaranty liability. Should the mortgage holder have to acquire the property because none of the other bids is as much as the "specified amount," it may exercise one of the following options:

(1) Notify VA that it intends to retain title to the property and effect a private sale for the best price obtainable. As a practical matter, this is done only if the holder is convinced that it

can realize net cash proceeds in excess of the VA's "specified amount."

(2) Exercise its right under the VA regulations to transfer title to the property to the VA for payment of its "specified amount." This payment, coupled with the guaranty payment, makes the lender whole, and the transaction is concluded. VA then proceeds to recoup its investment by effecting a sale of the property for the best possible price.

Establishment of Debts Against Defaulted Veterans: From the start of the home loan guaranty program, the Veterans Administration took the position that the guaranty benefit is an entitlement to have the loan guaranteed—not an entitlement to have a guaranty paid on the veteran's account with no consequence to the borrower.

On this basis, VA seeks to effect collection of these losses from the defaulted borrower as a matter of regular practice—through negotiation where possible, but, if necessary, through the courts. This practice is in marked contrast to that of FHA (except for Title I loans), where claims against defaulted borrowers are seldom pressed once the insurance claim has been settled.

Because of the legal situation in respect to defaulting mortgagors, the agency goes to great lengths to inform prospective borrowers of their potential indebtedness to the Government should default and foreclosure occur. In addition, when defaults are reported to the agency by the holders of guaranteed mortgages, agency personnel write to or otherwise contact the defaulted homeowner and encourage him and the lender to work out a mutually satisfactory cure of the default. Other supplemental servicing is undertaken as may be necessary, including, in extreme cases, taking an assignment of the mortgage from the holder and working out a solution with the veteran directly.

The Congress is well aware of the VA's guaranty recovery rights and has not seen fit to change those rights. VA itself has not sought any change—believing that the potential of an indebtedness to the Government is an important factor in the low foreclosure experience of VA-guaranteed home loans. Moreover, Congress has vested the agency with broad authority to waive payment of a veteran's indebtedness to the VA where this is warranted by the particular circumstances of the veteran concerned.

During the lifetime of the Loan Guaranty and Direct Loan programs (1944 through FY72), VA has collected from indebted veterans a total of $71.4 million, or about 25 cents per dollar, of indebtedness established against veteran mortgagors.

Use of Fee Appraisers: From the outset of the home loan guaranty program the VA operated with a small salaried staff of appraisal technicians who review, supervise, and supplement the appraisal activity of approved local private appraisers who report to the agency on a fee basis. The fee is paid by the veteran, lender, builder, or seller requesting the appraisal (or by the VA in cases in which the agency itself requests that the appraisal be made). All requests for appraisal must be submitted to the local VA office in the area, and that office assigns the request to an approved fee appraiser. Upon receipt, the appraisal report is reviewed by a salaried technician, and approved or adjusted. Based on the determinations of the VA, a Certificate of Reasonable Value is issued to the requestor.

Coordination with FHA: Because of the obvious similarity in the purposes, if not the techniques, of VA and FHA, it became necessary for both agencies to be aware of and work out consistent or compatible procedures and regulations on matters affecting lenders and builders who are participants in both the VA and FHA programs. As a result of such coordination, the VA has adopted FHA's minimum property standards; approves, for VA purposes, construction materials and contruction techniques accepted for FHA purposes by its engineering staff; and both agencies accept for their respective purposes construction compliance inspections of the other agency.

Direct Loans: There was no direct loan authority until the Housing Act of 1950 (previously cited) was enacted.

A very large volume of guaranteed loan cases (almost 542,000 in 1947 alone) was processed by the Veterans Administration in the first 5 years, but these cases originated almost entirely from metropolitan areas. Members of Congress representing rural areas found that their veteran constituents were being denied the opportunity to purchase homes in their districts because, as a practical matter, private lender financing on a no-downpayment, 4 percent interest (the program rate at that time), long term basis was simply not available in these areas.

In an effort to place rural area veterans more nearly on a parity with veterans in urban areas, the Congress authorized the Veterans Administration to make direct loans on the same terms authorized for guaranteed loans, whenever the VA finds that guaranteed loan financing "is not generally available in any rural area or small city or town" (not near a large metropolitan area), and the veteran

. . . shows to the satisfaction of the Administrator that . . . he is unable to obtain from a private lender in such housing credit shortage area, at an interest rate not in excess of the rate authorized for guaranteed home loans . . . a loan for such purpose for which he is qualified. (38 USC 1811)

Although the original direct loan authorization was temporary, the Congress continued to extend or renew the authority, and existing law no longer contains a cutoff date for making direct loans.

There are 3,094 counties and independent cities in the United States. The Veterans Administration has designated 2,092 of them as wholly eligible for direct loan financing; 254 are partially eligible, and 748 are ineligible. (The VA estimates that only 19.2 percent of the veteran population resides in areas eligible for direct loan financing.)

Referral of Approved Loans: In 1970, VA tried out a program to refer to private lenders those loans already approved for direct financing. Through this process, it was hoped to make doubly sure that direct loans were made only when private financing was not available on reasonable terms to the veteran. This effort resulted in placing about 30 percent of the direct loan cases with private lenders. Because of this success, VA has established a continuing direct loan referral procedure which eliminated some of the delays experienced under the earlier procedures. In fiscal year 1972, VA placed with private lenders 16 percent of the total number of loans referred, in spite of relatively tight market conditions.

Characteristics: Direct loans, because they are restricted to rural areas that lack private financial resources, differ significantly from guaranteed loans in a number of characteristics. The average home purchase price and loan amount is lower than for guaranteed loans. Because direct loans are made in areas of relatively low population density, existing and previously occupied properties dominate direct lending much more than lending under the guaranty program. VA direct loans are closed by fee personnel—attorneys, title companies, etc.

Changes and Improvements in Law Since 1944: The original law has gone through many refinements, improvements, and updatings since the original enactment in 1944. While many of the changes were significant, it would appear that only the first of those listed below represents a conceptual change from the original basic approach.

Reasonable Value: In the original law, it was the purchase price (not the loan) which could not exceed VA's determination of reasonable value. In 1968, this reasonable value determination was changed to apply to the loan, permitting veterans to pay a higher price where they chose to do so and their incomes permitted carrying the larger debt.

Direct Loans: As noted above, direct loans were not authorized in the 1944 legislation but were included in the Housing Act of 1950 in response to a demonstrated need in small areas where lenders could not or were not willing to make home mortgage loans secured by the top-of-the-risk guaranty offered by VA. Originally, the maximum direct loan was $10,000—subsequently increased to a present maximum of $21,000 (with $25,000 allowed in areas "where cost levels so require").

Interest Rates: Originally, and until 1966, the Congress established by law the interest rates which could be charged on VA loans. Under this system, changes to meet market conditions often lagged far behind the need and, in those periods of lag, VA loans were not generally acceptable to lenders. In recognition of the protracted difficulty that this caused for both the veterans and the home mortgage lenders, the VA Administrator was authorized in 1966 to establish interest rates not to exceed those set from time to time under FHA's Section 203(b)(5). Currently, FHA 203 and VA rates are the same.

Increases in Guaranty Limits: The 1944 legislation provided a guaranty for the lesser of 50 percent of the loan and $2,000. The 50 percent factor remained in effect until 1950, when it was changed to 60 percent, where it is today; the maximum guaranty amount was increased in 1945 to $4,000, thence to $7,500, and still later to $12,500, where it is today.

Expiration Dates for Eligibility: Earlier legislation limited the period of time before which eligible veterans must use their entitlement to housing finance. In 1970, expiration dates were dropped, and eligibility was restored for all veterans who had used less than their full entitlement.

Special Provision for Federal Savings and Loans and National Banks: The present law provides that any loan, at least 20 percent of which is guaranteed by the VA, may be made by any national bank or Federal savings and loan association without regard to the limitations and restrictions of any other law relating to ratio of loan to value; maturity of loan; requirement for mortgage or other security; dignity of lien; or percentage of assets which may be invested by such institution in real estate loans.

New Types of Home Financing: In 1970, three new types of home financing were included in the guaranty authorization—mobile homes, condominium units insurable under Section 234 of the National Housing Act, and refinancing of lien indebtednesses on properties owned or occupied by veterans as their homes. The authorization was also expanded to permit direct assistance to paraplegics for specially adapted housing, regardless of the area located.

Earlier Provisions Dropped: Three other provisions of the legislation, no longer in effect, are worth mention.

1. Until veterans of the post-Korean period were made eligible, no fee or premium had been charged. A fee of .5 percent of the loan was established for the new group, to be advanced and included in the mortgage, but this fee was dropped entirely as to all applicants in 1970.

2. From inception until 1953, when it was dropped, a small subsidy or "gratuity payment" (the lesser of 4 percent of the guaranty of $160) was made to the mortgagee on behalf of the veteran and applied to his loan (principal, interest, or both) in accordance with his instructions.

3. Originally, the law required that all loans to be guaranteed must be submitted to, and approved by, VA before closing. This resulted in processing delays and dissatisfaction by both borrowers and lenders. To meet this problem, Congress extended to specific classes of lenders (national banks, savings and loan institutions, insurance companies, etc.) the option of proceeding to loan closing as soon as VA's "reasonable value" determination had been received. These "supervised lenders" were given an automatic guaranty for loans made in accordance with applicable requirements, thus minimizing processing time. In later years, when VA had acquired more experience and had been more adequately staffed, most lenders submitted loan applications for approval and issuance of a guaranty commitment prior to closing—although the "automatic guaranty" procedure still may be used.

Universe of Eligible Applicants and Program Accomplishments: With the restoration of expired eligibilities in the 1970 amendments, all of the World War II veterans and about 1.2 million veterans of the Korean conflict regained their unused entitlements—a total of approximately 13.9 million veterans. Including these, and some who have partially used their entitlements but not more than $7,500, nearly 27 million veterans and eligible service people were eligible for VA loans as of June 30, 1972. The table below provides some indication of the age of the entitlements, from latest to earliest.

Service Era	Number (in thousands) with entitlements
Eligible service people	1,982
Post-Korean Period (11/55 to —)	9,034
Korean Conflict	3,257
World War II	12,698
Total	26,971

Although more than half of the eligibles are World War II and Korean Conflict veterans, logic and recent experience indicate that their housing needs are largely satisfied—only about 16 percent of the fiscal year 1972 loans were to this group.

Loan Authorization: There is no dollar limit in the statute on VA's authority for loan guaranty. Direct loans are limited; $707 million of direct loan authority remained as of June 30, 1972.

Cumulative Business: Through the end of March 1973, VA had made over 8.7 million direct, guaranteed, or insured loans totaling nearly $100 billion. The initial contingent liability for these loans was a little over half that amount (about $53 billion), the balance of the risk being assumed by lenders. At this same time, nearly 4.8 million loans totaling $54 billion were fully repaid, and VA's contingent liability for the remaining loans outstanding stood at about $23.5 billion of the $45.5 billion outstanding.

Fewer than 4 percent of the cumulative number of loans made have been direct loans, and VA has had to pay claims on relatively few of either type—about 3.3 percent of the total number.

Loan Characteristics: Since 1944, about 71 percent of the loans guaranteed by VA have been on a no-downpayment basis. In more recent experience (January-March quarter of 1973), 75 percent of those submitted to VA for approval before closing had no downpayment, and 55 percent of those closed by "supervised lenders" (prior to VA approval) were 100 percent loans.

Cumulatively, loan amounts have averaged $11,500, but rising costs have meant that the trend of this average is upward. In fiscal year

1972, guaranteed loans averaged $22,440 and direct loans $15,180—an increase of 7 percent and 11 percent, respectively, over fiscal year 1971 experience. In the first 3 months of fiscal year 1973, the average guaranteed loan was $23,456, over $1,000 above the 1972 average. Other characteristics of loans in this recent period are expressed in the table below.

Type	% With Down-payments	% With 100 % Financing	Total %
New homes	40	23	28
Existing Homes	60	77	72
	100	100	100
Percent of Total	27	73	100

On an average, the veterans assisted by these loans were applying about 35 percent of income to housing expenses.

Finally, as to the types of lending institutions making these loans: Real estate and mortgage companies have led the field since about 1950, and, in the 2-year period, fiscal year 1971 and fiscal year 1972, made over 65 percent of the total loans guaranteed (compared with their cumulative average of 44 percent). Savings and loan institutions and commercial banks made approximately 30 percent of the loans in the 2-year period; 5 percent came from mutual savings banks, and a smattering from insurance companies, individuals, and others.

Funding: When the Servicemen's Readjustment Act of 1944 became law, and until July 1, 1961, all administrative expenses and program expenditures were paid for from appropriated funds. With the establishment of the loan Guaranty Revolving Fund in July 1961, the Fund became responsible for program expenditures (guaranty payments, payments for properties acquired from lenders, property management expenses, brokers' commissions, etc.), limiting appropriation requests to the funds required for salaries and other administrative expenses. In the 11-year span fiscal year 1962 through fiscal year 1972, there have been no direct appropriations for operations of the Revolving Fund, except for $21,952,332 for insufficiencies resulting from sales of mortgage pool participation certificates sold between 1964 and 1969.

From 1944 through fiscal year 1972, total program expenditures for the Loan Guaranty Program (cumulative), were $4.2 billion. Total receipts from operations, sale of loans, and sale of participation certificates (also cumulative), through June 30, 1972, were $3.5 billion. Thus, total cumulative expenditures exceeded receipts by $672.2 million; however, all but $99.7 million of this amount represented assets in the form of loans, real property, and accounts receivable, which eventually will be liquidated and deposited into the Fund.

Through fiscal year 1972, appropriations for salaries and other administrative expenses were $472 million. This amount, plus an operating loss of $99.7 million, as noted above, results in a total loan guaranty program cost of $571.1 million for the 28-year period. During the same period, the program produced private credit assistance of more than $90 billion for veterans.

This total program cost does not take into account the net gain from direct loan operations of $251.2 million as of June 30, 1972. If such gain is taken into account, a total cost of $320.5 million is derived for the combined operations of the loan guaranty and direct loan program (excluding payments of $403.9 million under the gratuity provision no longer in effect).

Funding the Direct Loan Program: As noted above, Direct Loan Revolving Fund was established in 1950. Cumulatively, through June 30, 1972, income from program operations exceeded expenses and losses by $251.3 million. From time to time, pursuant to specific statutory authorization, direct loan retained earnings have been transferred to the Loan Guaranty Revolving Fund. The total transferred through fiscal year 1972 is $128.2 million. Retained earnings in the Fund on June 30, 1972, were $123.1 million. At the close of fiscal year 1972, there also was a total direct loan availability of $707 million.

Funding by Sale of Loans, Pooling of Mortgages, and Sale of Participation Certificates: In the Loan Guaranty Program, the Veterans Administration in most instances effects the sale of a property acquired from a lender who foreclosed a guaranteed loan (hence the term "acquired property") by taking back a note and mortgage or deed of trust from the purchaser for the difference between the sales price and the purchaser's downpayment, if any. These loan assets are called vendee accounts. These accounts are offered for sale to private investors from time to time under a Repurchase Agreement which obligates the VA to "buy back" the loan, if and when a serious default develops at the same price (percentage of par) at which the loan was purchased by the investor initially. Through this technique, the Loan Guaranty Revolving Fund has developed receipts amounting to $1.3 billion. The premium realized on loans so sold was $9.1 million through fiscal year 1972.

In the Direct Loan Program, the VA is authorized to sell loans in its portfolio for such prices as the Administrator determines to be reasonable under prevailing mortgage market conditions, and to guarantee such loans, when sold, up to 60 percent of the loan amount, or $12,500, whichever is less. From 1950 through fiscal year 1972, VA sold directly to investors $728.1 million of its direct loan portfolio.

In addition to the foregoing, VA has the authority to set aside direct loans and vendee accounts in mortgage pools with the Federal National Mortgage Association and other Government agencies. Under the mortgage pool arrangement, VA retains ownership and servicing of the loans set aside. Principal and interest collections from loans set aside are deposited with GNMA (Government National Mortgage Association) as Trustee for the various Trusts used for the retirement of participation certificates and for payments of interest to participation holders.

With respect to the loans thus set aside in trust, interest income has not fully covered interest expense on the participation certificates. This shortage has been covered by appropriations in the amount of approximately $22 million.

Program Summary: In the main, the objectives of the Veterans Housing Program today and the means of accomplishing them are still fully compatible with the original concepts. The following summary of the outstanding features of the system is as current now as when it was issued by the then-VA Administrator in a 1954 report:

> The salient features of the loan guaranty machinery may be summarized under three main headings.
>
> The first covers those characteristics of the loan that provide particularly advantageous financing terms to veterans. The distinctive elements of the GI loan from that viewpoint are: (1) A low, effective interest rate; (2) Long loan amortization periods; (3) Absence of a requirement for initial equity; (4) Absence of a charge or premium for the guaranty or insurance; (5) Prohibition of mortgage brokerage commissions; (6) Option of accelerated repayment without penalty; (7) Various beneficial provisions of the VA regulations designed to assist veterans in temporary straits which are incorporated into the loan contract by reference.
>
> The second related to the reasonable value rule, which requires that the purchase price or construction cost of property to be acquired with the aid of a GI loan may not exceed the amount determined to be the reasonable value by a proper appraisal made by the VA. This 'value protection' has been buttressed by the incorporation of minimum property requirements which set forth quality standards for dwellings.
>
> The third feature comprises those terms of the guaranty contract that make the GI loan plan attractive to lenders and holders. The elements are:
>
> 1. The incontestability of the guaranty or insurance certificate;
> 2. The prompt cash settlement of claims filed after default;
> 3. The opportunity to adjust the terms of the loan contract within statutory limitations, according to the agreed wishes of the veteran and holder and the consent of the VA, in order to prevent or cure a default or to avoid foreclosure;
> 4. The payment of interest on amounts owing until date of foreclosure sale or conveyance;
> 5. The option of conveyance of acquired security to VA or its retention under a net settlement plan, whenever the value of the security exceeds the unguaranteed portion of the loan;
> 6. The assumption of risk of loss and of waste to security property by VA from the date of notification of election to convey;
> 7. The maintenance of the full initial guaranty ratio irrespective of any damage or destruction to the improvements to real estate at or prior to the time of foreclosure or other liquidation, provided hazard insurance coverage has been maintained as required by VA regulations;
> 8. The allowance of all reasonable foreclosure costs in claims filed;
> 9. The acceptance by VA of the same quantum and quality of title as acquired by the holder.

There is one major difficulty affecting the current program which is not related to the basic machinery of the plan. This is the rapid increase in the cost of housing, especially during the last decade, which necessitates larger mortgage loans with the result that many lower and lower-middle income veterans cannot afford to take on the necessary monthly payments. Nevertheless the existence of these 100 percent, 30-year, guaranteed loans continues to make homeownership a reality for many thousands of veterans each year, so long as the VA interest rate bears some reasonable relationship to the market.

Credit Aids for New Communities

Since 1965, the Congress has authorized an accumulation of different forms of credit aids to encourage the development of "new towns" or "new communities."

These terms have been used in somewhat different senses, but basically they refer to a development larger than a typically large subdivision, with the self-contained features of a city such as schools, shopping areas, recreational and cultural facilities, a proper balance of housing for all income levels, and job producing activities through business, commerce, or industry. Any employment outside the new community must be nearby and reasonably accessible. A new community need not be remote from existing cities, and can adjoin or be within an existing urban area if it meets the other standards.

A basic feature of a new community is planning—both of the development itself and its relation to the comprehensive planning by the appropriate public planning body for the area.

Federal assistance for the development of new communities follows decades of increasing interest in them as alternatives to simply revitalizing cities and extending suburbs to take care of the rapidly increasing population of the United States. The problems giving rise to special Federal credit aids for new communities were expressed by the Congress in its finding that:

> . . . desirable new community development on a significant national scale has been prevented by difficulties in (1) obtaining adequate financing at moderate cost for enterprises which involve large initial capital investment, extensive periods before investment can be returned, and irregular patterns of return; (2) the timely assembly of sufficiently large sites in economically favorable locations at reasonable cost; and (3) making necessary arrangements, among all private and public organizations involved, for providing site and related improvements (including streets, sewer and water facilities, and other public and community facilities) in a timely and coordinated manner.[56]

Before this Federal assistance, several score developments had been classified as actual "new towns." It was also true that the Government had built or assisted a few such entities in the past, such as the three "greenbelt" towns and the towns needed at AEC installations.

Because the housing construction itself in a new community could be assisted under the regular FHA programs, the credit aid sought was primarily for the development of the site from raw land and the installation of utilities. As will be shown, other structures came to be assisted also.

Mortgage Insurance for Land Development

In 1965, HHFA proposed a new mortgage insurance program for land development needed by new communities, but the Congress considered it too ambitious without further study,[57] and enacted a truncated program of "land development."

Notwithstanding that change, the program authorized (Title X of the National Housing Act) helped meet a great need of subdivision and smaller residential builders. Until then, there had been no Federal credit aid for the development of raw land into building sites. Accordingly, developed land for home builders, especially small builders, became extremely scarce, and the price of land rose proportionately more than any other item of housing construction. The limited number of entrepreneurs developing sites could charge very profitable amounts for land.

By the beginning of last year, 27 mortgages had been insured under the new Title X, totaling about $43 million, and involving over 21,000 lots. These were land development rather than new community projects, and the whole program did not constitute as extensive an operation as might have been expected. Land development is inherently speculative, and the statute prohibited mortgage insurance unless the project represented a good insurance risk. This made processing through regular FHA procedures difficult. Also, the mortgage insurance was quite limited in amount by its fixed ratios to value and cost. It could not exceed (1) 75 percent of the value of the completed land development; nor (2) the total of 50 percent of the land value before development, plus 90 percent of the cost of development.

The new communities proposal first made by HHFA in 1965 was made a part of the Title X mortgage insurance authority by the Demonstration Cities and Metropolitan Development Act of 1966. To be eligible, a proposed new community had to be of such size and scope as to make a substantial contribution to economic growth of the area in the form of economies in provision of improved housing sites; adequate housing for those employed in the area; maximum accessibility to industrial and other employment centers and to commercial, recreational, and cultural facilities in or near the new community; and maximum accessibility to any major central city in the area. The development had to be approved by the local governing body.

This was the rhetoric of new communities, but so long as the program was restricted to mortgage insurance it remained essentially land development, as described above.

Federal Guarantee

Recognizing the ineffectiveness of mortgage insurance to generate an adequate volume of credit for new community development, HUD recommended in 1968 an entirely new additional assistance program based on the Federal guarantee of bonds and other obligations issued by the private developer of the new community. This meant that the Government would guarantee, backed by the full faith and credit of the United States, the payment of the principal and interest on the obligations of the private developer, if

[56] Section 710(e) of the Housing and Urban Development Act of 1970.

[57] Report of House Committee on Banking and Currency on the Housing and Urban Development Act of 1965 (H. Rept. 365, 89th Congress, 1st Session), pp. 15 et seq.

sold to investors or at public sale as approved by HUD after it had approved all other prerequisites with respect to the development. That program, which included certain supplemental grants for public utilities and other facilities, was enacted as Title IV of the Housing and Urban Development Act of 1968.

In reporting on the legislation, the Senate Committee on Banking and Currency emphasized the obstacles to financing without the potent guarantee assistance,[58] saying that a single large project could require as much as $50 million in borrowed funds at one time for a relatively new type of investment. Also, during an extended planning and development period, large expenditures would be necessary for debt service, overhead, and taxes, while income would not start for several years. The guarantee, said the committee, would make investors, including those not interested in the usual mortgage investment field, willing to provide financing geared to the realities of internal cash flow in new community developments.

This guarantee program was reenacted with broader scope and further supplemental financial aids, as discussed below, in Title VII of the Housing and Urban Development Act of 1970. The major functions in the program were placed under a new "Community Development Corporation" in HUD, with a five-man board of directors, including the Secretary of HUD and three persons appointed by him. One director, to be appointed by the President with the advice and consent of the Senate, serves as General Manager of the Corporation.

A new community project under the guarantee program includes the development of land and the provision of utilities and other facilities for residential, commercial, industrial, or other uses. It also includes the construction of buildings to be owned and maintained by the residents of the community under joint or cooperative arrangements. The development has to meet the same standards as under the earlier program, including requirements concerning planning and a substantial provision of housing for low and moderate income persons. It must also assist the local home building industry and encourage its broad participation, particularly the small builders.

The amount of obligations which could be guaranteed for a project was increased to the sum of 80 percent of the value of the real property before development, and 90 percent of the actual cost of land development.

The 1970 Act extended the guarantee program to locally authorized public agencies and permitted their obligations to be issued up to 100 percent of those items, but provided that such obligations could not be guaranteed if exempt from taxation. Grants by HUD are authorized to compensate the public agencies for loss of the interest rate advantage of tax exemption, but State legislation normally would be required to make the obligations taxable.

HUD (through the Community Development Corporation) is authorized to establish maximum interest rates and other terms of the obligations it guarantees, and to charge fees for insurance looking toward a self-sustaining revolving fund.

Guaranteed obligations are authorized up to $500 million, and the maximum for each development is $50 million.

The changes made by the 1970 Act were set in the context of an extensive legislative statement on national urban growth policy. That statement established standards for the development of such a policy and required the President to submit a Report on Urban Growth every 2 years, beginning in 1972, giving prescribed information on urban growth and recommending any legislation considered desirable.

Federal Aids Supplemental to the Federal Guarantee

Grants for Public Facilities: Where grants under any Federal program are being furnished for public utilities or certain other facilities to be used as part of the new community development, then HUD can furnish supplemental grants up to 20 percent of the cost of the particular projects (but combined Federal grants cannot exceed 80 percent of that cost). These projects can include facilities for water and sewer systems, roads, mass transportation, airports, public health, public libraries, recreation and open space, and public education. This authority was extended to grants for private, as well as public, developers by Section 7 of a Joint Resolution in 1971 (Public Law 92–213). Funds have been appropriated for these grants.

Loans to Pay Interest on Guaranteed Obligations: To encourage further credit for new community development in view of the long period before project income starts, HUD (through the Community Development Corporation) can lend funds to the developer to assist in making interest payments on obligations issued for the

[58] Report of Senate Committee on Banking and Currency on the Housing and Urban Development Act of 1968 (S. Rept. 1123, 90th Congress, 2nd Session), p. 48.

project. This can apply to the interest charges until project income is sufficient for payment, but not exceeding 15 years. The loans by HUD carry an interest rate equal to the current yield on outstanding obligations of the United States; appropriations are authorized for these loans but have not yet been made.

Public Service Grants: There is authorization for certain public service grants to public agency developers or public bodies having responsibility for furnishing services to meet the needs of the residents of the development. The grants cannot exceed the cost of providing these services during an initial period, not exceeding 3 years, prior to completion of permanent arrangements for providing the services.

Appropriations are authorized for these grants, but have not yet been made.

Special Planning Grants: Until June 30, 1975, HUD is authorized to enter into agreements with new community developers to furnish funds up to two-thirds of the cost of planning a new community, including planning relating to its public purposes and the use of new and advanced technology. These agreements can be entered into only with respect to a new community which has already been actively considered for approval. In the case of a private new community developer, the assistance can only be for planning the project's special purpose objectives beyond normal market, financial, and engineering feasibility.

Appropriations are authorized for these grants but have not yet been made.

Program Development

Since the availability of the guaranty aid, there has been great interest in the development of new communities. Substantial time elapsed, however, before the first guarantee commitment occurred in February, 1970, because of the novelty of the program as well as the size of each project undertaking. Unique controls had to be developed to assure protection of the Government's financial interests, as well as the preparation of extensive new types of documents on behalf of developers. A typical "project agreement" between the United States and a developer is more than 100 pages in length, and the typical "Indenture of Mortgage and Deed of Trust" for the debenture financing by a developer is about the same length.

Fourteen new communities have received a guarantee commitment from HUD, varying in amounts up to the maximum $50 million. The total amount of these guarantees is about $300 million.

Federal Tax Devices to Generate Housing Credit and Funds

Several Federal tax provisions have had an enormous impact in generating housing credit and funds, and should be discussed briefly in this Part. However, it is beyond the scope of this study to attempt to furnish a detailed legal or economic analysis of the impact of these several tax measures. Also, the major current tax issues have been the subject of recent studies and articles in depth. Worthy of special attention are: "Federal Income Tax Incentives in Low- and Moderate-Income Rental Housing" by James E. Wallace [59]; the subjects on tax incentives in the Report of the Secretary's Task Force on Improving the Operations of Federally-Insured or Financed Housing Programs [60]; and the HUD staff memorandum on "Syndication of Equity in Section 236 Projects" by G. Richard Dunnells, January, 1972.

This study does not discuss the homeowner's income tax deductions for real estate taxes and mortgage interest payments, which are sometimes identified as Federal subsidies to homeowners that discriminate against tenants. (See "Federal Housing Subsidies" by Henry Aaron,[61] alleging about $10 billion annual subsidy to homeowners.) Those deductions are not designed to generate credit, nor to assist housing as such. The same deductions are available to owners of rental properties and, to the extent an equity issue may exist, it involves the relationship of rentals to landlord profits.

The following general conclusions can be expressed with respect to all of the major tax incentives for housing credit:

1. They have been highly successful in generating housing credit, apart from any questions as to the merits of the measures in terms of dollars lost to the Treasury.

2. There is a prevalent belief, with respect to each tax incentive, that it costs the Government more in actual dollars ultimately lost than cash payments would have cost if appropriately

[59] "The Economics of Federal Subsidy Programs, A Compendium of Papers Submitted to the Joint Economic Committee, Congress of the United States, Part 5—Housing Subsidies," Oct. 9, 1972, Joint Committee Print.

[60] "Multifamily Housing," "IV-Federal Tax Laws and the Sponsorship/Ownership of Subsidized MF Housing"; and Appendices A and C.

[61] "The Economics of Federal Subsidy Programs," supra.

made to accomplish the same objective. The Treasury Department in particular has consistently taken the position, often shared by the Administration at the time, that it is wasteful to furnish subsidy for any purpose through income tax exemption in place of direct subsidy. The reason given is that the amount of tax exemption bears no relation to the amount of benefit necessary to give in the particular case. A further major inequity results from the fact that the value of the exemption (and the resulting loss to the Government) is correspondingly greater as the income of the beneficiary is higher.

3. Generally, the vested interests in the status quo for each major tax incentive have made infeasible its complete repeal, or the substitution of another type of incentive. (The repeal of the tax exemption of income from shares in Federal savings and loan associations (by virtue of the Public Debt Act of 1942) might be regarded as an exception to this.)

4. Excessive financial benefits given as tax incentives cannot properly be termed abuses by the taxpayer, as it must be presumed that the statute intends full advantage to be taken of the benefits it affords.

Tax Exemptions of Local Public Agency Obligations

From the beginning of the low rent public housing program under the United States Housing Act of 1937, it has had special Federal tax advantages (in addition to the exemption of housing projects and local agency obligations from taxes under State laws), especially the following exception in that act (Section 5(d)):

> . . . Obligations, underlying interest thereon, issued by public housing agencies in connection with low-rent-housing or slum clearance projects, and the income derived by such agencies from such projects, shall be exempt from all taxation now or hereafter imposed by the United States.

The Federal tax exemption of income from local agency bonds and other obligations was one of the factors making it possible to use private, instead of public, funds in financing local public housing projects. This financing device was of historic significance to public housing and was of enormous magnitude in the whole field of municipal and local agency financing.

Some moves have been made in the past, particularly in the Treasury Department, to seek the repeal of this exemption, on the ground it is a wasteful form of subsidy that is especially undesirable because of the Federal guaranty of the same exempted obligations. Municipalities and their representative organizations have effectively opposed inroads on the tax exemption of any local agency obligations through fear that any change would be the opening wedge for abolishing tax exemptions of municipal obligations generally. The potential force of municipal opposition has been adequate to prevent effective steps to modify or repeal the above exemption.

Real Estate Investment Trusts

A small number of real estate trusts have existed since the last century, based on the Massachusetts real estate trust with transferrable shares purchased by the general public. However, it was not until the enactment in 1960 of an amendment to the Revenue Code, providing special tax treatment for real estate investment trusts, that the industry came into existence as we know it today. That amendment (Section 10(a) of Public Law 86–779) [62] was passed by the Congress partly on the basis that it would broaden the source of funds for investment in housing and other real estate developments.

This tax amendment provided substantially the same tax treatment for real estate investment trusts that the laws had provided for about 20 years with respect to regulated investment companies. If they distributed 90 percent or more of their ordinary income, they were taxed only on their retained earnings, and the distributed earnings were taxed only to the shareholders.

Thus, the most forceful argument for the amendment was one of equity—that is, it gave to real estate trusts specializing in investments in real property and real estate mortgages the same advantages as regulated investment companies specializing in investments in stock and securities. For tax purposes, the trust could exclude the amount of its earnings distributed to individuals, if 90 percent or more of its ordinary taxable income (excluding certain capital gains) was so distributed.

The advantages of the real estate investment trust provision included, as intended by the Congress,[63] the spreading of the risk of loss by the greater diversification of investment obtained through a pooling arrangement and the opportunity of small investors to secure advantages normally available only to those with larger resources.

[62] Adding "Part II—Real Estate Investment Trusts" to Subchapter M of Chapter 1 of the Internal Revenue Code of 1954.
[63] House Committee on Ways and Means (H. Rept. 2020, 86th Congress, 2nd Session), p. 3.

The amendment restricted this "pass-through" of income for tax purposes to what was clearly passive income from real estate investments, as contrasted to income from the active operation of businesses involving real estate. Specific requirements were imposed on the eligible real estate investment trust to assure that most of its income excluded for tax purposes came from mortgages, rentals, and other receipts relating to real property. The beneficial ownership of the trust had to be held by 100 or more persons.

This tax advantage quickly spawned the creation of real estate investment trusts, bringing the total number in 1968 to 50, which had assets of about $1 billion.[64] Most of those trusts specialized in investment in real property, while only a few specialized in construction and development. It was from that time until the present that the industry mushroomed, so that there are now more than 190 trusts with more than $14 billion in assets and hundreds of thousands of individual shareholders. One cause of this sudden increase was the tight money period in 1969 and 1970 for traditional lenders.[65]

Although the growth of these trusts has been phenomenal since the tax amendment, their investments have not been primarily in long term mortgages on housing or other properties, as expected. The trend of investment has been away from real property and toward construction and development. Only 13 percent of investments are now in long term mortgages, compared to 59 percent in construction and site development.[66] The long term loans made are generally conventional mortgages on apartment buildings or commercial properties.[67]

The trusts specializing in construction and site development ("short term mortgage trusts") are criticized as being in the development business or private ventures, as distinguished from being sources of mortgage credit. Typically, the trust may borrow from a commercial bank at close to the prime rate and realize a yield on short term construction loans as high as almost 13 percent.[68] It is contended that this is not consistent with the spirit of the 1960 tax amendment, which prohibits holding property primarily for sale in the course of business and limits certain short term operations.

[64] "Real Estate Investment Trusts: An Industry Profile," REIT, 1101 17th St., N.W., Washington, D.C.
[65] Ibid.
[66] Ibid.
[67] Ibid.
[68] "Audit's Realty Trust Review," Vol. IV, No. 7.

National Housing Partnerships

Throughout the history of the housing agencies, their legislative proposals seldom ventured substantially into the field of tax law, but HUD did so in proposing authority for creating National Housing Partnerships. It had been recommended by the President's Committee on Urban Housing (the Kaiser Committee), and was enacted as Title IX of the Housing and Urban Development Act of 1968. This new legislative authority had almost no legal significance from the standpoint of tax law. Basically, it provides for federally chartered private corporations (but with 3 of 15 directors appointed by the President) to act as catalysts in mobilizing private housing investment, for low or moderate income housing, through the incentive of existing tax advantages. Although more than one corporation was authorized, to preclude any undesirable monopoly, no more than one was contemplated at the start. The corporation in turn was authorized to form a limited partnership—the corporation acting as the general partner on a national basis, with the advantages of scale operations and continuity.

The tax advantage is received through the limited partnership which was formed as provided in the law, and is similar to some small limited partnerships previously existing. Each limited partner (who also owned stock in the corporation) receives a tax advantage in proportion to his investment in the partnership (inasmuch as he is part owner in each venture to that extent). At the same time, the limited partner has no liability for debts beyond his investment, unlike the usual sponsor or the general partner. Neither does he have any responsibility for the construction and operation of the housing, which is left to the general partner.

The principal tax advantage of the limited partner is his right to deduct his proportionate losses in the partnership from his profits from other sources in computing his Federal income tax liability. Normally, partnership losses for that purpose consist of operating losses plus the amount of "accelerated depreciation" allowed in the law. Instead of merely permitting a loss credit on the basis of a steady rate of depreciation ("straight-line depreciation") over the economic life of the property (such as 40 years), accelerated depreciation allows the loss to be taken at greater amounts during the early years. This can be 200 percent of straight-line depreciation in the case of new residential construction.

Upon sale of the project, a tax must be paid on the portion of the sale price that exceeds the depreciated value. That amount, however, is taxed at the lower capital gains rate (subject, in addition, to certain recapture provisions as explained in Appendix A). This tax advantage, of course, has a proportionately greater value for taxpayers in the higher income brackets.

In accordance with the 1968 act, the national partnership operates through equity investments in local partnerships or other local sponsors. These investments vary from 25 percent to 90 percent of the equity in each project.

The National Housing Partnership got under way notwithstanding the shortage of investment funds during 1969 and 1970. At the beginning of this year, the Partnership was committed to participate in 116 projects with a total replacement value of $370 million. Agreements for working capital and other initial cash requirements totaled $1.7 million, and for equity interests $26.7 million.

The Partnership projects are almost all under HUD mortgage insurance programs, and most of the projects are under the section 236 subsidized rental program. With the current freeze on new section 236 commitments, however, a few more projects with conventional mortgage financing are anticipated this year.[69]

Tax Reform Act of 1969 and Equity Syndication

"Equity syndication" is the technique that has developed, primarily under the section 236 rental housing insurance program, to sell to passive equity investors the income tax advantages in connection with sponsoring a project. That technique existed prior to the Tax Reform Act of 1969, but developed into its present scale of operations within the framework of that Act and after a new investment vehicle had emerged patterned after the National Housing Partnership.[70]

The 1969 Act constituted a milestone revision of the Revenue Act provisions relating to new and rehabilitated housing. It was designed to cut back primarily on the use of accelerated depreciation for tax shelter while channeling more private investment into housing production through the use of preferential tax incentives. It permitted continued use of the 200 percent accelerated depreciation (discussed above) for new residential properties while cutting back this percentage for commercial and industrial structures, and to a lesser degree for existing residential structures. The Act also permitted a taxpayer to elect to amortize rehabilitation expenses incurred with respect to low income rental housing (as defined) under the straight-line method in the short period of 5 years. Also, stricter rules for depreciation recapture in the event of sale were applied to conventional housing development.

These tax incentives for housing were motivated by a recognition (shared by the Treasury Department) that the availability of the tax shelter was essential to attracting adequate amounts of private equity capital to achieve section 236 production.[71] Without a tax incentive there would be little section 236 development under profit-motivated sponsorship because of the maximum 6 percent dividend.

Appendix A, entitled "Tax Reform Act of 1969" (a HUD staff memorandum) explains the changes made by that act, and thus indicates the current provisions now used in equity syndication, as well as the earlier provisions which had applied to rental housing for many years.

New construction and rehabilitation projects under the section 236 program constitute the most preferred form of real estate investment from the standpoint of tax incentives, and, as such, attract a degree of equity investment that would not otherwise be available to housing. That results from a combination of:

1. The preferred position given to the projects in the Revenue Act itself.

2. The greater potential of a section 236 project for tax shelter than a conventionally financed project because of larger (90 percent) debt (which gives a greater ratio of depreciation dollar losses to equity dollars invested).

3. The availability of the limited partnership device, which is a convenient instrument of ownership for permitting tax losses that are in excess of the sponsor's needs to be sold to limited partners as passive investors.

4. To some extent, the Federal subsidy for reducing rentals, which helps assure project occupancy.

The extent of the tax incentive under this form of equity syndication is shown by a detailed prototype explained in the article by James Wallace (mentioned in footnote 52) at page 679 of the Committee Print. For a typical section 236

[69] National Corporation for Housing Partnerships staff.

[70] HUD staff memorandum on "Equity Syndicator," by Richard Dunnells, see text supra, p. 2.

[71] Ibid.

project involving new construction, investors in the 50 percent income bracket who are able to use the tax losses would expect an annual after-tax return of 15 percent. The investors in the 70 percent bracket would, of course, obtain larger after-tax returns. The developer-sponsor would obtain equity investments equal to 15 percent of the mortgage amount and extract a fee of about 12 percent of the mortgage amount (but out of equity funds, not from mortgage proceeds).

The facts given by Mr. Wallace for a typical section 236 rehabilitation project show a mortgage amount of $2 million and equity contributions by investors of $500,000. (See page 685 of above Committee Print.) These investors receive a tax shelter of $400,000 a year (worth $200,000 a year to 50 percent bracket investors) for 5 years. The typical developer's cash cost is $60,000 and he pays a $100,000 fee to the tax shelter broker. He retains a "fee" of $340,000, or an amount equal to 17 percent of the mortgage amount.

Equity syndication has reached the stage where SEC-registered limited partnerships sell limited partner interests in the open market. With ownership so far removed from project operations, questions have been raised as to the effect of that on project management. The limited partners' only interest in operations at any time is to prevent foreclosure. Their tax advantage and all interest ends within 20 years, although mortgage operations would normally continue for another 20 years.

* * * * * *

Although the above tax incentives for generating credit and funds for housing are extending tax benefits as intended by statute, the great loss of tax revenue, as well as certain inequities, are now a matter of concern to the Department of the Treasury, which has issued "Proposals for Tax Change," April 30, 1973, that includes proposed limitations on some of those tax benefits.

Coordination of Federal Policy Toward Housing Credit

Brief Summary of Major Organization Developments in HUD

The establishment of a Department of Housing and Urban Development as the eleventh Cabinet Department of the Executive Branch was the outgrowth of a long series of actions and developments reflecting the growing national concern over the problems of housing and the urban environment, and the increasing involvement of the Federal Government in the development of national policies and the exercise of national leadership in this area.

In the 1930's, a series of major Congressional actions gave rise to new agencies and new forms of Federal activity connected with housing—notably the establishment of the savings and loan system and the Federal Home Loan Bank Board; the development of mortgage insurance and the establishment of the Federal Housing Administration; and the initiation of subsidized low rent public housing and the creation of the United States Housing Authority.

In 1942, the principal housing programs and agencies of the Government were brought together in a single agency for the first time, through the establishment by the President of the National Housing Agency. This action was taken under the temporary war powers of the President, and was aimed primarily at the more effective prosecution of the war effort.

In 1947, the temporary war agency was replaced by a permanent Housing and Home Finance Agency, brought into being through the exercise of the peacetime reorganization powers of the President.

In 1950, the Federal National Mortgage Association (then in the Reconstruction Finance Corporation) and the Community Facilities Service (then in the General Services Administration) were transferred by Presidential reorganization action to the HHFA.

Throughout this period, and through the balance of the 1950's, the Congress greatly increased the activities and responsibilities of the Federal Government's housing agency. In addition—through the assignment of such functions as urban renewal and grants for comprehensive urban planning—the Congress manifested an evolving—though not specifically declared—view of the agency as its primary instrument for obtaining advice and for articulating policy in connection with urban problems in the broad view, reaching beyond the boundaries of housing as such. This expanding perspective is evident in the opening language of the first major policy statement enunciated by the Congress in this field, in the Housing Act of 1949, which, although styled a "Declaration of National Housing Policy," begins as follows:

> The Congress hereby declares that the general welfare and security of the Nation and the health and living standards of its people require housing production *and related community development* sufficient to remedy the serious

housing shortage, the elimination of substandard and other inadequate housing through the clearance of slums and blighted areas, and the realization as soon as feasible of the goal of a decent home *and a suitable living environment* for every American family, *thus contributing to the development and redevelopment of communities* and to the advancement of the growth, wealth, and security of the Nation. (Emphasis added.)

In 1961, the President recommended legislation to establish a Department of Urban Affairs and Housing. In early 1962, when it appeared unlikely that this bill would reach a vote in the House of Representatives, the President submitted a Reorganization Plan to the same general effect, with technical differences due largely to the limitations on reorganization power as compared with what could be accomplished by legislation. The Congress, however, did not permit the Plan to take effect.

In March 1965, the President, in a special Message to the Congress on Problems and Future of the Central City and its Suburbs, declared: "Our urban problems are of a scope and magnitude that demand representation at the highest level of government."

Shortly thereafter, legislation was recommended to the Congress to create a Department of Housing and Urban Development. After debate and amendment, the bill was passed by the Congress and signed into law September 9, 1965. By its terms, it became effective 60 days later, on November 9, 1965 (Public Law 89–174, 42 U.S.C. 3531).

In establishing the Department, the Congress characterized its action and intentions as follows:

DECLARATION OF PURPOSE: Sec. 2. The Congress hereby declares that the general welfare and security of the Nation and the health and living standards of our people require, as a matter of national purpose, sound development of the Nation's communities and metropolitan areas in which the vast majority of its people live and work.

To carry out such purpose, and in recognition of the increasing importance of housing and urban development in our national life, the Congress finds that establishment of an executive department is desirable to achieve the best administration of the principal programs of the Federal Government which provide assistance for housing and for the development of the Nation's communities; to assist the President in achieving maximum coordination of the various Federal activities which have a major effect upon urban community, suburban, or metropolitan development; to encourage the solution of problems of housing, urban development, and mass transportation through State, county, town, village, or other local and private action, including promotion of interstate, regional, and metropolitan cooperation; to encourage the maximum contributions that may be made by vigorous private homebuilding and mortgage lending industries to housing, urban development, and the national economy; and to provide for full and appropriate consideration, at the national level, of the needs of the people who live and work in them.

Relationship of Organization to Coordination of Housing Credit Policy

It was a recurring theme in many of these major reorganizations that there should be improved coordination of Federal credit policy with regard to housing on a Government-wide basis, and that such reorganizations would contribute importantly to that end. This was argued in support of the establishment of the permanent HHFA in 1947. As noted earlier, it was one of the bases for transferring the Federal National Mortgage Association from RFC to HHFA in 1950. The same idea was emphasized by the President's Advisory Committee on Government Housing Policies and Programs in 1953.

Again in connection with the legislation which finally established the Department of Housing and Urban Development in 1965, it was predicted that giving these programs "a voice at the Cabinet table" would help to secure greater recognition for the credit needs and problems of the housing economy, and to facilitate the development of a consistent approach and policy toward Federal participation in the housing credit market.

The unfortunate but unmistakable fact appears to be that these objectives, however laudable, have never been achieved and remain today as remote as ever. The organizational moves which it was hoped would bring them within reach did not, in fact, have that effect.

Two kinds of cause may be recognized for this failure.

In the first place—even though construction is the largest single activity in the national economy, and residential construction the largest element in total construction—housing credit needs never have been viewed at policymaking levels in Government as demanding priority of consideration as against such broader national concerns as inflation, budgetary balance, and the national debt.

The decisionmaking centers with respect to credit policy in the Executive Branch were, and are, the Treasury, the Office of Management and Budget, and the Council of Economic Advisers. The Treasury approched credit policy from the standpoint of revenues, debt management, and the overall economic situation—a perspective in which housing credit needs were a secondary, even if important, consideration. The OMB approached credit policy from the standpoint of total budgetary impact and its effect on the budget surplus or deficit—a perspective in which housing credit needs were a secondary, even if important, consideration. The Council approached credit policy from the point of view of economic growth, full employment, and the avoidance of excessive inflation or deflation—and, once again, in this perspective housing credit needs were seen in a secondary role, except at such times as housing was emphasized for one of the broader purposes mentioned.

The Federal Reserve Board, even though its interests lie mainly in the area of monetary policy, also played an important role in major credit decisions. This has led the Board to take an active interest in housing matters from time to time. However, the Board does not cultivate intimate relationships with the operating departments and agencies of the Government, even when it has occasion to interest itself in their affairs. The Board generally has had its own housing economists and, not infrequently, its own housing policies. Certainly, it was not within the capability of the Housing Administrator or the Secretary of HUD to exercise much coordinating influence over the policies or decisions of the Board.

A second cause lies in the fact that, much as the idea has been discussed, there never has been an official (other than the President) who was in a position either to evaluate or to speak authoritatively for housing credit programs and policies Government-wide.

Thus the Home Loan Bank Board was brought into the temporary National Housing Agency (in 1942), and retained in the permanent Housing and Home Finance Agency (since 1946), in large part to give the Administrator a broader base for policy formation and hence a greater voice in decisionmaking. But the Board was taken out of the Agency again by legislation in 1955 (largely at the urging of the savings and loan industry) and reconstituted as an independent agency, the Federal Home Loan Bank Board, which promptly resumed its traditional arms-length relationship to other Executive agencies.

Similarly, the Federal National Mortgage Association was transferred to HHFA in 1950, in part for the stated purpose of improving coordination between its activities and those of related Federal housing programs. But FNMA's secondary market functions were removed in 1968, not only from the Department but from the Federal Budget and, nominally at least, from the Federal Government.

The GI housing program of the Veterans Administration was naturally seen very soon to be basically a program dealing in housing and housing credit, and the anomaly of conducting such a program wholly outside the Government's housing agency was clearly perceived. So, too, were the many inconsistencies and confusions that arose out of simultaneous FHA and VA operations in the same communities and often in the same housing developments. But while there was much discussion of these matters, the preference of the Congress and of the veterans' organizations for keeping all major programs of veterans benefits together in VA effectively prevented any action.

Similarly, the Farmers Home Administration, which from a small beginning grew into a major housing agency with a nationwide program extending into towns of substantial size, continued on its independent way in the context of other farm and agricultural programs in the Department of Agriculture.

With the establishment of HHFA, a special effort to coordinate housing and housing credit policies across the Government was made with the creation of the National Housing Council. The Council was intended to provide a means ". . . for promoting the most effective use of all the housing functions of the Government, *for obtaining consistency between these functions and the general economic and fiscal policies of the Government . . . etc.*" (Emphasis added.) (Message of the President Accompanying Reorganization Plan No. 3 of 1947.) With this end in view, the Council included (in addition to the Administrator as Chairman and the two HHFA Commissioners) representatives of the Home Loan Bank Board, the Veterans Administration, the Department of Agriculture, and RFC (where FNMA was still located).

Thus there was created a forum in which spokesmen for most of the major Federal programs with a significant effect on housing credit could make their views known. Neither the Council nor its Chairman, however, had any decision-making powers. As matters developed, the Council proved ineffectual. With the passage of time it met more and more irregularly and less frequently, until, finally, it was abolished. (Reorganization Plan No. 4 of 1965.)

Conflicting, Duplicating, and Confusing Housing Laws—Need for Simplication

It would seem to be self-evident that the Nation's housing laws should be clear, consistent, unambiguous, and as simple and uniform as feasible. This is desirable in order to:

- Encourage good administration of the programs involved. They must, first of all, be understandable and clear to those who administer them.

• Avoid complexities, confusion, and "red tape" which discourage participation in the programs by lenders and sponsors. The laws and regulations must not be prone to latent problems of interpretation which will plague both the administrators and participants.

• Have laws and regulations which are understandable by housing consumers and other beneficiaries. Inconsistencies in statutory provisions are a chief source of dissatisfaction and public complaints about government, especially where those laws confer benefits in an inequitable manner.

• Help keep development costs at a minimum as a saving to consumers, builders, and to the Government in the case of subsidy programs or of defaults and insurance guaranty claims. The well-known complexities of regulations and redtape in Government-aided housing programs are a definite cost factor in project development under them.

• Avoid controversy with local officals, particularly with respect to programs where the city or other local public body is a participant.

• Keep litigation at a minimum. Litigation not only can embitter program participants and promote political and other controversy, but it can absorb an inordinate amount of official and staff resources and lead to protracted delays (which also drive costs up).

• Permit proper congressional oversight and understanding by individual Congressmen and Senators.

There is no need for great complexity in the housing laws. Insurance of residential mortgages is a relatively simple and clear-cut concept, requiring no more than two programs apart from subsidy operations—one for home mortgages and one for mortgages on multifamily structures, with adequate authority in the agency to provide for varying conditions and circumstances. Indeed, the original National Housing Act was just that.

Instead, our Nation's housing laws today, after almost 40 years, are a hodgepodge of accumulated authorizations, replete with inconsistencies, conflicts, and obsolete provisions and without overall design or coordinated structure.

Testimony given in Congress on behalf of the Executive Branch has emphasized the number and complexity of these existing authorities, as well as the resulting frustration, cost, and redtape that seriously impede good administration, discourage participation by builders, lenders, and sponsors, confuse consumers and even the experts, and hinder congressional oversight. In one of several statements to that effect, former HUD Secretary George Romney said to the Senate Subcommittee on Housing and Urban Affairs:

> To function properly, our housing programs must bring together private builders, private lenders, private housing sponsors, public agencies and private purchasers. At present the number and complexity of our existing statutory authorities act as a deterrent to the effective participation of these groups in our housing programs. Even the most sophisticated and experienced builders, lenders and sponsors find it frustrating and costly to accommodate their operations to the red tape and delay occasioned by the maze of our confusing authorizations and the regulations, circulars, forms and processing procedures that have grown out of them.
>
> The man most successful and at ease in the present statutory framework of our housing programs is the packager, knowledgeable in the intricacies of our forms and procedures, who can put together an attractive application and milk the most in subsidy out of the Federal programs by combining the different forms of assistance available under our several statutory authorities. Too often the most efficient producers of housing refuse to participate in our programs because they are unwilling to deal with the intricacies of our processing and program requirements. (Hearings on "Housing and Urban Development legislation of 1970," part I, July 13 to July 23, 1970, p. 10.)

The extent of the total statutory authorizations, regulations, and procedures is enormous. The statutes applicable to the FHA mortgage insurance programs alone fill many hundreds of pages in the statute books, and the implementing procedures and requirements confront the building and lending industries with some of the most confusing of all Federal redtape. Experienced participants in these programs are in agreement that their very complexity in itself substantially delays housing production, adds to project cost, and thereby increases industry criticism of the Federal Government's practices and procedures.

The sheer number of the individual insurance programs makes them difficult to understand and use. The greatest number of these are administered by HUD. A simple loan and mortgage insurance authorization in the original National Housing Act has grown into 40 mortgage and loan insurance programs. These 40 HUD programs are in addition to a number of others which have been terminated, but which have still a large volume of outstanding insured liability subject to default procedures and all the complex steps and processes which may result therefrom.

There are home mortgage insurance programs for:

• The basic mortgage insurance to assist the construction or purchase of a home (Section 203(b)).

• Special similar operations for moderate income families (Section 221(d)(2)).

• Farm housing (Section 203(i) in a proviso).

• Recreational housing Section 203(m)).

• Cooperative construction of homes (Section 213(a)(2)).

• Improvements to existing standard homes (Section 205(k)).

• Improvements to existing housing in urban renewal areas (Section 220(h)).

• Homes for servicemen (Section 222).

• Homes for disaster victims (Section 203(h)).

• Homes for persons in outlying areas (Section 203(i)).

• Homes in urban renewal areas (Section 220(d)(3)A(i)).

• Individual units purchased in an existing multifamily structure already under Section 221 (d)(3) rental insurance program (Section 221(i)).

• Purchase of deteriorated homes and rehabilitation and sale to low income families (Section 221(h)).

• Purchase of Government-owned housing (Section 223(a)).

• Housing in older declining areas (Section 223(e)).

• Development of experimental homes (Section 233).

• Purchase of a unit in condominium housing (Section 234).

• The subsidy homeownership operations in Section 235.

• Purchase of home by low or moderate income family who has had special credit problems, but has adequate prospects of being good risk (Section 237).

• Homeowner obtaining fee simple title to property he holds under leasehold (Section 240).

• Homes for civilian employees of the Department of Defense, NASA, and AEC (Section 809).

In addition to home mortgage insurance, HUD has multifamily mortgage insurance programs for:

• The basic mortgage insurance for multifamily structures (Section 207).

• Cooperative ownership projects (Section 213(a)(1)&(3)).

• Purchase by cooperative of a multifamily structure already under Section 221(d)(3) rental insurance program (Section 221(j)).

• Multifamily structures in urban renewal areas (Section 220).

• Improvements to existing multifamily structures in urban renewal areas (Section 220(h)).

• Low and moderate income multifamily housing (Section 221(d)(3)).

• Moderate income housing (Section 221 (d)(4)).

• Housing for the elderly (Section 231).

• Experimental rental housing (Section 233).

• The subsidy operations for rental housing under Section 236.

• Improvements to any multifamily structure (including a group practice facility or nursing home) already having mortgage insurance under another HUD program (Section 241).

• Housing for servicemen and civilians in areas impacted by military installations (Section 810).

• Rent supplement operations (Section 221 (d)(3) in conjunction with Section 101 of the Housing and Urban Development Act of 1965).

Another HUD program, applying to homes, rental housing structures, and commercial buildings, provides insurance to financial institutions against certain losses on repair and rehabilitation loans (Title I).

In addition to all these, there are five HUD mortgage insurance programs for projects other than housing structures:

• Land development and new communities (Title X).

• Group medical and dental practice facilities (Title XI).

• Mobile home courts (Section 207).

• Nursing Homes (Section 232).

• Hospitals (Section 242).

The great number of mortgage and loan insurance programs only partially explains the tremendous complexity of operations under them. The individual programs differ with respect to important features of the insurance operations as well as the specific eligibility items relating to the mortgage, the mortgagor, and the property involved.

Underwriting principles vary among these programs. The requirement of "economic soundness" in the basic home and multifamily insurance programs was waived in many programs with special purposes in favor of a more relaxed standard called "acceptable risk." Similarly, some programs base the amount of the insured mortgage on "appraised value," as in the original mortgage insurance programs, but others use "replacement cost," which generally results in a higher mortgage amount and thus a greater insurance risk. Also, some programs have a higher maximum ratio of loan amount to the value of the property, resulting in greater risk.

In the case of some programs, the statute authorizes, in effect, certain types of special credit risks to be assumed, such as those resulting from the location of the property in an urban renewal area or the blighted condition of the area, and even the credit of the home borrower to a certain extent. Similarly, the statute sometimes permits the waiver of usual property standards because of the location of the property in outlying areas or in older, declining areas.

The mortgage terms required by the statute for insurance eligibility differ in a multitude of ways under the many programs. The statute authorizing one program may prescribe 20 or more special dollar and percentage figures relating to the maximum mortgage amount. Each program has its own set of these figures, some consistent with those in other programs, and some not. These maximum mortgage amounts result in different minimum downpayments for purchasers and other borrowers under the programs, as well as imposing different responsibilities on lenders, closing attorneys, and others.

A bank or other lender using FHA mortgage insurance is typically confronted with two quite different FHA insurance programs in its day to day operations—those under the regular FHA mortgage insurance programs, and those under the Title I program for insuring against losses on loans for repair or improvement. Unlike the mortgage insurance programs, the Title I loan insurance program involves no HUD processing of individual loans, and contains a coinsurance feature of 10 percent of the amount of each loan.

In the case of the rent supplement program and Sections 235 and 236 (which involve Federal subsidies to the home owner or tenant), lenders and builders are confronted with quite different subsidy techniques and formulae, and significantly different requirements bearing on the way in which they conduct their own business affairs.

In addition to all of the above programs administered by HUD, there are Federal programs administered by other agencies of the Government with still different techniques and requirements: the Veterans Administration and the Farmers Home Administration. That increases the confusion for lenders and builders, not only because of the additional number of programs administered by those agencies, with different requirements and procedures, but because of the need for a lender or sponsor to deal with several agencies on similar types of development.

A discussion of specific duplications, conflicts, inconsistencies, and obsolete provisions is given under the heading below: "Examples of Confusing Features of Existing Housing Laws."

Why Did the HUD Housing Laws Develop as They Did?

One reason was the complexity and profusion of purposes in this area from the anti-Depression measures of the 1930's through the increasing responsibilities given the Federal Government in the decades that followed for stabilizing and improving the general economy; for measures to assist the Nation's least fortunate citizens, the poor, the elderly, and the handicapped; and for attempting to cope with the emerging problems of municipal development and redevelopment accompanying our increasingly urbanized and mobile society. The goals of Federal housing efforts during that period fluctuated in line with uncertainties as to (1) the desirable degree of Federal involvement in private housing credit and production, (2) the desirable amount of responsibility for public action at each level of government—Federal, State, and local, and (3) the appropriate and preferred financial and administrative techniques for carrying out basic policy in this field.

An equally important reason for the massive and complex structure of the legislation was the timing and process of its enactment. Until very recently, there has been an omnibus housing bill enacted by Congress almost every year since the conclusion of World War II. An "omnibus" bill covers many independent items of legislation over a broad subject. That was true with respect to each omnibus housing bill which, in addition, reflected an accumulation of proposals in the executive branch and the congressional committees over a period of a year or more. Normally, the committees did not, in the interim, act on individual housing bills referred to them.

The enacted housing bills were usually a combination of executive branch recommendations—usually refined by Congress to reflect its varied makeup—and the pleadings of special interest groups. Rising costs repeatedly upset the validity of the numerous dollar ceilings in the housing statutes, requiring extensive amendments. Typically, in each annual housing bill there were proposals (such as public housing increases in the early years) that might well not have been enacted if considered as separate pieces of legislation. To obtain the support, or at least minimize the opposition, of organizations or individuals in Congress, a variety of amendments were added—such as an amendment favored by a national interest group, or special aid for a project in the district of a particular Congressman. With this aid for everyone, critics often referred to an omnibus housing bill as a Christmas tree with gifts for all.

As indicated by the legislation itself, proposals to Congress for new programs were often responses to emerging needs or pressures from interested groups. When enacted, each program was added to the old, so that the whole package of legislation grew in size continually.

Generally, the Agency's legislative proposals to the Congress were not based on systematic study or reevaluation of the Federal Government's overall policies and legislative authorities with respect to housing credit. Until recently there was not even a continuing long range study looking toward the next year's legislative program. Typically, there was a belated effort by the Agency to meet a deadline for presenting the legislative recommendations for the coming year to the Bureau of the Budget. Sometimes new approaches of possible merit were discarded because of the lack of needed time for study.

Also significant was the practice of using repetitions of statutory provisions whenever a new program was authorized. Primarily, that resulted from internal agency pressure to preserve intact the original mortgage insurance operations (especially the home mortgage program with its "mutuality" mechanism) and insulate them from possible adverse effects from new "social purpose" programs with less rigid underwriting standards. Paramount importance was attached to the original insurance fund. Therefore, a new program was given a new "fund" with all of its related provisions. That, in effect, almost mandated a completely separate statutory authorization with repeating provisions for the new program, except as to certain routine items that could be incorporated by reference.

Another obstacle to obtaining coordinated Federal housing legislation has been divided responsibility for developing executive branch policies having a major impact on HUD housing programs. For example, the earliest (and some later) Federal programs designed to generate mortgage credit for housing were placed in separate Government agencies. It naturally developed that the executive branch's recommendations for such programs came primarily from the agency involved, which was deemed to know its own needs best, or how a proposal would affect it. Accordingly, the recommendations were fragmented and narrow.

This practice still continues to the extent that major housing credit programs are in the Veterans Administration, the Federal Home Loan Bank Board, and the Department of Agriculture, as well as the Department of Housing and Urban Development.

At the same time, there is a division of committee jurisdiction in the Congress on some aspects of housing and urban development, although most of the legislation in this area is handled by one set of House and Senate Committees.

In more recent years, the statutory complications were multiplied by the authorizations for additional subsidy operations under four different types of major programs (each for a dominant purpose at the time of enactment): Section 202 direct loans at below-market interest rates; Section 221(d)(3) mortgage insurance at below-market interest rates supported by the Federal National Mortgage Association purchases; rent supplements; and the subsidized interest rates for home purchasers and rental housing sponsors under Sections 235 and 236.

Also, it must be recognized that in formulating proposed housing legislation there are conflicting major policy goals that continue with respect to housing itself, or with respect to housing and other major government objectives. These often account for compromises and gaps in meeting desirable and consistent housing objectives. Some of these conflicting goals are discussed under a separate heading below, and represent a type of problem applicable to new, as well as past, proposals.

There has always been recognition that administrative problems have resulted from these duplications. As early as the 1940's, significant proposals were made to have the entire National Housing Act rewritten. The technical basis for such a reform was not laid, however, until 1970, when the first draft was prepared by the Department of Housing and Urban Development and submitted to Congress. Comprehensive legislation of this nature has not been enacted.

Examples of Confusing Features of Existing Housing Laws

For illustrative purposes, the characteristics of existing housing law that tend to generate confusion, inequities, and excessive length and redtape can be grouped under (1) duplications, (2) conflicts and inconsistencies, and (3) obsolete provisions.

Duplications: Although not as substantive as conflicts and inconsistencies in the housing laws, duplicating provisions are so extensive and so pervasive in those laws that they constitute one of the major problems. Duplicative provisions have varying effects. In the case of the scores of FHA insurance programs, there is an unnecessary repetition of program provisions, including eligible mortgage terms, for each program, almost as though there were that many separate agencies administering similar programs. This might seem to result only in massive provisions and regulations, but, inevitably, it leads to inconsistencies and further confusion because of the way pressures for amendatory legislation and enactment occur. In fact, this particular repetition has led to so many variations in insurance terms that the programs are extremely difficult to understand. It also has led to inequities and inconsistencies, some of which will be mentioned later. As noted, this repetition of FHA programs originated largely in the agency's desire at the time to protect the "mutual" fund (discussed below) from the feared effects of programs not using the fund—a reason which is now obsolete as a practical matter, and probably was never as important as it was thought to be.

Other types of duplication represent substantive duplication of functions. The HUD-subsidized mortgage insurance programs for rental housing (rent supplements and Section 236 subsidized interest rates) are duplicating functions having largely overlapping objectives. Often the differing techniques of the two programs have been combined for application to the same project. In fact, most of the mortgage insurance programs are duplicating, and they could be consolidated with only such variations in operations as determined administratively desirable for a particular purpose.

The duplicating housing programs of HUD, the VA, and the Farmers Home Administration have been mentioned. In the case of the VA and HUD, their duplicating programs are quite often used within the same housing project, because a builder may have to qualify under both agencies, not knowing in advance whether a purchaser will be a veteran or not. The extent of the resulting confusion is evident for developers, lenders, and home purchasers, who must meet different requirements in the same project.

The overlap of HUD and Farmers Home Administration programs is particularly confusing where they both operate in the same town. This happens because Farmers Home Administration programs extend to housing in towns up to 10,000 population (while no population standard is set for FHA mortgage insurance).

The housing programs of these agencies have a common major purpose—to assist housing construction, purchase, or repair—but they differ widely in techniques of operation and benefits conferred. These are explained below.

Another example of duplicating housing functions concerns those of the Federal National Mortgage Association, the Government National Mortgage Association (in HUD), and the Federal Home Loan Mortgage Corporation (under the board of directors of the Federal Home Loan Bank Board). These secondary market agencies duplicate one another because each has as its primary functions the buying and selling of Government-insured or guaranteed mortgages. In addition, the authority of the Federal Home Loan Mortgage Corporation (FHLMC) (created by the Emergency Home Finance Act of 1970) to carry on a secondary market in conventional—as well as Government-insured or guaranteed—mortgages, duplicates the same authority given to FNMA in the same act. This is a good illustration of how a duplicating operation will spawn more complex ones. The duplication here was a natural result of the establishment of the Federal Home Loan Bank Board as an independent policymaking agency in the housing field.

Before the 1970 act was even passed, the Congress found it desirable to enact further duplicating programs. These were the parallel operations (enacted as part of the same act) designed to furnish subsidy payments to FNMA and FHLMC to enable them to reduce interest costs to "middle income" families (the Section 243 programs). Although not yet funded, these programs show the type of legislation necessary to accomplish a single purpose when the agencies involved have almost identical functions. The practical difficulties of coordinating and compromising the independent policies and decisions of these agencies was shown by the protracted negotiations required to reach agreement on procedures and forms necessary for implementing their secondary market operations covering conventional mortgages.

Conflicts and Inconsistencies: Following are some conflicts and inconsistencies.

"Mutuality": Only the regular Section 203 home mortgage programs and the management-type cooperative housing program under Section 213 have a "mutuality" feature. The mutuality concept is designed to return to the home purchaser or mortgagor, in effect, the unneeded portion of the premiums he paid. In the case of Section 203, this feature was contemplated in the original 1934 enactment as a means of establishing an adequate insurance reserve, when there had been no significant experience with fixing premiums under mortgage insurance. The mutuality feature was intended to permit premiums to be sufficiently high for soundness of the system, while at the same time assuring the homeowner that his premium payments were not excessive.

As experience with the Section 203 program accumulated, mutuality proved to be unnecessary as a crutch for determining appropriate premium amounts. Also, as FHA insurance became an accepted part of the home financing world, mutuality was not necessary to "sell" the program to consumers. As a matter of fact, most consumers were not even aware that the so-called mutuality arrangement existed. A great many homeowners who received payments at the termination of their group accounts were baffled as to why they were receiving them, and not infrequently attempted to return the money to FHA on the assumption that the checks had been sent through some sort of mistake. Yet it continued, with all its original requirements for establishing "group accounts" for similar type mortgages and for keeping records on individual transactions in order to compute and make such payments to each individual mortgagor as the credit balance in his particular group account warranted. In 1954, the "group accounts" were abolished, but the system otherwise remains. Today it serves no purpose.

"Mutuality" is objectionable principally as an anachronism, but it is also objectionable as an operating procedure that applies only to the above programs in a manner inconsistent with operations under other programs, requiring different recordkeeping and a staff to handle the payment of distributive shares of funds to mortgagors.

Single Mortgage or Cost Ceiling for all Areas of Country: Each of the statutory maximum mortgage amounts (although inconsistent with other mortgage ceilings) applies uniformly to all areas of the country, except where an increase is authorized for certain high cost areas. Increases are authorized for Alaska, Guam, and Hawaii; they are also authorized in some special purpose programs for high cost areas generally, but to a wholly inadequate extent.

Because of the extremely wide range of construction costs in different regions of the country, and among rural, suburban, and central city areas, any fixed dollar ceiling for the whole country is bound to be inequitable and harmful to the housing programs. If the uniform ceiling is high enough to encourage building in all areas, it will necessarily be too high in some. In the latter areas, builders will tend to gravitate to the highest permissible ceiling in order to increase their profits. On the other hand, if ceilings are made sufficiently low for those areas, sponsors will be discouraged from building in other areas. In fact, too-low ceilings have prevented some major programs from being used to any significant extent in certain large cities.

Where the maximum statutory ceiling is sufficiently high (which it generally is not) some variation may be made among areas administratively, but this has led to delays and dissatisfaction in the private sector.

Where Federal housing subsidies are involved and a too-low mortgage ceiling prevents construction, low income people in that area are thus prevented from participating in subsidy benefits, while a too high ceiling will result in unnecessarily high mortgage and construction costs. In the latter case, there would be a waste of Federal funds (in addition to extra costs to the consumer under the interest rate subsidy programs) because the subsidy is based on the total mortgage amount, which in turn is inflated by these unnecessary financing and construction costs.

In addition, fixed dollar mortgage ceilings tend to become obsolete very quickly, and have probably required more individual statutory amendments than all other mortgage provisions combined.

In the case of low rent public housing, this entire problem was removed in 1970 by the repeal of dollar construction cost limits, and the substitution of authority for fixing ceilings on the basis of prototype costs established administratively for each area on the basis of representative costs. Of course, this public housing procedure for fixing ceilings, while advantageous, presents an inconsistency with the dollar ceilings in mortgage insurance laws.

"Economic Soundness:" Under the original Sections 203 and 207 mortgage insurance programs, the property or projects with respect to which the mortgage is executed must be "economically sound." This underwriting standard still exists with respect to those programs, but it generally has been waived for the special purpose mortgage insurance programs, and an "acceptable risk" standard substituted.

A most significant waiver of the economic soundness standard was made by Section 223(e) of the National Housing Act, which also permitted waiver of other eligibility requirements to encourage more mortgage insurance in any "older, declining area." The area had to be "reasonably viable" and the property "an acceptable risk," giving consideration to the needs of "families of low and moderate income in such area."

The substitution of "acceptable risk" for "economic soundness" produced confusing inconsistency because, although the Congress intended the substitution to encourage liberalization, it certainly did not intend to authorize the insurance of unsound loans. The extent to which "acceptable risk" is something less than "economic soundness" is vague in the statutes, which either provide no standard at all for determining that difference, or use some vague language such as "taking into consideration the needs of families of low and moderate income in such area." Some contend that "economic soundness" and "acceptable risk" are interchangeable, because risk is always present in insurance, and at the same time insurance should always be reasonably sound. In practice, "acceptable risk" has been applied quite differently from "economic soundness." Even so, it has not been uniformly applied, as is evidenced by the fact that in some programs where "acceptable risk" is used, there have been abnormally high default rates, but in other such operations that has not been true.

"Acceptable risk" can be applied conservatively, but it also can be used as an open door to loose underwriting that can result in such scandals as have been recently experienced.

"Appraised Value": As another underwriting concept, the insured mortgage under the original FHA programs could not exceed a stipulated fraction of the appraised value of the property. That standard took into account the long range value of the property over the life of the mortgage. A "replacement cost" maximum amount was generally substituted for "appraised value" in the special mortgage insurance programs, which were enacted after the original programs. Because "replacement cost" is only one of the measures commonly used to determine "value," a maximum mortgage amount computed on the basis of replacement cost alone usually results in a higher maximum amount. The use of "replacement cost" thus tends to lower the underwriting standards applied. This was deliberately authorized by the Congress to encourage sponsors to participate in the special purpose programs. It does establish an important inconsistency in mortgage insurance operations, however, and in the quality of security behind the mortgage instruments insured by HUD and sold in the secondary market throughout the country.

Maximum Dollar Mortgage Amounts: Each of the many FHA mortgage insurance programs has flat dollar limits on the amount of eligible mortgages. In the case of home mortgages, these ceilings range from $14,400 to $33,000 for a single family unit. While amendments have brought about some consistency from time to time, there are still differences that cannot be explained on any basis other than the average costs at the various times of enactment, or the policies prevalent at those times. Examples are the discrepancies among the dollar ceilings in the regular Section 203 home mortgage program, the Section 220 home mortgage program for urban renewal areas, and the home mortgages under Section 221 for moderate income families, especially as to structures for more than one family.

The dollar ceilings with respect to the multifamily housing programs present a different problem of inconsistency. Each program has such an array of varying ceilings that they defy meaningful comparison. These ceilings have fixed maximum amounts per mortgage varying from $12.5 million to $50 million, but the more significant variations are geared to amounts per dwelling unit in various types of structures and areas.

Downpayments: Statutory provisions determining necessary downpayments by mortgagor purchasers contain desirable variations for differences in mortgage amount and some other factors, but they also contain some inconsistencies. Generally, the amount of the downpayment is determined by the permissible loan-to-value ratio of the mortgage. That varies from 75 percent (in the case of recreational housing) to as much as 100 percent (which can apply to a mortgage amount as high as $24,000 in the case of Section 221(d)(2) housing for moderate income families and to Section 235 subsidized housing). The 100 percent maximum is not applicable to a comparable mortgage amount under other programs. In the case of Section 221(d)(2), unlike other programs, specific downpayment dollar amounts are prescribed on the basis of the number of units in the structure and whether the purchaser had been displaced from his previous home.

Generally, the formula for arriving at the loan-to-value ratio allowable on an individual mortgage is stated in terms of a fixed percentage of X dollars of appraised value, with progressively smaller percentages prescribed for additional increments of value up to the maximum mortgage amount stipulated in the statute. However, these graduated steps and percentages are not uniformly applied in all programs, as can be seen, for example, by comparing their treatment in connection with home mortgages insured under Sections 203 and 220.

Eligibility of Families for Housing Under Subsidy Programs: With little logic or rationale, statutory requirements as to eligibility for subsidized housing vary greatly under the several programs, producing substantial inequities. The principal subsidized housing programs under existing law are the Sections 235 and 236 subsidized interest rate programs for homeownership and rental housing, the rent supplement program, and the public housing program. (The Section 221(d)(3) below-market interest rate program and the Section 202 direct loan program for elderly housing have been phased out in favor of Section 236.)

Each of these programs has its statutory income limit requirements for determining the group eligible to participate in the program. Not only are the income limits for each program different, but income limit requirements for a particular program are often applied in different ways in neighboring communities.

The public housing statute defines "families of low income" (including elderly and displaced persons) as those who are in the lowest income group and who cannot afford to pay enough to cause private enterprise in their locality to build an adequate supply of decent, safe, and sanitary dwellings for their use. The statute provides, however, that the actual income limits for admission to occupancy shall be fixed by each local public agency (housing authority) after taking into consideration certain prescribed factors. These limits are then approved by HUD. Thus, each of some 3,000 local housing authorities establishes its own income ceilings for admission, and continued occupancy with different dollar amounts for various categories of occupants and for other circumstances and with different methods of computing family income. These all vary from those established by the other housing authorities. Inequities are thus created for low income families living in different areas.

In the rent supplement program, income limits are tied to the income limits actually established in a community for its public housing program. However, because the Federal definition of income in the rent supplement program differs from the definition of income imposed by each of the various local housing authorities, actual income limits in the rent supplement program differ from those prevailing in the local public housing program. (Income limits in the Section 221(d)(3) program were generally tied to median income in the area in which the housing assisted under that program was to be constructed.) Because of the highly controversial nature of the authorizing legislation, it was subject to legislative history restrictions on eligible income that were not applicable to other programs, such as specific tight limitations on the amount of assets held by an applicant for admission to occupancy.

In the Section 235 homeownership program and the Section 236 rental program, there are two separate income limits: "regular limits," based on 135 percent of the public housing limits in effect in the area where the housing assisted under Section 235 or 236 is constructed, and "exception limits," based on 90 percent of the limits established in that area for the Section 221(d)(3) program. (The "exception limits" apply to not more than 20 percent of the Section 235 and the Section 236 subsidies for the whole country.) The "regular limits" for the Section 235 and 236 programs in an area are based on 135 percent of the income limits actually established for public housing in that area.

In those counties in which no local housing authority has been established and no public housing program operates, "regular limits" set for the Section 235 and 236 programs are based on the maximum statutory income limit that could be established by a local housing authority operating in that area. However, income limits established by a local housing authority are almost always below the maximum statutory amount that could be established in the area. Therefore, sections 235 and 236 income limits in a county where there is no housing authority are often much higher than income limits in an adjoining city with a housing authority. To private housing developers interested in producing such housing, and to needy families living in urban areas who cannot qualify for assistance because they live in the city and not the suburb, this result is inequitable and irrational. Eligibility criteria which impose lower income limits in high cost metropolitan areas than in predominately rural counties cannot be justified.

If the above seems unduly complex and bewildering, it must be admitted that indeed it is. And, beyond that, it is a fact that many inequities exist in the admission of tenants to subsidized housing projects, both on a national basis and in individual areas or neighborhoods.

Rentals in Subsidized Housing: Each of the subsidized housing programs also has different requirements with respect to the amount or proportion of income that a family must pay in rent or toward ownership. In the public housing program, each of the local housing authorities establishes its own requirements as to the percentage of its income a subsidized family must contribute. These differences create substantial inequities among the beneficiaries of the programs, especially because the computations of incomes on which rentals are based vary so widely.

In the Section 236 rental program and in the rent supplement program, tenant families are required to apply at least 25 percent of their income to rental, but there is no similar statutory requirement for public housing. Even between the Section 236 and the rent supplement program, rentals are inequitable because of the different methods of computing income. Under the Section 235 program of subsidized interest rates for a home purchaser, he must pay 20 percent of his income on the mortgage loan, including principal, interest, taxes, insurance, and mortgage insurance premium.

In 1969, the Congress became concerned over the high percentage of income which some tenants in public housing had to pay, and enacted the so-called first Brooke amendment (Section 213(a) of the Housing and Urban Development Act of 1969), which generally limits to 25 percent the portion of income that any tenant in public housing may be required to pay as rent, and defines income for that purpose. That provision, however, did not apply to other subsidy programs in which lower income families often contributed more than 25 percent of their incomes.

Another rental inequity exists within the public housing program itself. By statute, a gap of at least 20 percent (except in the case of displaced or elderly families) must be left between the upper rental limits for admission to a public housing project and the lowest rents at which private enterprise, unaided by public subsidy, is providing a substantial supply of decent housing. That provision removes an income bracket of low income families (except for the displaced and elderly) from the benefits of the program; there is no reason for this, except to assure private sponsors that public housing will not reach an income group close to one they might serve.

Also, this 20 percent gap provision for public housing is inconsistent with provisions applicable to other programs which have no such requirement.

Coinsurance: The HUD Title I repair and rehabilitation program requires a 10 percent coinsurance by the lender on each loan involved, which provides a real incentive for the lender to assume responsibility for the soundness of the loan. That coinsurance requirement was imposed to prevent a continuation of gross abuses under the Title I program, as explained above. The HUD mortgage insurance programs contain no significant coinsurance feature. This major difference in the programs confronts the typical bank or other lender using any HUD insurance operations, as mentioned above.

Hidden Subsidies and Costly Devices to Defer Federal Budget Impact: Program-financing schemes to avoid the need for appropriations or to permit a technical Federal budget reduction are inconsistent with good management, frank information as to Government costs, efficient and economical administration; they generally result in extreme complexities.

Housing programs have been particularly subject to these devices, largely because of budget restrictions, and sometimes because of specific proposals developed in the Bureau of the Budget (OMB). Those legislative results are relevant today not only because some are still in operation but because there is no reason to conclude that similar emphasis on budget factors will not be applied to future proposed housing legislation by those primarily concerned with Federal budget matters.

Hidden Subsidies: An early use of hidden subsidy in housing was through the FNMA special assistance operations (now carried out by GNMA) where the subsidy is provided by purchasing mortgages at prices above their value at the time—often at par. This contrasts with the direct loan and the subsidized interest rate housing programs. The use of the Tandem Plan in a variety of ways (as explained above) is one form of subsidy which is sufficiently hidden to avoid the extent of controversy that would result from a frank subsidy in an equal amount.

Another similar device exists under the rural housing insured loan system of the Farmers Home Administration. The Housing and Urban Development Act of 1965 establishes that system and a Rural Housing Insurance Fund to finance it. That was done in large part to get around budget restrictions that had been applied to direct loans which the Farmers Home Administration had been making under earlier authority (a practice which still continues). Under the insurance system, the rural housing loan is made by the Farmers Home Administration and secured by a note and mortgage. The note is packaged with other similar notes as collateral for a special type of Government-guaranteed security. These securities are sold in the private market at rates determined by conditions in the money market at the time. The proceeds of the blanket security sales are deposited in the above Fund. Since the interest cost on the blanket securities generally exceeds the interest realized on the underlying notes, subsidies are in effect necessary and are paid on the loan transactions. These are treated as operating costs and paid from income to the Fund to the extent available, but deficits in the Fund must be restored with annual appropriations.

The Government financing of Capehart military housing—with the "Rube Goldberg" scheme permitted by Title VIII of the National Housing Act—was described above. It was a major program under which HUD mortgage insurance is still outstanding, and is perhaps the classic example of a complex use of programs in a network of procedures to circumvent a limitation in other legislation.

Deferral of Budget Impact: Because of the immediate budget impact of Federal direct loan programs, Federal agencies have been restricted or prevented by budget considerations from proposing legislation for such programs, and there has been strong pressure from Federal budget officials to shift existing loan programs to some form of subsidy operation. The HUD programs have been affected repeatedly by this overriding policy.

Examples are the suspension of the Section 202 direct loan program for the elderly in favor of Section 236 interest rate subsidies, and the shift from direct loans for college housing to subsidies for paying portions of the interest on college housing loans from private sources. The ultimate effect on the Federal budgets, and the taxpayers, over the loan period of, say, 40 years would be less under the loan system than under a system of annual or other periodic subsidies to accomplish the same objective. That is true, of course, because the amount of the loan is normally recovered with interest, while the subsidy is not recovered.

The extent of ingenuity and the magnitude of operations involved in financing gimmickry affecting housing is tremendous. In 1964, the Bureau of the Budget wanted to convert large sums from Government's holdings of mortgages into "budget receipts," without having to face the criticism that would have resulted from selling these mortgages—all insured or guaranteed by the Government—at heavy discounts. Accordingly, a scheme was developed (and enacted as Section 701 of the Housing Act of 1964) to get billions of dollars from the sale of interests in FNMA-held mortgages and other Government-held mortgages, without actually selling the mortgages themselves. (The residue of the FNMA operations under this scheme is now administered in HUD by the GNMA.)

Of course, the efficient and above-board alternative would have been to sell the mortgages on the market. Instead, "participation certificates" were authorized and sold, giving the purchaser the right to certain proceeds from the mortgages, plus a guarantee backed by the full faith and credit of the United States.

To the extent that mortgage proceeds were insufficient to make timely payments on the certificates, appropriations were authorized. That complicated monstrosity handled the sales of almost $10 billion worth of "participation certificates," and the Federal cost in the form of appropriations because of deficiencies in mortgage proceeds has already amounted to hundreds of millions of dollars, and will continue to grow as long as any of these certificates remain outstanding.

Stabilization of Housing Credit and Production: The stabilization of housing credit and production has always been a prime objective of the Government housing programs. This was strengthened by the establishment (in Title XVI of the Housing and Urban Development Act of 1968) of a specific 10-year national housing goal of 26 million new or rehabilitated units. At times of critical need, however, the general principle of stabilization has often been ignored for measures aimed at the current problem.

Instances of interest rate and other mortgage insurance changes for countercyclical purposes were mentioned above. The use of FNMA special assistance for that purpose is more common. One example was the Act to stimulate residential construction in April, 1958 (Public Law 85–364), which added $500 million to the existing FNMA special assistance authority.

Local Approval Requirement: By Federal statute, a rent supplement project is prohibited in a community unless the local governing body has approved it through adoption of an applicable "workable program" or otherwise. That is inconsistent with the requirements of local laws, which do not normally make the construction of a private housing project subject to governing body approval. It is also inconsistent with Federal provisions applying to the Section 236 subsidized interest rate program, where no such requirement is imposed. This inconsistency runs contrary to an even and equitable distribution of subsidies for families throughout the country, as families in some areas can be deprived of program benefits without reason. The application of this approval requirement to various existing insurance programs was one of the major issues in the Congress concerning housing legislation pending in 1972.

Interest Rate Ceiling: In the overall housing credit policy of the Federal Government, there is a major conflict with respect to control of interest rates. All FHA-insured mortgage loans are subject to maximum interest rate controls prescribed in Federal regulations—these ceilings in regulations have always been subject to statutory ceilings, except for the current temporary suspension which leaves the ceilings to administrative decision—while loans by Federal savings and loan associations are not subject to such Federal controls, although assisted by the United States through the facilities and financial backing of the Federal Home Loan Bank System. This inconsistency has become more pronounced since the savings and loans have been given the facilities of a Government secondary market (in both FNMA and the Federal Housing Loan Mortgage Corporation).

Inconsistent Programs of Farmers Home Administration and HUD: As explained above, there are some advantages and some disadvantages to the home financing methods of the Farmers Home Administration compared to those of HUD, but there is no adequate rationale for the inconsistency of the two programs, especially in the physical areas of operation where they overlap, which were mentioned above. The Farmers Home Administration assistance (Title V) is initiated with a direct government loan that is later used to obtain private funds—unlike private lending under the HUD insurance programs and the VA guarantee program, where public funds are sometimes substituted for private funds by virtue of a secondary market operation.

Divided Planning Functions: Adequate responsibility relating to planning was given to the Housing and Home Finance Agency in connection with the program functions under the Urban Mass Transportation Act of 1964. Reorganization Plan No. 2 of 1968, however, transferred the latter functions to the Department of Transportation. Thus the planning authority was divided, leaving HUD with the part primarily concerned with the relationship of the urban transportation system to the comprehensively planned development of the urban area, and giving all other planning duties under the Act to DOT. Regardless of the debatable merits of the Reorganization Plan, the division of functions relating to the interwoven planning of a transportation system in an area is adverse to consistency in that planning.

VA "Guaranty" and HUD "Insurance": A number of important inconsistencies exist in the requirements and procedures under the programs of these two agencies which cause confusion for builders, lenders, and home purchasers. These problems were recognized soon after the enactment of the GI Bill in 1944, and several unsuccessful efforts were made in the Executive Branch through the years to develop remedial legislation, but, essentially, only administrative procedural steps have been taken. One of the rationales for the separate VA housing operations—the temporary nature of that program—has been removed by the legislation, making all veterans eligible for benefits on a permanent basis.

Major inconsistencies in the HUD and VA operations are:

1. The VA uses a "guaranty" system in contrast to the HUD "insurance." This means that VA loans carry full protection against loss (including interest and foreclosure costs) up to the limit of the guaranty on each loan; HUD requires a slight coinsurance by the lender which can result in some loss of interest and a portion of foreclosure costs. This difference in programs is perhaps more significant because of the complexity of the HUD "certificates of claim" procedure discussed above.

2. The VA-guaranteed loan can be up to the full "reasonable value" of the property, in contrast to the downpayment generally required for

a home purchaser under HUD procedures. This becomes a more significant difference in the higher cost ranges.

3. The VA establishes the "reasonable value" for the purpose of fixing the loan amount, but this tends to become, in effect, the sales price, and is distinguished from "value" established by HUD for computing maximum mortgage amount. The latter is based upon the value of the property as security for long range insurance purposes.

4. The VA charges the veteran no premium for the guaranty, in contrast to the HUD-required premium paid by the homeowner in most HUD programs.

5. The VA pays guaranty benefits in cash, in contrast to the HUD debenture system (which, however, as explained above, now permits cash payments under certain conditions).

6. The VA uses fee appraisers to fix "reasonable value," as distinguished from the general use of staff appraisers by HUD.

7. The VA follows quite different procedures in the event of default on the loan and foreclosure proceedings. Unlike HUD, it takes custody of the property in order to protect it as soon as notified, and generally proceeds against the borrower (which HUD rarely does) for losses it incurs through its payment under the guaranty.

Obsolete Provisions: In one sense, a large part of all of the massive HUD mortgage insurance statutory structure is obsolete, because an updating and simplification of that obsolete structure would eliminate a large part of the existing provisions. The consolidation of 10 programs into one, for example, would eliminate the bulk of the existing provisions for 10 programs.

However, many provisions (including all of the laws for some programs) are obsolete without reference to any overhaul of the statutes. A number of programs, by their terms, are no longer applicable to new projects. These authorizing provisions are obsolete and need not remain on the statute books because of outstanding contractual obligations. These will include, for example, Section 8 of the National Housing Act (the former program for housing in outlying areas), Sections 603 and 608 (the World War II defense housing programs), Sections 903 and 908 (Korean War housing programs), and Title VII Capehart housing provisions.

Other provisions—such as those designed to permit special types of projects to go forward at a particular time or place—have become obsolete because of the passage of time. Some provisions were never used, such as the yield insurance program authorized in 1948 under Title VII of the National Housing Act.

Some of the public housing provisions in the United States Housing Act of 1937 are obsolete, such as the references to the United States Housing Authority, and the references to corporate stock and auditing provisions applicable to corporations. The pump-priming provisions in the act, referring to alleviating present and recurring unemployment, go back to Depression days.

The most harmful provisions are those obsolete ones which have a substantive effect, such as the "mutuality" provisions of Section 203, discussed earlier. It is perhaps the outstanding anachronism in the housing statutes; it has sometimes resulted in a return of a portion of premium charges to a surprised homeowner who purchased the property after most of the premiums had been paid.

Conflicting Goals in Determining Housing Policies and Proposals

Executive and Congressional action on past legislative proposals in the housing field make clear that certain major conflicting goals will continue to confront those acting on future proposals in this field. They are relevant with respect to future legislation as factors to be weighed in judging executive or congressional acceptance and action on proposals. Some of these conflicts are:

Government Participation v. Independent Private Enterprise: This presented the major issue for the 1931 President's Conference on Home Building and Home Ownership. With the unprecedented concern for the plight of the home building industry and the national economy during the Great Depression, the reports of the Conference are nevertheless replete with expressions of fear concerning any Government participation in housing credit operations. But with the background conditions then existing, the Congress for the first time put the Federal Government substantially into this field of operations.

This conflict of goals still presents an issue in most new program proposals being considered. With respect to any proposal, the position taken by an individual within the range of these goals is directly related to his political and economic philosophy. Production incentives often are tempered with protection to "private enterprise," meaning those similar operations handled without the benefits of the new program. The degree of Federal participation is weighed against the urgency of the need and the extent of pressure for the proposal from constituents or private or public groups.

Program v. Budget Goals: Normally, the breadth or authorized volume of any program using appropriated funds is modified by goals of the Federal Budget. This is true of any program involving grants, loans, or other forms of Federal expenditure—such as through the special assistance functions of GNMA—and can be true of other programs.

In addition to dollar controls, budget goals may determine the very nature of the program. Thus, the President's budget office always opposes direct loan programs because of their initial budget impact, whether or not alternatives might result in greater expenditures over their full life cycle.

Production and Management Goals v. Consumer Protections or Benefits: Normally, consumer protections involve some additional burden on the lender, builder, or manager of the housing. Thus, builders have objected to the existing requirement that they give the home purchaser a warranty against structural defects and the requirement that the purchaser receive a copy of the HUD "appraised value" of the property. Such items may be objected to only because they are redtape, or because they may involve financial loss. These and many other mortgage insurance requirements bear on whether a sponsor decides to use mortgage insurance. That affects production. Therefore, any proposed legislation for additional consumer protection or other benefits must be weighed against its possible curtailment of the use of the program. This is desirable from the standpoint of the consumer as well as industry, because if curtailment is sufficiently drastic, other program benefits to the consumer of greater value could be lost.

Equal Opportunity controls present a good example: The major purpose of subsidy housing programs to make more adequate housing available for low or lower income families is sometimes in direct conflict with the objective of Equal Opportunity controls. This can be true where HUD Equal Opportunity regulations prohibit the location of public housing in areas of racial concentration. That tends to restrict the volume of such housing provided (regardless of the merits of the control). Also, making such controls applicable only to housing processed by the Government tends to reduce the volume of FHA-assisted housing for lower income families and encourages conventional housing with lower construction standards and lacking other consumer protections—contrary to some of the major goals of mortgage insurance legislation. Any policy seeking to enforce equal opportunity policies by withholding, or threatening to withhold, Federal financial assistance can have a similar effect.

Consumer benefits can create problems for management as well as production. Because of revelations that many public housing tenants were being charged a very high percentage of their incomes for rent, the Congress enacted the so-called "Brooke Amendment" (Section 213(a) of the Housing and Urban Development Act of 1969 amending Section 2(1) of the United States Housing Act of 1937), which prohibited tenants being charged more than 25 percent of their incomes for rent. That amendment removed hardship for many tenants, but it created tremendous management and maintenance problems for many housing authorities because of their resulting loss of income, amounting to many millions of dollars. The amendment permitted an allocation of Federal annual contributions for operating expenses of local authorities, but that proved to be inadequate in view of the depreciation of housing projects over many years and the inaccurate original estimates of the adequacy of operating reserves and receipts.

A collateral problem involving payments under the welfare programs of the Department of Health, Education, and Welfare illustrates some of the complications of HUD housing programs which extend into those of other agencies. The Brooke amendment waived the required reduction in a tenant's rent if that would result in a lower welfare payment to him. That was intended to force a continuation of the welfare payment without reduction, so that the tenant would not lose the advantage of his rent reduction. In some States, however, such welfare payments had to be reduced under those circumstances because of State law, so rentals were not reduced. A later Brooke Amendment (Section 9 of Public Law 92–213) prohibited local public agencies from reducing welfare payments to tenants because of the rent reductions. That result has been objected to on the basis that the tenant now receives, in effect, a double subsidy.

"Business Type Operations" v. Social Purposes: One major current issue is a form of the above conflict of goals—whether mortgage insurance programs should be free of special social purposes. This has been a perennial issue from almost the beginning of FHA programs. Through the years, one of the chief advocates against special social purposes in mortgage insurance has been the Mortgage Bankers Association of America (MBA), whose expressions on this issue have become more vigorous since the fraud and default problems that surfaced in 1972. An expression of its consistent position is put succinctly in one of its staff papers ("Restoring the Vitality of FHA—An Essential Need," Staff Paper #1, Mortgage Bankers Association of America, Washington, D.C., September 29, 1972):

> Beginning in 1938, FHA mortgage insurance has been repeatedly thrust into the attempt to accomplish social, economic, and political objectives. However commendable, these objectives were often of questionable adaptability to the insurance device or to personnel trained in underwriting mortgages. Some objectives made it necessary to lower underwriting standards and, in so doing, invited chicanery.
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> Over the years, FHA was called upon to insure mortgages on housing for defense workers, servicemen and their families, critical defense areas, the elderly and the poor, as well as mortgages on nursing homes, hospitals, and facilities for group medical practice. Many of these special and social purpose programs were not acceptable to private investors, not for lack of confidence in federal mortgage insurance, but from past experience that told them the loans would not survive. This apparent contradiction was an outgrowth of the lender's experience with special purpose programs. From the earliest diversion from FHA's original purpose, lenders had learned that when special purpose housing was no longer needed (e.g., critical defense housing which depended upon defense production jobs to maintain the market and the mortgage loans) foreclosures would follow and then the lenders would become the scapegoat for the program's eventual failure.

The MBA blamed, in particular, the loose underwriting standards flowing from the waiver of "economic soundness" and the use of "replacement cost" instead of "appraised value," as discussed earlier, which was pointed to as attracting entrepreneurs after large or fraudulent profits.

The counterargument given to the MBA position is that FHA was never solely a business-type operation, as distinguished from socially oriented programs. It has always had social objectives which the Congress considered sufficiently important to warrant Federal involvement. Originally, the principal objective was employment, a basic social purpose at the time, and the original program contained requirements which constitute consumer benefits as well as individual safeguards—minimum property standards, appraisals of insured properties, and the features of the long term, low downpayment, amortized mortgage with a controlled interest rate.

Similarly, it is contended that the serious processing deficiencies and industry abuses in 1972 did not constitute defects in the programs themselves or in basic mortgage insurance concepts, but pointed to inadequate management and staffing. It is a myth that social objectives cannot be mixed successfully with market-type operations, it is said, because competent staff have handled both successfully through years of FHA operation.

Public and Political Acceptance v. Efficiency and Cost Savings: It would seem that this conflict should never exist, but it does. In choosing the program technique for an established objective, it is not unusual for the choice to be made on the basis of what industry or the public may accept, even though that is not necessarily the least expensive or most efficient operation.

Ever since 1950, for example, direct Federal loan programs for a broad range of housing have been introduced in Congress and rejected or ignored, a paramount reason being the adverse reaction of private lending institutions. However, a direct Government lending program could make loans available at lower interest rates for home purchasers (without subsidy) because of the lower interest rates at which the Government can normally borrow funds.

Alternatives that are used include the indirect and more complicated procedures under the Government's secondary marketing operations, which provide an indirect subsidy through special assistance operations that assure a financial yield to private lenders. The highlight of this approach, of course, was the Section 221(d)(3) program, where the lender's profit came chiefly through servicing privileges and construction financing opportunities with virtually no private risk. Also, the subsidies that are less overt—such as special assistance—have from an early time been selected because they are less likely to stir up opposition.

In this connection, the Comptroller General of the United States, Elmer B. Staats, recommended to the Subcommittee on Priorities and Economy in Government of the Joint Economic Committee, December 4, 1972, that Congress consider legislation permitting loans under the section 235 homeownership program and the section 236 rental program to be financed directly by Government borrowing, rather than by private lenders, because of the lower interest rate at which the Government could borrow funds, notwithstanding the initial budget impact. He estimated the present value of the resulting Federal savings could amount to about $1 billion under the section 235 program, and about $1.2 billion under the section 236 program, for housing planned to be provided during fiscal years 1973 through 1978.

Political Reality v. Consistency: Major inconsistencies in housing legislation flow from the known position of the Congress toward benefiting certain groups as compared to others. Direct loans at low interest rates to farmers were accepted and noncontroversial at an early time, when such assistance to low income families generally was extremely controversial. Similarly, the absence of premium charges for veterans, plus other benefits, under the VA home loan guaranty program represented a special paternalistic approach for one group only. Currently, it is feasible to obtain authorization for assistance to the elderly and handicapped that would be strongly objected to by other low income groups (migrant labor, for example) with less emotional political appeal.

Appendix A. Tax Reform Act of 1969 (Public Law 91–172) (Changes Affecting Real Estate)

The real estate sections of the act are designed to limit the use of accelerated depreciation for tax shelter while, at the same time, channeling more private investment into housing through the use of preferential tax incentives.

Under current law, accelerated depreciation permits certain high income taxpayers to escape payment of tax on substantial portions of their economic income. This is done by using accelerated depreciation deductions to shelter income otherwise taxable. Moreover, depending upon the period the taxpayer chooses to hold real estate before sale, the taxpayer (under current recapture rules) may have all or a part of the gain on sale to the extent he has claimed accelerated depreciation deductions (which were previously offset against ordinary income) taxed at long term capital gains rates.

The major changes of the act affecting real estate are revisions to the accelerated depreciation rules and the recapture rules and the imposition of a minimum tax on the use of accelerated depreciation deductions. Particularly in the case of commercial and industrial construction, the act reflects the judgment that current accelerated depreciation rules constitute undue tax benefits. Consequently, the act's real estate sections provide for a three-tiered structure of tax treatment favoring investment in publicly assisted housing over other rental housing and rental housing over commercial and industrial construction.

Accelerated Depreciation

A. New Buildings

1. Housing—The act retains the 200 percent declining balance and sum-of-the-years digits methods of accelerated depreciation for new residential rental housing. A building qualifies as residential rental housing if 80 percent or more of the gross rental income from the building for the taxable year is rental income from nontransient dwelling units.

2. Commercial/Industrial — Commercial and industrial buildings, the construction of which was begun before July 25, 1969, or for which a construction contract or permanent financing contract was entered into before July 25, 1969, continue to qualify for the 200 percent declining balance and sum-of-the-years digits methods of depreciation. Commercial and industrial buildings contracted for or constructed after July 25, 1969, are limited to the 150 percent declining balance depreciation method.

B. Used Buildings

1. Housing—The act permits 125 percent declining balance depreciation (rather than 150 percent under current law) to be used on residential rental housing acquired after July 24, 1969, which, at the time of acquisition, had a remaining useful life of 20 years or more. Residential rental housing with a remaining useful life of less than 20 years acquired after July 24, 1969 (other than that acquired pursuant to a pre-July 25, 1969, contract) is limited to straight-line depreciation.

2. Commercial/Industrial—All commercial and industrial buildings acquired after July 24, 1969 (other than those acquired pursuant to pre-July 25, 1969, contracts) are limited to straight line depreciation (rather than 150 percent under current law) irrespective of their remaining useful lives at the time of acquisition.

C. Rehabilitation of Housing

The act permits a taxpayer to elect to amortize rehabilitation expenditures incurred with respect to low income rental housing after July 24, 1969, and before January 1, 1975, under the straight line method using a useful life of 5 years and no salvage value. The aggregate rehabilitation expenditure which may be amortized under this 5-year fast writeoff may not exceed $15,000 per unit but must exceed (over a 2-year period) $3,000 per unit. The term "rehabilitation expenditures" means amounts chargeable to capital account incurred for additions or improvements with a useful life of 5 years or more. The term "low income rental housing" means dwelling units held for occupancy by persons of low and moderate income as determined in accordance with the policies of the 1968 Housing Act.

If the unit is sold following rehabilitation, the difference between the amount of amortization taken under the 5-year fast writeoff over the amount of amortization that would otherwise have been taken using a straight line method for the actual useful life of the improvement is "recaptured" to the extent of gain at ordinary income rates.

The termination date of January 1, 1975, is designed to give Congress and HUD an opportunity to evalute the effectiveness of this new tax incentive.

Recapture of Excess Depreciation

A. Publicly Assisted Housing—Current recapture rules are retained for limited return, Federal, State, or locally assisted housing projects constructed, reconstructed, or acquired before January 1, 1975. Under current law, gain on sale is treated as ordinary income ("recaptured") to the extent the seller has claimed depreciation deductions in excess of those that would be allowed under the straight line method if the sale occurs in the first 20 months. After a 20-month holding period the excess depreciation over straight line which is recaptured at ordinary income rates is reduced by 1 percent per month. After 120 months (10 years) no recapture applies to a sale, and gain, to the extent of excess depreciation taken, is taxed at capital gains rates.

The termination date is designed to give Congress and HUD an opportunity to evaluate the effectiveness of this tax incentive.

B. Other Rental Housing—In the case of all other residential rental housing which is sold after December 31, 1969, the excess depreciation over straight line taken after December 31, 1969, will be recaptured under a formula wherein the 1 percent per month reduction in the amount of excess depreciation recaptured commences after a holding period of 100 months (8⅓ years). The effect of this change is to require the taxpayer to hold the property 16⅔ years (rather than 10 years under current law) before all gain to the extent of excess depreciation taken is taxed at capital gains rates.

C. Commercial/Industrial—In the case of commercial and industrial buildings sold after December 31, 1963, all excess depreciation over straight line taken after December 31, 1969, will be recaptured at ordinary income rates irrespective of the period the property is held by the taxpayer.

Note: The act applies the new recapture rules to excess depreciation attributable after December 31, 1969. Depreciation attributable to periods before December 31, 1969, is subject to recapture under current law. In addition, the act applies current recapture rules where the sale of the property was subject to a binding contract in existence prior to July 25, 1969, even though the transfer is to take place after that date.

Sales of Federally Assisted Low Income Housing

The act provides that gain on the sale of a federally assisted housing project (235 or 221(d)(3)) will not be recognized (i.e., not currently taxed) if the seller reinvests the proceeds of the sale in a second federally assisted housing project. To qualify for this "rollover" tax incentive the first project must be sold to tenants, a cooperative or other nonprofit organization, and the sale must be approved by HUD. As stated, no gain is recognized on the sale of the first project to the extent the proceeds of the sale are invested in a second project. The taxpayer's basis in the second project is reduced by the amount of gain not recognized on the sale of the first project. The holding period of the first project is taken into account in determining how long the second project is held but only to the extent the proceeds from the sale of the old project are reinvested in the new project.

Minimum Tax

In order to correct the situation wherein high income taxpayers pay little or no tax due to the use of special tax exempt income and/or special deductions (called tax preferences), the act provides a minimum tax on tax preferences which applies to individuals and corporations. Under the Act the total of tax preferences, after the deduction of a $30,000 exemption and the deduction of the taxpayer's regular Federal income tax, is taxed at a flat 10 percent rate. The

11 items of tax preferences which make up the base of the 10 percent minimum tax include: (1) Accelerated depreciation on real estate in excess of straight line depreciation, (2) amortization of rehabilitation expenditures in excess of straight line amortization, and (3) capital gains in the case of individuals to the extent of one-half the gains and, in the case of corporations, to the extent of 18/48 of the gain.

Miscellaneous

Under current law, members of cooperative housing corporations can deduct their pro rata share of taxes and interest if, and only if, the corporation qualifies as a cooperative housing corporation. To qualify, the corporation must derive 80 percent or more of its gross income from its tenant stockholders. The act provides that, in determining whether a corporation is a cooperative housing corporation, no account is to be taken of stock owned or units leased by public housing authorities. The effect of the change, effective December 31, 1969, will be to allow individual tenant stockholders to take the above deductions even though more than 20 percent of the cooperative housing corporation's income is derived from a governmental agency.

A Review of Federal Subsidized Housing Programs

By Milton P. Semer, Julian H. Zimmerman, Ashley Foard, and John M. Frantz
Semer and Zimmerman

Introduction

This review of the origins and development of Federal housing subsidy programs in the United States begins with the emergency programs undertaken during the Great Depression in the early 1930's. It might as suitably, perhaps have begun some decades earlier in Great Britain, where many of the institutional forms and social concepts that we were to borrow later were taking shape.

The study devotes what may seem to the reader at first glance to be a disproportionate degree of attention to the development, consideration, and ultimate enactment of the first really major subsidized housing program in this country—U.S. Housing Act of 1937. There is, however, solid reason for this treatment.

Close examination of the history of the 1937 act will reveal that, with minor topical exceptions, all of the issues were then developed and debated; all the ordinary means of housing subsidy were identified and recognized; all the major social and political motivations that make up the tissue of subsidized housing debate played their part in shaping the action finally taken. In the nearly forty years that followed, we have in the main been ringing the changes on old themes. It is, therefore, fundamental to an understanding of what followed to examine in some detail what the nation did, and what it thought it was doing in 1937, concerning the housing of its low income individuals and families.

In the interest of holding this narrative to a reasonable length, as well as maintaining some focus on the main issues, some highly specialized and relatively small housing subsidy techniques or programs have been treated briefly, or in some cases not at all. Thus, Mrs. Sullivan's "experimental" program for low income homeownership under FHA section 221(h) is mentioned only in passing. Rehousing grants to families displaced from urban renewal areas are not discussed. The GNMA-Tandem plan is mentioned but briefly because it is not in fact a subsidy program, but a mechanism for providing mortgage financing for projects that may be subsidized by other means, or, for economic reasons, that may be subsidized accidentally, as it were, through the mortgage price.

The study ends with the freeze on all housing subsidy programs imposed by the administration in January 1973, except for brief note of the administration's pending proposals for additional low and moderate income housing. No effort is made to track these in detail through the 1974 legislative process not only because of the intricacy of the subject but because the final outcome of that process remains shrouded in doubt and uncertainty.

It would be inappropriate to end this review without calling attention to a circumstance that must appeal to one's sense of the unconscious ironies of history. With the freeze clearly in place and holding, we have come almost full circle to where we were in 1937. Unless and until the executive and the Congress reach some new accommodation on a further course of action, the massive legislative accomplishments of 1949, 1954, 1959, 1961, 1965, and 1968 will lie lifeless and inert upon the statute books. Apart from its custodial functions over these inactive programs, what remains to the Department of Housing and Urban Development is the pair of tools with which it began: FHA mortgage insurance and housing subsidies under the U.S. Housing Act of 1937.

What perhaps has most greatly changed is their institutional setting. Mortgage insurance operates through a nationwide complex of mortgage banking and other forms of insured mortgagee institutions. Public housing subsidies operate through local housing authorities in cities, towns, and rural areas throughout the country. Both institutional systems today face deep and even perilous problems and difficulties—as do the programs that called them into being.

A Brief Glossary of Subsidy Systems or Techniques

Many people who are not engaged regularly in the management of subsidized housing programs sometimes find confusing the great variety of techniques or methods by which a subsidy may be extended, or as the economists like to say, "delivered," to a target family or group. For their convenience, there follows a brief summary of the principal subsidy devices that have been employed from time to time in this country, and that are discussed or referred to in this study.

Cash Payments to Public Owner-Sponsors: Payment of housing subsidies in cash to public bodies, agencies, or institutions has been authorized in three different forms:

Periodic Contributions: These are payments—usually annual—to reduce or offset all or part of the debt service costs of an assisted project, thus permitting lower rental charges than otherwise would be feasible. In the low rent public housing program, the Federal fixed annual contribution covers the portion of the long term debt service each year that cannot be met from operating receipts after provision for expenses and reserves. In the college housing program, Federal grants are made to the college for the difference between the actual debt service payments due on a project and the level of payments that would have been required on bonds carrying a 3 percent interest rate.

Initial Capital Contributions: The U.S. Housing Act of 1937 authorized, as an alternative to annual contributions, an initial capital contribution of up to 25 percent of the development cost of the project—thus relieving it, to that extent, of carrying charges and permitting lower rents. This alternative has never been used.

Operating Subsidies: These are used to increase project income, and thus avoid the necessity for rent increases to maintain solvency. Special operating subsidies are authorized in the low rent public housing program for units occupied by the elderly and handicapped, or by relocatees displaced from previous housing by governmental action. Such subsidies are also authorized to overcome operating deficits resulting from rising costs and statutory limitations on rent levels.

Cash Payments to Private Owners: Cash payments may be made to owners of rental housing to cover a part of the economic rent applicable to subsidized units, and thus make lower rents available to eligible occupants. Payments of this nature are made to lessees under the public housing leasing program and indirectly under the rent supplement program.

Cash payments also have been made to individuals to assist in the purchase of homes. In the early years of the GI program, veterans received modest sums called "gratuities" to assist them in purchasing homes. Under the urban renewal program, grants may be made to homeowners displaced from their homes by urban renewal action to assist them in obtaining standard housing elsewhere, and payments are made for moving expenses of displaced individuals and families.

Cash Payments to Private Lenders Related to Debt Service Costs: Cash payments are made directly to private mortgagees on certain insured mortgages in amounts equal to a certain portion of the debt service on the mortgage attributable to a particular unit. Such payments are applied to reduce the rent otherwise chargeable for that unit. This is the subsidy technique employed in the FHA section 236 program. A similar method is used to reduce the carrying costs of homeownership under the section 235 program. Substantially the same form of subsidy is authorized for similar classes of beneficiaries in the Farmers Home Administration's rural housing program.

Land Subsidies to Reduce Total Unit Cost: Federal surplus land may be sold at values that may be set taking into account their intended use for low rent housing. Similarly, the fair reuse value of land in urban renewal projects to be used for low and moderate income housing may be established taking the nature of the intended use into account.

Tax Relief: Partial or full abatement of local real estate taxes may be used as a method of reducing operating costs, thus allowing lower rents. Projects receiving annual contributions under the low rent public housing program are required to be exempt from local taxes, although certain payments in lieu of taxes are authorized to compensate the cities for such general municipal services as trash collection, police and fire protection, and the like. (Some State assisted programs, as in New York, use tax abatement as a method of achieving reduced rents.)

Below-market Loans: Loans at below-market interest rates are used to achieve artificially low debt service requirements, and thus permit the projects to operate at reduced rental levels. These have taken two distinct forms:

Direct below-market loans have been made by Federal agencies at interest rates fixed by statute or statutory formula to specified classes of borrowers. Examples among HUD programs are the direct loans formerly made to colleges and universities (and certain other institutions) for dormitory or faculty housing; loans to nonprofit sponsors of housing projects for the elderly or handicapped; and loans for rehabilitation of certain existing housing or small business properties (section 312). Similar direct loans are made by the Veterans Administration in rural areas, and to a limited extent by the Farmers Home Administration.

Indirect below-market loans result when a private lender is induced to originate the loan at a below-market rate on the basis of a commitment that he can sell the loan when completed to the Government, at a predetermined price acceptable to him. This is the method employed in the section 221(d)(3) below-market program, and in the FNMA-GNMA tandem operation.

Cash Payments Directly to Persons or Families of Low Income: Payments in cash directly to low income people for housing benefits (frequently called "housing allowances") have been used in the United States only on an experimental or pilot basis. Such an experimental program is now being conducted by HUD under special legislative authority. General support or welfare payments are widely made under federally supported State welfare programs. In some cases, these payments include an earmarked or set-aside amount for housing, and in other cases they may be used for such purposes as rent without a specified amount.

First Federal Housing Subsidies—Direct Construction

The first housing subsidies by the U.S Government were provided under the slum clearance and low income housing program of the Housing Division of the Federal Emergency Administration of Public Works (PWA).

That program was initiated in February 1934, but statutory authority for actual subsidies was not formally granted by Congress until June 29, 1936. Housing projects were constructed directly by the Federal Government (as distinguished from local public agency construction in the later low rent public housing program, pursuant to the U.S. Housing Act of 1937) [1] under the authority given in two major enactments that appropriated funds primarily to relieve unemployment through the construction of useful public works.

The first of those acts was the National Industrial Recovery Act [2] enacted June 16, 1933, which created the Federal Emergency Administration of Public Works (section 201) and required its Administrator, under the direction of the President, to prepare a comprehensive program of public works that would include among other things:

> (d) construction, reconstruction, alteration or repair under public regulation or control of low cost housing and slum clearance projects; . . .

Authority was given and funds were appropriated ($3.3 billion) to construct or finance public works under that program, including the making loans and grants to States and local public agencies.

The second was the Emergency Relief Appropriation Act of 1935 [3] enacted April 8, 1935, making additional funds ($4 billion) available for useful projects to provide relief and increase employment, including $450 million for "housing."

It is quite clear in context that the basic purpose of these measures, taken at the depth of the Depression, was to relieve suffering and put people to work. Provision of housing for families of low income was thought of not so much as an objective in itself, but as one among other socially useful means of accomplishing this broad purpose. Indeed, from the beginning, the efforts to utilize relief appropriations to provide housing for low income people ran into serious legal limitations and obstacles, as well as the numerous practical problems that are all but inevitable in pioneering operations in new fields of government activity.

Beginning in July 1933—even prior to the initiation of the low cost housing program of the PWA Housing Division—that Division had attempted to provide housing within the reach of low income families through mortgage loans made with appropriated funds to private limited dividend companies. The loans were long term (30 years) at 4 percent interest. According to Secretary of the Interior Ickes (also, by Presidential designation, the Administrator of Public Works), that approach was taken because of the absence in 1933 of local public bodies with authority under State law to undertake slum clearance and low cost housing projects, and thereby to qualify for, accept, and utilize PWA loans and grants for that purpose. That was in contrast to the powers of most cities and many other local public bodies to undertake other types of construction projects, for which they could and did receive loans and grants.[4]

[1] United States Housing Act of 1937 (50 Stat. 888 and amendments).

[2] National Industrial Recovery Act (48 Stat. 115).

[3] Emergency Relief Appropriation Act of 1935 (49 Stat. 115).

[4] Hearings before the Senate Committee on Education and Labor, 75th Congress, on S. 1685, "The United States Housing Act of 1937," Apr. 14 to May 11, 1937, p. 49.

Lending to limited dividend corporations was terminated in February 1934, because rentals in the assisted projects—at $10 per room per month—were determined to be in excess of what families of low income could afford. Rentals at those levels resulted from the absence of Federal subsidy, lack of eminent domain to hold down land costs, and the limited sponsor profit permitted.[5] Only 7 limited dividend housing projects were built with a total of 3,113 dwelling units.[6]

Because of the continuing absence of any substantial number of cities or other local public agencies with legal powers to undertake housing projects, the PWA Housing Division then turned to direct Federal construction and ownership, which it regarded as the only feasible alternative if a Federal initiative in housing construction was to be made an effective means of helping to meet immediate relief of employment problems.[7] Accordingly, the Housing Division proceeded to acquire land in many cities, select architects, draw plans, and advertise for construction bids.

From original total allocations of almost $400 million, a specific program of 79 low cost housing projects, to cost almost $250 million, was underway in the spring of 1935 when the Housing Division ran up against still another and much greater legal obstacle, one that all but destroyed the future of the program. This was the adverse court decision in the case of *United States* v. *Certain Land in the City of Louisville, Jefferson County, Kentucky*,[8] which ruled that Federal eminent domain power could not be invoked to carry out the program.

The decision of the Federal district court was upheld on July 15, 1935 by the Court of Appeals for the Sixth Circuit, which held that the general welfare clause in the Constitution does not authorize condemnation of private property for low cost housing and slum clearance. Provisions (section 203(a)(3)) of the National Industrial Recovery Act on eminent domain as applied to such housing were declared unconstitutional. It was held that housing is not a "public use," as required for eminent domain, on the ground that benefits of employment and aid to a limited group of low income people did not constitute a "public use." Some hope for a reversal of the lower court decisions in the case existed until the appeal was dismissed on motion of Solicitor Reed on March 5, 1936.

The power of eminent domain was essential in the assembly of most slum sites, so that the loss of that power effectively thwarted one of the basic statutory purposes of the program—the clearance of slums. Thereafter, the program could only continue with projects planned on vacant and available land, except in the rare situation where a locality, such as New York City, could acquire slum sites under State laws and transfer the property to the Federal Government.[9]

During the above litigation, the low cost housing program of the PWA Housing Division suffered a second major legal setback that came as a surprise and disappointment to its officials. Because no statutory provision dealt with the fixing of rentals in the projects, the Comptroller General of the United States concluded that no authority existed for making Federal subsidies to reduce the rentals. (The then Comptroller General, Mr. McCarl, was widely noted at the time for the very conservative tenor of his decisions. Also, it should be noted that at that time the Comptroller General exercised the power of prior review and approval of most Federal contracts and expenditures, as contrasted with the post-audit that became the prevalent practice some years later.) That conclusion was reached through two decisions.

The first of those decisions, on October 29, 1935,[10] concluded that funds under the two authorizing acts (the National Industrial Recovery Act of 1933 and the Emergency Relief Appropriation Act of 1935) were available for operating as well as construction costs of the housing projects in the program, but that all rentals and other receipts from operations must be covered into the Treasury as miscellaneous receipts without deduction (as required generally for Federal receipts under sections 3617 and 3618 of the Revised Statutes). In this connection, the Comptroller disapproved a proposal to lease a project to a private manager who would pay operating costs and return the excess to the Government—or in the event of a deficit, the Government would make up the loss. No statutory provision dealt specifically with the fixing of rentals in this housing.

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[5] Report by Secretary Ickes at above hearings, p. 21.
[6] Ibid., p. 20.
[7] Ibid., p. 21.
[8] *United States* v. *Certain Land in the City of Louisville, Jefferson County, Kentucky*, 9 Fed. Supp. 137 (Jan. 4, 1935), 78 Fed. 2d 684 (July 15, 1935), *certiorari granted* 296 U.S. 567 (Oct. 28, 1935), appeal dismissed on motion of Solicitor General Reed (Mar. 5, 1936).

[9] Hearings before the House Committee on Banking and Currency, 75th Congress, on H.R. 5033 and S. 1685, "The United States Housing Act of 1937," Aug. 3 to 6, 1937, p. 151.
[10] Decisions of the Comptroller General of the United States, Volume 15, p. 352 (A-65345), Oct. 28, 1935.

The second of the Comptroller's decisions, on January 17, 1936,[11] rejected a proposal of the Federal Emergency Administrator of Public Works that rentals in the first completed housing project (Techwood Project, Atlanta, Ga.), be established on a basis that would be within the reach of persons of low income, which was asserted to be one of the purposes of the authorizing legislation. The average rental for that purpose was determined to be $6.31 per room per month. To make that possible, it was proposed that 45 percent of the original cost of the project be written off as a grant, similar to grants being made to public works projects of local agencies, and the remainder of the original cost would be amortized over a 60-year period. That amortization was calculated to be feasible at the rentals proposed based on the amounts of the original project cost including carrying charges, all operating costs including payments to depreciation and other reserves, and the payment to the Treasury of 3 percent of the Government's original investment. (It was calculated that full amortization without the grant would have required rentals of $9.37 per room per month.)

The Comptroller General, rejecting that proposal, concluded that there was no authority to contemplate any loss whatsoever to the Federal Government in the sale or lease of the housing, and that rentals must be fixed in sufficient amount to amortize the full cost of the project that would bring in a net return on the money invested in the property equal to the rate the United States pays on its bonded indebtedness. The above statutory authority for providing "low cost" housing projects, being a secondary benefit to employment, was interpreted as conferring benefits on tenants only to the extent lower costs were brought about by "careful planning and quantity production." Any further reduction in rentals was held to be giving away Government claims without statutory authority, although the Comptroller did permit the exclusion of land costs from the required amortization if interest were paid on an amount equal to the cost of the land.

No authority for housing subsidies to the program existed until the enactment of the so-called George-Healey Act[12] on June 29, 1936. That relatively obscure statute was actually the first clear congressional authorization for subsidies in a Federal housing program. Among several provisions relating to these PWA Housing Division projects, the act (at section 4(a)) provided:

> In the administration of any low-cost housing or slum-clearance project described in section 1, the Federal Emergency Administrator of Public Works shall fix the rentals at an amount at least sufficient to pay (1) all necessary and proper administrative expenses of the project; (2) such sums as will suffice to repay, within a period not exceeding sixty years, at least 55 per centum of the initial cost of the project, together with interest at such rate as he deems advisable.

The stated purpose of that provision[13] was to make it possible to operate the housing projects at rents within the financial reach of persons with low incomes. Under the quoted language, the tenants were given the benefit as to resulting rent levels of a capital grant of 45 percent of the cost of the project.

As noted by Secretary Ickes, rents were also favorably affected in many cases by assistance from municipalities in the form of donations of property, provisions of parks and recreational facilities adjacent to projects, provision of streets and sidewalks without assessment, and furnishing of services at reduced rates.

Section 4(b) of that 1936 act also contained the first provision on tenant selection:

> Dwelling accommodations in such low-cost housing or slum-clearance projects shall be available only to families who lack sufficient income, without the benefit of financial assistance, to enable them to live in decent, safe, and sanitary dwellings and under other than overcrowded housing conditions: *Provided,* that no family shall be accepted as a tenant in any such project whose aggregate income exceeds five times the rental of the quarters to be furnished such family. The term 'rental' as used in this subsection includes the average cost (as determined by the Federal Emergency Administrator of Public Works) of heat, light, water, and cooking, where such services are not supplied by the lessor and included in the rent.

Under those provisions of the George-Healey Act, average rentals ranging from $3.97 to $5.88 per room per month, excluding utilities, were established for the 9 projects on which rentals were fixed at the time of the congressional hearings on the proposed U.S. Housing Act of 1937; the average annual income of families was $947 in the 3 projects in operation at the time.[14]

(In addition to its provisions relating to housing subsidies, the George-Healey Act contained some other matters of historical interest at this early stage. Thus (1) it waived exclusive Federal jurisdiction over property acquired by

[11] Ibid., p. 619 (A-65368), Jan. 17, 1936; see also Volume 16, p. 617 (A-82300), Dec. 23, 1936.

[12] George-Healey Act (49 Stat. 2025).

[13] Secretary Ickes in his report furnished at the above hearings of the Senate Committee on Education and Labor, p. 37.

[14] Ibid., p. 50.

PWA for housing and slum clearance, and (2) it authorized PWA to enter into agreements to pay local public bodies amounts in lieu of taxes. These sums were to be based on the costs of local services furnished to the property, taking into consideration the benefits to be derived by the State or locality from such property.)

Primarily because of the above problems of the PWA Housing Division program, it was greatly reduced from its original plans. Also, substantial amounts of funds previously allocated for the program had been diverted for other relief efforts. In all, housing projects with allocations totalling $200 million were dropped although ready for action.[15] Under the final program, 50 projects costing about $135 million were built in 37 cities providing about 21,600 dwellings for low income families. The number of projects built on sites of former slums was reduced to 27.[16]

One additional factor affecting the decisions that curtailed, and eventually ended, the PWA Housing Division program was its limited statutory objective. From the beginning, the program had been conceived as an emergency measure designed primarily to provide employment, as distinguished from a program carefully planned and developed to meet long range goals. As also previously noted, the PWA Housing Division went to direct Federal construction because there were not enough local agencies with adequate legal powers to undertake the projects. As early as December 1934, however, the President wrote the governor of each State suggesting enabling legislation for the creation of local agencies with powers to undertake housing for persons of low income and providing for tax exemption and other assistance to such housing by States and localities.[17] A new alternative Federal housing program of assistance to localities was becoming more feasible as States enacted more of these laws. By April 1937, they had been enacted in 27 States, with drafting and other technical help by PWA.

Although the volume of completed housing under the PWA Housing Division program fell well below original plans, it constituted an operation of greater significance than is generally recognized today. The volume of production was substantial in terms of a brief Government operation getting underway in an entirely new field.

More important, but less recognized today, was the pioneering work done then in coping with the basic problems generally confronted in public housing operations. Many major policy decisions made at that time have influenced developments through the years. The problems of land acquisition and assembly, including the significance of eminent domain, have been mentioned. Conclusions had to be reached on the types and standards of construction necessary to achieve low maintenance and operating costs to keep rentals at a minimum. The early projects had the usual community relations problems, and were opposed by some groups with substantially the same arguments that have been used against public housing in recent times. From the beginning of the program, substantial attention was given to the relocation of displaced families. Secretary Ickes reported at the hearings on the proposed U.S. Housing Act of 1937 that about 9,000 of those families had already received assistance in obtaining dwellings, and that these dwellings were generally superior to their former ones but often had slightly higher rentals.[18]

A Search for a Better Way— The U.S. Housing Act of 1937

I may say in passing that during my time in the Senate I have never advocated legislation which was of such a noncontroversial nature.

Senator Wagner
1937 Congressional Record 10357

The U.S. Housing Act of 1937 [19] inaugurated the first major American experiment in housing directly and explicitly subsidized with public funds. Almost 40 years later it is still by far the largest program in which public subsidies are employed in an effort to ameliorate the disadvantage under which lower income families and individuals have found themselves in an affluent society. For even in 1937 America was an affluent society by comparison with the circumstances of most of the world—notwithstanding that the initiative toward subsidized housing came while the nation was still in the grip of the most severe and prolonged economic depression in its experience.

The new act authorized Federal loans for the development of public housing and "slum clearance" projects, and provided for either capital grants or annual contributions to assure their continued availability to low income people. It required a local contribution to the subsidy but

[15] Ibid., p. 25.
[16] Ibid., p. 32.
[17] Ibid., p. 50.
[18] Ibid., p. 35.
[19] Public Law 75-412, Sept. 1, 1937.

permitted this to be accomplished through local tax exemption. It was designed to encourage the construction of housing for the poor; but it also required destruction, on a one-for-one basis, of substandard housing as new units might be built. Further, however, in recognition of the dubious feasibility of such "equivalent elimination" in many if not most communities, it authorized the demolition of substandard structures to be postponed where it was determined that the immediate results would be overcrowding and hardship.

Although the original legislation has been marvelously reworked and elaborated over the years, the 1937 act can legitimately be said to establish the basic framework and the general conceptual scheme that even today we know as the "public housing program."

As of June 30, 1973, there were some 1,088,000 units in management (i.e., occupied or available for occupancy) in the program. The annual subsidy pledged to meet debt service requirements amounted to $587.8 million and was rising. To this figure must be added an additional $514 million of payments for leased units and for operating subsidies of various kinds—a figure which also was clearly destined to rise in future years.

While exact figures were never kept, it is evident that several million families and individuals have been served—however well or ill—by the program over the years. No other program of subsidized housing in the United States has been active over so long a period. None has been involved in the construction of so large a number of units. None has affected the lives of so many people. None has generated such bitter, continuing controversy. None has brought into existence such a variety of new institutions, skills, and professional organizations. None has involved a like expenditure of the public funds.

In approaching a chronological examination of the history of Federal legislation for subsidized housing in the United States, therefore, it seems worthwhile to inquire in some detail into the circumstances of the birth of this program in 1937. What did the Congress and the program's sponsors think they were seeking to accomplish? What did the opponents think they were opposing, and why? What bearing do these matters have on the later history?

1935

Serious consideration of the legislation that ultimately would authorize the public housing program began in 1935.

Not all the moving forces behind the legislation are clearly discernible in its formal history. To some degree, it clearly reflected disillusionment with the earlier efforts of the Resettlement Administration and the Housing Division of the Public Works Administration. The projects developed by these agencies—primarily as one among many devices to combat unemployment—had been afflicted with site controversies, high development costs, long delays in completion, and rent levels that, though below those in the private market for comparable housing, were still considerably above what many had hoped for and expected.

Another source of difficulty for these early programs was the uncertainty surrounding their objectives. In the minds of some supporters their main purpose was to put people to work; others saw them as providing a kind of cultural bridge between urban and rural life—the urban worker fortified by his open space and his garden. Still others hoped for an American adaptation of the British greentowns experiment—an early and (in England) quite reasonably successful effort to develop what later came to be called a "new towns" approach.

A more concrete and practical motivation, however, is probably to be found in the decision of the Circuit Court of Appeals in the case of a project in Kentucky,[20] which severely limited the ongoing PWA program at that time. The court held, in substance, that housing and slum clearance were not such public purposes as would bring the acquisition of land for them within the power of the Congress under article I of the Constitution to "provide . . . for the general Welfare." The ramifications of this decision were extensive.

Its immediate thrust was to bar the use of the power of eminent domain for Federal housing projects. This immediately limited the available sites for such projects to those obtainable through negotiation and purchase in the open market. Moreover, it effectively set the land values for such projects at the price that a canny seller could exact from a needful buyer, or a buyer open to political or other indirect pressures. Because PWA had no explicit authority to subsidize rents, an upward pressure on site costs implied higher development costs and hence even higher rent levels.

The Supreme Court accepted the Louisville case for review, but the Government, perhaps

[20] *United States* v. *Certain Land in the City of Louisville, Jefferson County, Kentucky,* 78 Fed. 2d 684, *certiorari granted* 296 U.S. 567, appeal dismissed 297 U.S. 726 (1936).

concerned about the effects of a possible adverse decision on other cases at various stages of judicial review, decided at the last moment—on the morning of the day on which the Court had set the case down for oral argument—to withdraw its appeal. This decision engendered some bitterness among the dedicated proponents of a public effort to improve housing conditions, including some lawyers who felt that there was a reasonably good prospect of obtaining a decision overruling the circuit court. However that might have been, the decision of the Department of Justice not to proceed further ended the case.

In this general context, Senator Wagner of New York introduced S. 2392 of the 74th Congress—"A Bill to Promote the Public Health, Safety, and Welfare by Providing for the Elimination of Insanitary and Dangerous Housing Conditions, to Relieve Congested Areas, to Aid in the Construction and Supervision of Low-rental Dwelling Accommodations, and to Further National Industrial Recovery Through the Employment of Labor and Materials."

S. 2392 would have established a permanent Division of Housing within the Department of the Interior. The emergency-born Division of Housing was then located in the Federal Emergency Administration of Public Works (PWA). The Administrator was Harold Ickes, who was also Secretary of the Interior. The arrangement proposed in the bill was, therefore, more than a formalistic change, because PWA was not actually in Interior, but rather was directed by an Administrator who happened also to be Secretary.

S. 2392 also would have authorized appropriations of $800 million for loans and grants to "encourage, aid, assist, and cooperate with local public-housing bodies to formulate and to execute slum clearance and low-rent public-housing programs and projects." Thus in this earliest version the legislation acknowledged receipt of the message from the Court: The Federal Government was prepared to bow out as the principal sponsor, owner and manager of public housing projects; henceforth, its role mainly would be to give financial assistance to State and local agencies. The term "local public housing body" was defined to mean ". . . a State, territorial, county, or municipal housing corporation or authority, authorized and empowered by statutory enactment to clear slums and/or to provide housing at a low rental for persons of low income." [21]

It is worthy of note that the "Declaration of Policy" proposed in this forerunner bill, after referring to "congested and insanitary housing . . . which seriously affect the public health, safety, morals and welfare . . . of the American people," laid down a gloomy conclusion that future experience was not substantially to change: "It is found that the correction of these conditions is impossible by private initiative and funds . . . ." [22]

What strikes the contemporary viewer in this review of the proposed bill is the variety and disparity of purposes that were thought to be the object and justification of the legislation. Its sponsor, Senator Wagner of New York, chose to remain on the sidelines and let others speak for the purposes of his bill.

Representatives of the Public Health Service viewed the proposal as dealing with abatement of health hazards. They called attention to the typical lack in the slums of adequate ventilation, sewage disposal, screening, and pure water, and the resulting prevalence of tuberculosis, pneumonia, typhoid fever, diphtheria, and other ills.[23]

The witness who spoke for the United Mine Workers applauded the measure as in the interest of economic recovery and the provision of better living standards for low income workers, but he saw it more specifically as offering a means of breaking through the company town arrangements then prevalent in mining areas, and thus of redressing the imbalance of strength between owners and workers in the collective bargaining process.[24]

Rabbi Israel, Vice President of the National Public Housing Conference, saw the justification for the proposed program mainly in what he thought would be its remedial effects with respect to crime, juvenile delinquency, and infant mortality.[25]

A spokesman for the National Urban League quoted with approval the statement of a former Secretary of Commerce that, "The Negro's housing problem is part of the general problem of providing enough housing of acceptable standards for the low income groups in our society." Nevertheless, he went on to support the bill on the premise that it might help to solve the special housing problems of the black communities of the nation.[26]

The witness on behalf of the Building Trades Department, American Federation of Labor, called attention to the high rates of unemployment in the building trades. Although he made it

[21] S. 2392, 74th Congress, 1st Session, sec. 9.

[22] Ibid., sec. 1.

[23] Hearings before the Senate Committee on Education and Labor, 74th Congress, 1st Session, on S. 2392, June 4-7, 1935, p. 7 ff.

[24] Ibid., pp. 11-12.

[25] Ibid., p. 13.

[26] Ibid., p. 16.

clear that he was not appearing to endorse any particular bill or proposal, he urged that something be done promptly to meet a "twofold purpose"—i.e., to stimulate employment in construction and to relieve the housing conditions of low income workers.[27]

Other witnesses called attention to the deplorable conditions existing in the slums: overcrowding, disease, filth, infestation by rats, and ruthless profiteering on the part of mainly absentee landlords.

Only one witness—Catherine Bauer—made any serious effort to give the Senate Committee on Education and Labor a broader sense of perspective concerning the sweep of the problems in which it was embroiling itself. In language that reads as aptly today as when it was used 40 years ago, she told the committee:

> The major part of the housing problem is a simple economic fact: Ordinary private enterprise is totally unable to provide adequate new housing at a rental or sale price which families in the middle and lower income groups can pay. This situation is apparently permanent in our national economy.[28]

The chairman pointed out that the 14 million units that the witness had said were needed in the next 10 years would involve, at 1935 costs ($4,000 per unit) an investment of $56 billion. Miss Bauer was unmoved. "There is no way out . . ." she told the chairman.

The highly pragmatic flavor of much reaction to the proposal is abundantly clear in the record. Thus, for example, the Associated General Contractors filed a statement supporting the bill, but urged that it be amended to provide that the projects would be constructed through competitive bidding.[29] The Council of Real Estate Associations, on the other hand, sent a letter in opposition, predicting that enactment of such a bill, ". . . will destroy existing real-estate values and will prevent local municipalities from collecting taxes which they need so badly at the present time." [30]

Only two organizations appeared in outright opposition. The President of the Bronx Borough Taxpayers League told the committee,

> We believe that it [the bill] is going to be the beginning of the end of private ownership of real estate. If we are going to have communism and socialism we prefer to go about it in a straightforward way and not in a roundabout way.[31]

[27] Ibid., p. 26.
[28] Ibid., p. 86.
[29] Ibid., p. 212.
[30] Ibid., p. 213.
[31] Ibid., p. 213.

A spokesman for the Real Estate Owners Association of the 12th and 19th wards of Manhattan took a slightly less apocalyptic view. "We want to be recorded in opposition," he said,

> . . . for we feel there is no necessity for any construction, and the right thing to do would be to rehabilitate the old houses, because they are the only things that can produce a low rent.[32]

The year 1935 was one of gestation only. The Senate hearings identified many of the needs, the problems, and the forces at work for and against a Federal initiative in this new area. However, neither the House nor the Senate took action in the 1st session of the 74th Congress.

1936

In the 1935 hearings, some witnesses with long professional involvement in housing matters had expressed a preference for some of the specific provisions contained in a bill introduced by Representative Ellenbogen of Pennsylvania, as compared with those in Senator Wagner's version. Mr. Ellenbogen's 1935 bill did not even reach public hearings, but the message was not lost on those in Congress anxious to procure some form of legislation.

There appears to have been no question that Senator Wagner of New York generally was assumed to be the leader of and spokesman for what may loosely be called the public housing effort. By the time the 2nd session of the 74th Congress turned to these matters, the Senator and Mr. Ellenbogen had accommodated their views, and introduced identical bills—S. 4424 and H.R. 12164. The new bills included not only many of Mr. Ellenbogen's ideas, but also refinements and improvements which originated with a number of people in private and public life with whom they consulted informally.

As a result the relatively brief and general bill proposed in 1935 was replaced by a much more carefully drafted, more complex piece of legislation.

Presumably to facilitate the development of a consensus in support of the bill, the diverse motivations of those supporting it were not so much sorted out or clarified as embraced, in one catch-all statement of purpose in which anyone at all favorably inclined might find something to which to respond. After various findings of fact, the bill set forth that:

[32] Ibid., p. 139.

It is hereby declared to be the policy of the United States to promote the general welfare of the Nation by employing its funds and credit, as provided in this Act, to assist the several States and their political subdivisions to alleviate unemployment and to remedy the unsafe and insanitary housing conditions and the acute shortage of decent, safe and sanitary dwellings for families of low income that are injurious to the health, safety and morals of the citizens of the Nation.[33]

This language survived with only minor changes in the 1937 act as finally agreed to. Principal changes were the addition of a reference to "present and recurring" unemployment, and a phrase making clear that the objectionable conditions existed in both urban and rural areas.

What is notable about the quoted statement is that, although it commits the Congress to look favorably upon full employment, good health and safety, and sound moral standards, it conspicuously says nothing about housing policy as such, except as that may be deemed to be ancillary to the ends actually spelled out.

Conceivably, the authors of this paragraph intended to put the Congress on record as saying that—as a matter of national policy—all Americans should be decently housed, regardless of their economic status and capacities. If so, they grievously failed. What seems more likely is that they deliberately avoided such a challenge out of deference to the immense figures such an undertaking would involve (e.g., the $56 billion mentioned the year before by Chairman Walsh to the unflinching Miss Bauer), and out of an abundance of caution about seeming to invade what might be thought to be the preserves of private enterprise. In either event, it is not too extreme to think that in this formulation a profoundly disabling ambivalence was built into the American approach to subsidized housing which was to plague it far into what then was the distant future.

The new bill featured many refinements and some new inventions. The 1935 bill had included only one defined term—"local public housing body." This was defined as ". . . a State, territorial, county, or municipal housing corporation or authority, authorized and empowered by statutory enactment to clear slums and/or to provide housing at a low rental for persons of low income." S. 4424 added a number of other important terms to the technical language: "low-rent housing," "families of low income," "slum" and "slum clearance," and others. Of particular significance, perhaps, was the definition of "families of low income," who were declared to be those who,

. . . cannot afford to pay enough to induce private enterprise in their locality to build an adequate supply of decent, safe and sanitary dwellings for their use.[34]

Clearly, this was one of a number of opportunities to define such families (for housing purposes) as those who could not afford, by some reasonable and generally acceptable test, to house themselves decently without some form of assistance or subsidy. Instead, the approach selected was a definition that did not in fact identify anybody, and that mainly served to soothe those who were apprehensive about the possibility of Government competition with private business. Here, perhaps, can be discovered the first roots of such moral and ethical dilemmas as the "20 percent gap" which entered the picture at later stages.

Instead of a Housing Division in the Interior Department, the new bill would have established a U.S. Housing Authority headed by a five-man board, of which the Secretary of the Interior would be one member, ex officio.

Provision was made for grants up to 45 percent of total development or acquisition cost, payable either in full in advance or deferred (in whole or in part) in the form of an annuity to be paid over a period not to exceed 60 years. Appropriation of $326 million over 4 years was authorized for grants.

Also authorized were loans to public housing agencies and "limited-profit" (i.e., private) housing agencies, up to the full amount of the development cost (less any initial capital grant) in the former case, and up to 85 percent in the latter. Borrowing authority of $650 million was provided to the authority to obtain funds for such loans.

Finally, the bill provided for "demonstration" —that is, federally built and operated—projects, ". . . to demonstrate to localities the benefits to be derived therefrom."

The general themes of support and opposition which had been evident in the 1935 hearings were repeated in 1936, although it is clear that the hearings were more definitely purposeful, the witnesses more concerned, and the appearance less pro forma than the year before. The Secretary of the Interior endorsed the bill,[35] as did the Secretary of Labor. (In passing, Secretary Ickes threw some light on the troubles of the

[33] S. 4424, 74th Congress, 2nd Session, sec. 1.

[34] Ibid., sec. 2 (1).

[35] Hearings before the Senate Committee on Education and Labor, 74th Congress, 2nd Session, on S. 4424, 1936, p. 19.

PWA emergency housing program, which may have a bearing on his interest in finding a new approach. According to his testimony, of some $400 million of emergency funds allotted for housing projects, considerably more than half was impounded and reprogramed for other purposes before it could be used.) The labor movement was represented this time by no less than the President of the American Federation of Labor, William Green, who endorsed it with the observation that,

> We regard the measure as of deep economic and social significance, and we interpret it as being in a very large degree a remedy for unemployment.[36]

That Mr. Green's endorsement was intended as something less than an all-out declaration of war on substandard housing is suggested by his testimony that he could identify four important points in the pending measure. Two of these were the necessity of " . . . adequate safeguards against Government competition with legitimate private enterprise," and " . . . measures to keep down the Federal expenditures to the minimum . . . ." He did, however, use a phrase that this and subsequent committees were to hear many times in the years that followed. "We are face to face" he told the committee, "with an acute housing shortage."[37]

That the private sector did not view Senator Wagner's bill with universal hostility is made clear by the appearance, for example, of a witness on behalf of the prestigious banking and investment firm of Blythe & Company of New York, who warmly endorsed the bill, with the observation that it should mean ". . . private capital can be drawn into the investment field of low-rent better housing under the terms of the bill." [38] (An astute and far-sighted observation. By the 1960's, of course, guaranteed tax-exempt notes and bonds of local housing (and later urban renewal) agencies had become the largest single component of the national market in State and municipal obligations, but at the time Mr. Couffer appeared these instruments had not even been invented, much less sold in the market.) The publisher of the Philadelphia Record and the New York Evening Post not only supported the bill, but took the trouble to attend the Senate hearings to say so in person.[39] The chairman of the Federal Home Loan Bank Board spoke with high favor of the objectives of the legislation (although he admitted he had not had time to study it in any detail).

Although the record seems clear that support for the legislation had increased from 1935 to 1936, it seems equally clear that there was little, if any, more agreement among its supporters as to precisely what they were in favor of, and why. Senator Wagner himself in presenting his bill to the committee, virtually brushed off the subject of housing and bore down heavily on his expectation that the new program would contribute to economic recovery and the relief of unemployment. Other witnesses supplied their own notions of the aims that the legislation was to achieve. An example both representative and comprehensive was the support offered by a Mr. Colleran, President of the Operative Plasterers and Cement Finishers International, AFL. Of a bill ostensibly addressed to a solution for the nation's vast and intractable housing problems, Mr. Colleran said:

> Now, in conclusion, we heartily approve and pray for the passage of this housing bill, for the reasons, first, of its potentialities toward the relief of unemployment; second, for its long-range planning effects which will stabilize employment; third, for its slum clearance, which will help eradicate sickness and pestilence, which, in turn, will lessen crime; and, finally, this is the "big push" that was needed to end depression.[40]

So much for a national housing policy—a subject to which the Congress would not specifically address itself for another 13 years.

The grounds of opposition on the part of those who appeared to state their views were also much the same, though the record does not reflect other arguments that undoubtedly were made in private offices and in the hallways of the Capitol. Mr. Pederson of the New York Council of Real Estate Associations, restated the warnings of doom:

> We believe that it would be the beginning of the end of private ownership, and it will eventually create communism and chaos, and we are opposed to it for that reason . . . .[41]

Viewing the problem in general, and differing widely from Mr. Green of the AFL, Mr. Pederson observed that, "We do not believe that any housing shortages exist in any part of this country."[42] He urged the use of the abundant vacancies which he said were available and "habitable and sanitary" (as well as cheap), and stressed the importance of tenant maintenance. He called the committee's attention to certain

[36] Ibid., p. 76.
[37] Ibid., p. 81.
[38] Ibid., p. 109.
[39] Ibid., p. 149.

[40] Ibid., p. 180.
[41] Ibid., p. 336.
[42] Ibid., p. 331.

properties with which he was familiar that were ". . . just as clean and wholesome as any apartments I have seen." He continued, "Of course, there were no modern improvements, no bathrooms, no electric lights in the apartments." [43]

It was Mr. Pederson also who offered a thought that was to be echoed many years later as part of the reasoning for suspending the subsidized housing programs that had evolved over the intervening years. Challenged by the committee to propose something, he observed: "The root of the evil is the people do not earn enough money to live in what the proponents of this bill call decent housing accommodations."

Mr. Herbert Nelson, appearing on behalf of the National Association of Real Estate Boards, questioned the necessity or desirability of creating yet another Government agency to deal with housing. He said:

> I have here a pamphlet issued by the Government called "Services of the Federal Government to Home Owners and Tenants," and the first page of this pamphlet lists more than 40 present agencies set up by the Federal Government to deal with various questions in the housing field.[44]

Mr. Nelson went on to make the somewhat baffling observation that:

> It is our feeling that in this country there is no particular necessity to subsidize housing projects, that we have not so much a slum problem as a problem of blighted, or run-down areas where people do not like to live and where it is difficult to maintain desirable housing conditions, which lead, of course, to undesirable social results.

If there was little new in the arguments for or against the Wagner bill of 1936, there were, scattered through the record, suggestions of potential problems—clouds, perhaps none of them larger than a man's hand. Certainly, none then suggested the thunderstorms that would some day gather around each of these issues, and bring to grief the very program which at that time was being so ardently supported by the very witnesses who raised them.

A few examples will suffice to illustrate this perspective.

S. 4424 as it lay before the committee was very clear in specifying that annual contributions—where these were chosen over the alternative possibility of initial capital grants—were to be provided for in a contract "guaranteeing such fixed and uniform payments over such fixed period" (i.e., a period not exceeding 60 years, regarded as an alternate choice to the loan provision).[45]

It is clear that this provision was intended to reflect what its proponents believed to be one of the key elements in the British public housing program, from which many of the concepts of the American legislation were drawn. Dr. Edith Wood defined this aspect of the British lesson for the committee in these terms:

> . . . it has always taken the form of fixed annual subsidies to the local authorities which build and operate the houses, and also fixed for a given number of years, so in undertaking any housing projects the local authority could know exactly what it had to count on per house.[46]

Later, for a variety of reasons which will be touched upon, the American plan was modified so that only the number of years was "fixed," and only the debt service was "guaranteed." The result was that while the bondholders "could know exactly what [they] had to count on," the local authorities could not. In time, this seemingly innocuous change was to have (and is still having) profound effects on such diverse matters as standards for initial and continuing occupancy, policies for fixing rent levels, policies governing maintenance and operating reserves, and still others.

Related to the question of a fixed annual contribution was the doubt expressed by some as to whether another approach to subsidizing low rent housing might not be preferable. Foreshadowed in these early discussions were techniques which were later undertaken under such programs as rent supplements, sections 235 and 236, and the ongoing housing allowance experiments.

Thus, the then Secretary of Labor, Miss Perkins, argued that the provisions of the bill would require some sort of means test for the occupants of public housing, which she said would be ". . . very difficult to administer, and very repugnant to our ordinary point of view in American life . . . ." As an alternative, she suggested:

> I think it would be a much better approach if the Government provided for it on a basis of, say, an annual subsidy of the difference between the economic rent on the building which is built under the stimulated plan and the rent which those living in it can afford to pay.[47]

By contrast, Miss Bauer, one of the more widely recognized housing specialists to appear before the committee, referred to the various

[43] Ibid., p. 332.
[44] Ibid., p. 311.

[45] S. 4424, 74th Congress, 2nd Session, sec. 9 (b).
[46] 1936 Hearings, op. cit., p. 213.
[47] Ibid., p. 63.

proposals then being advanced for "rent subsidies," and observed:

> . . . apparently . . . what most people mean by it, [is] that a subsidy should be provided directly to each family in accordance with that family's need.
>
> That means a variable subsidy changing with each family in each apartment or each house, and also changing, presumably from one month to another, or at least one year to another.
>
> That is absolutely impossible of administration, there would not be any way to carry out such a subsidy.[48]

Dr. Wood addressed herself to the same subject. She pointed out that subsidies would take any of five forms: "(1) lump-sum grants, (2) interest subsidy, (3) fixed annual grants . . . , (4) tax exemption, or (5) rent subsidy." She strongly advocated following the British example in the form of fixed, uniform annual subsidies.

Alluding to the support of rent subsidies by the Chamber of Commerce and the building and loan associations, she suggested that ". . . what they meant was family relief locally administered." She grounded her objection to this, not upon its inherent administrative difficulties, but on principle:

> . . . I want to state emphatically that to give any such trend as that to our legislation would be to defeat the whole purpose and end in view. It is not family relief we are after; it is the beginning of remedying a Nation-wide condition, the housing of a very substantial share of the population . . . who are unable to pay a high enough rent to induce private enterprise to build modern houses for them.[49]

Thus, more than a year before the U.S. Housing Act of 1937 was actually enacted, Dr. Wood propounded a fundamental question to the committee: What is, or should be, the objective of such a program? Is it in essence a form of welfare assistance to the needy, or is it on the other hand "remedying" a nationwide housing condition? The question remained unanswered, and still does. Dr. Wood's dilemma is as alive, as relevant, and as unsettled in 1974 as it was in 1936.

Another issue that was to loom larger with the passing years was touched on by Mr. Grimm, a real estate man who apparently appeared on his own behalf because of his interest in the subject matter. In the course of a statement covering a variety of matters, Mr. Grimm remarked:

> It is hardly conducive to diligence or the will to earn and save to find that the fruits of one's labor can purchase less desirable homes than are provided for those who cannot or will not earn or save as much.[50]

Mr. Grimm may not have worded his point ideally, but nevertheless he had put his finger on a grave difficulty that was to plague the public housing program increasingly with the passage of time: How is the policeman, the postman, the schoolteacher, the clerk, or the farmer to be persuaded that it is equitable to tax his barely sufficient income in order to provide housing for still lower income families at a higher standard than he can afford for himself, and for which he is declared to be ineligible on the ground that his earnings are too high to admit him to these benefits? There was no comment—then—on the massive psychological and political stumbling block which Mr. Grimm thus pointed out.

Speaking many years before a majority of the Congress was prepared to listen, Walter White, Secretary of the NAACP, urged that,

> It should be made clear in the act that these housing projects shall be available to all Americans without regard to race, creed, or color.[51]

This should be done, he told the committee, not merely to pay lip service to the American ideal, but on practical grounds as well, and he cited the tendency of local governments to provide Jewish and Negro projects a lower standard of municipal services such as street paving and lighting, and police and fire protection. Mr. White was thanked for his appearance.

Of somewhat less import perhaps, but nevertheless of interest in the light of the subsequent evolution of the program, was a cautionary note sounded by a Kansas City developer. Pressed for his general view of the bill, he conceded the need for slum clearance, although he said that in his opinion the extent of the housing need was being exaggerated. He proposed what we would now call large-scale rehabilitation, plus the building of new low cost homes. In discussing costs he mentioned such matters as reform of building codes and the possibility of making greater use of factory fabrication. But he also told the committee:

> It has not been our experience that when you go out and build 50 houses, or a hundred houses, that there is a saving in cost over building two or three houses at a time. I have seen a good deal of statements by people that are quoted on the subject that there can be a saving of as much as 20 percent in building 50 or 100 houses at one time. That has not been our experience. . . . The cheap homes that are built today are built by an individual builder who builds two or three at a time. He has no office, he has no salesmen, he works on the job himself, he watches every expenditure, and as a rule he can build the

[48] Ibid., p. 189.
[49] Ibid., p. 213.
[50] Ibid., p. 198.
[51] Ibid., p. 208.

house just as cheaply as those who build 50 to 100 houses at one time.

I think that is where the Government is going to be disappointed in this project, by expecting that it can build houses more cheaply by building a large number at a time.[52]

How many of those then involved recognized the significance of these fragments of handwriting on the wall is no longer possible to determine. In any event, they appear not to have greatly swayed the legislative process. When the Senate committee favorably reported the bill, the ambivalence with respect to its purpose appeared full blown in the language with which it opened its presentation:

During the past 3 years, the Federal Government has been committed to the policy of encouraging the development of safe and sanitary homes for persons of low income. [This is itself a highly dubious assertion, in the context of the times.] General agreement has been reached that this line of activity promotes the creation of useful employment opportunities for capital and labor, and at the same time ameliorates living conditions that are conducive to ill health, crime, and other social evils.[53]

The committee also said—no doubt with a predominantly tactical purpose, but not less significantly—"The bill represents a clarification and simplification of governmental procedure rather than an innovation." [54]

The report included too what would appear on its face to be an answer to the basic question posed by Dr. Wood:

The committee is convinced that in dealing with the housing of families of low income, systematic low rent housing should be substituted for relief. This procedure will be cheaper for the Government, more beneficial to business, and infinitely more desirable to those of our citizens who are now living in slums and blighted areas . . . .[55]

The flourish appears to have been purely rhetorical, however. Nothing else in the report, or indeed in the bill itself, suggests that the committee was so persuaded, let alone "convinced."

One change that the committee made in Senator Wagner's bill is of particular significance in retrospect. Obviously dissatisfied with the fact that the definition of "families of low income" proposed in the bill failed to define such families, the committee undertook a new approach. "Families of low income," the bill as reported said, means,

. . . families who lack sufficient income, without benefit of financial assistance, to enable them to live in decent, safe, and sanitary dwellings and under other than overcrowded conditions: *Provided, That* no family shall be accepted as a tenant in any low-rent-housing project whose aggregate income exceeds six times the rental of the quarters to be furnished such family.[56] [Amended on the floor to five times the rental.]

By this change, the committee injected into the bill the concept of a fixed mathematical relationship between eligibility, income, and rent levels—an inherently complex concept which was to become more complex with the passage of time and the evolution of the program, and the ramifications of which, it seems certain, have not yet been fully worked out.

One other set of related changes struck a note of warning concerning what lay ahead for the proposal that the committee had described as a mere clarification of procedure, rather than an innovation: The proposed authority for $650 million in borrowings by the new U.S. Housing Authority (USHA) was reduced to $450 million, and the authority for appropriations for grants from $326 million to $10 million.

The Senate debated and passed the bill by a comfortable margin (42 to 24), and with little substantive change. But the Congress as a whole was not yet ready to act. The House took no action on the Senate bill (nor on the companion bills on the House side), and the whole matter thus went over for consideration in the 75th Congress.

1937

On the 24th of February in the 1st session of the 75th Congress, Senator Wagner introduced S. 1685, the bill that was destined to become the U.S. Housing Act of 1937.

Mr. Wagner's new bill followed very closely the provisions of the bill that had passed the Senate the year before. The executive branch had in the meantime drafted its own bill, which it considered to be more carefully thought through and worded. Senator Wagner and his advisers, however, decided to follow the bill that the Senate had already approved. Perhaps the most noteworthy changes made by Mr. Wagner's bill were that the authorization for appropriations for grants was increased to $51 million for one year, and the borrowing authority proposed to be provided for the new U.S. Housing Authority was increased to $1 billion, to become available over a 4-year period. (The $51 million appropriation was the first year's increment of the $326 million proposed in the 1936 bill as introduced. The same

[52] Ibid., p. 328.
[53] S. Rept. 2160, 74th Congress, 2nd Session.
[54] Ibid., p. 2.
[55] Ibid., p. 7.

[56] S. 4424 as reported 6-1-36, Calendar #2270, 74th Congress, 2nd Session, sec. 2(2).

figure was retained in the 1937 proposal, but subject to the limitation that contracts for annual contributions could not be entered into aggregating more than $10 million per year during any fiscal year, plus any leftover authorization from prior years.)

The bill retained the restriction adopted earlier by the Senate limiting eligibility for occupancy to families whose income did not exceed five times the rental of the quarters to be provided, but applied this test to "net income" (undefined), rather than to "aggregate income," and provided that the rental for this purpose should include the "value or cost" of utilities furnished such families.[57] Interestingly, this provision was moved from the subsection defining families of low income to that defining the term "low rent housing."

Another highly significant change concerned the character of the annual contribution itself.

The 1936 bill had provided with respect to the authority for grants that—"The Authority shall embody the provisions for such grant in a contract of grant guaranteeing such fixed and uniform annual contributions over such fixed period." The identical language was retained in section 9(b) of S. 1685. Immediately following this sentence, however, the 1937 bill introduced a quite new and, in the context, remarkable provision as follows:

> Such annual contributions as are contracted for shall be strictly limited to the amounts and period necessary, in the determination of the Authority, to assure the low rent character of the housing project involved: Provided . . . etc.

Here was, in the words of Gilbert and Sullivan, a most ingenious paradox. The first two sentences of the new section 9 declared unambiguously that grants to be made in the form of annual contributions were to be contracted for and made in "fixed and uniform" amounts, over a fixed period not exceeding 60 years. The third stated equally explicitly that the same annual contributions were to be neither fixed nor uniform (though the period of years remained "fixed"), but were to vary as necessary to limit them "strictly" to the amounts deemed necessary by the Authority to achieve the objective of low rent housing.

The new sentence quoted above survived the legislative process and remained in the law as finally enacted, although its manifest contradiction of the basic prescription concerning annual contributions was rendered slightly less conspicuous by moving it into a different paragraph.

It seems reasonable to suppose that in adding these words the sponsors of the 1937 bill had little if anything more in mind than offering some rhetorical assurance to doubtful Senators that Federal grants would not be frivolously or needlessly given out, but instead would be prudently applied to the achievement of low rents. Its ultimate effects, however, were far-reaching.

Clearly, the Authority could not make any such "determination" as was required of it without a periodic review of the facts and circumstances applicable to each project—nor, indeed, did it ever attempt to do so. Out of this innovation, therefore, arose a management relationship between the Authority and the local housing agencies far more continuing and intimate than had ever been visualized by the original proponents of public housing.

The language was the death knell of the concept of fixed and dependable annual payments which Miss Bauer and Dr. Wood (and others) had stressed so heavily as critical to the success of a system patterned on the British model. For the local housing agencies were put on notice from the beginning that prudence and efficiency in management would result, not in a somewhat more comfortable and stable financial position for the local agency, but in a reduction of the Federal subsidy. Thus too began the inevitable transformation of the annual contribution from simply a means of securing low rents for the families housed to a means of also securing low interest rates upon the borrowed capital with which the projects were developed; from a means of guaranteeing the ability of the local housing agencies to discharge their mission to a means of also guaranteeing the bondholders against any possibility of loss on their investments.

It is hardly an exaggeration, therefore, to find in this little noticed sentence, added to the 1936 bill in its 1937 form, the genesis of many of the financial perplexities in which the public housing program was to find itself many years later.

It would be unduly repetitious and burdensome to follow the 1937 hearings in detail. The main themes of support and opposition dominated the discussion, and indeed a great many of the witnesses were the same. In tracing the course of congressional consideration of the public housing bill, therefore, it will be profitable to turn attention to the actions of the congressional committees, and the consideration of the bill on the floor in the Senate and House.

[57] S. 1685, 75th Congress, 1st Session, sec. 2(1).

Senator Black (later Mr. Justice Black) reported the bill favorably, although with amendments, on July 23, 1937. It is evident from the first page of his report that 3 years of consideration had done little to focus attention upon housing as such. The committee's presentation of the bill for the consideration of the Senate began as follows:

> The main purposes of the bill are closely related to general objectives frequently expressed. There is wide recognition of the imperative necessity for meeting the unemployment problem on a long-range rather than a temporary basis; for guiding the Federal Government's assistance to business, labor, and the general public along lines dictated by permanent rather than emergency objectives; for measuring each dollar of public moneys spent in terms of its ultimate accomplishments rather than its immediate ameliorative effects; and for withdrawing public assistance as private capacity mounts, thus creating a balance wheel to stabilize the industrial activity of the Nation.[58]

The report did make some slight effort to characterize the bill as a major housing program. Describing the proposal as "long-range and carefully planned," the committee said:

> At a cost much cheaper than the terrible social and business toll of unhealthful housing—in terms of disease, crime, and maladjustment—it will provide better living quarters for millions who now dwell in dismal and insanitary surroundings.[59]

Even the authors of the report can hardly have intended this assertion as more than harmless hyperbole, however, in the light of the committee's own estimate that its bill would finance the provision of about 175,000 units of low rent housing (see page 10 of the same report).

A more accurate, or at least realistic, reflection of the committee's assessment of its initiative probably is to be found in the report's discussion under the heading "Economic Objectives of the Bill," where we read:

> The first objective of the bill is to provide opportunities for reemployment in a preeminently useful type of enterprise . . . .
>
> The committee is aware that the very modest public assistance provided by the bill, if taken alone, would neither make a real dent upon slum conditions nor stimulate general construction . . . .
>
> . . . [but] with the Government supplying the necessary spark, [it] will tend to ignite the building industry generally, will remove one of the most serious forces now operating against complete economic recovery, and will introduced into that economic recovery a truly stabilizing influence.[60]

Before turning to the Senate's reception of the bill on the floor, it may be useful to take brief note of the changes that the committee itself had made in the new version introduced by Senator Wagner.

The committee's amendment was a clean bill in the nature of a substitute, but this appears to have been essentially a parliamentary convenience, because the changes made were not so extensive that they could not have been handled by reporting the bill with amendments.

Many of the changes were administrative in nature, or technical, or merely clarifying. (For example, the proposed three-member board of directors for the Authority was replaced by a five-member board, one of whom would have a higher salary and the title of Administrator, etc.) The committee did make some effort to reconcile the hopeless conflict in the provisions of the bill requiring that annual contributions be simultaneously "fixed and uniform" and variable, by inserting some general standards for regulations that the Authority might issue governing maximum contributions, and by providing that the contract respecting a particular project should be reviewed, and if necessary modified, after 20 years, and at the close of each 10-year period thereafter. How all this might be reconciled with a 60-year contract for fixed and uniform contributions, the committee did not say.

The bill as reported also dropped the term "grants" for the standard form of financial assistance to be provided, and included separate treatment of annual contributions and of initial capital grants as an "alternative." These were limited to not more than 25 percent of the development or acquisition cost of a project. (Later discussion on the floor made it clear that neither the proponents nor the opponents took this provision very seriously. A few pointed to the obstacle presented by the high initial cost, but more doubted that any local community would opt for a 25 percent grant when it could obtain a much larger grant by going the annual contribution route.)

More significant, as a measure of the delicate balance of support and skepticism that the bill enjoyed, were the changes made in its financial provisions. Thus:

- The authority-proposed $10 million per year in annual contributions contracts executed was reduced to $5 million in the first year and $7.5 million in subsequent years.
- The $1 billion proposed borrowing authority for USHA was reduced to $700 million.
- The $51 million authority for appropriations contained in the bill as introduced was reduced to $26 million.

[58] S. Rept. 933, 75th Congress, 1st Session, p. 1.
[59] Ibid., p. 1.
[60] Ibid., pp. 3–6.

One other oddity is perhaps worth noting. In extolling the merits of the annual contributions technique, the report said:

> This system . . . has many merits. It provides a constant check against extravagance and waste in the operation of projects. It enables the Government to stop its contribution at any time if the full benefit does not accrue to those who need very low rentals or if people with higher incomes are allowed to come into the projects. It is the only method which measures the aid given directly against the rentals charged, which assures rent reductions for every penny given, and which really reaches the underprivileged poor.[61]

One must suppose that some critical printing deadline or similar circumstance accounts for the fact that a paragraph, not only so internally inconsistent but so flatly in conflict with provisions of the bill itself remained in the final document.

Consistent with the general ambiguity of purposes to which the committee saw itself responding, the title of the bill was amended to add "eradication of slums" to the already formidable list of its stated objectives.

It would be incomplete to leave the subject of the committee's actions on the bill committed to it without calling attention to at least one action that the committee did not take. This has to do with the formulation of the considerations of public policy upon which the Congress would be invited to ground its action.

It must be remembered that this was the third version of a major bill which the Senate Committee had considered in as many years, and that it was acting amidst a general expectation that the bill would be enacted in some form in that 1st session of the 75th Congress. The various public housing bills had been urged upon the committee by many different interests and upon many different grounds. At least some of the major witnesses supporting these bills were deeply concerned about housing policy as such.

If, in fact, the committee had by then reached the conclusion that it was contrary to the public policy for a large proportion of the American people to be very badly housed, and that the solution of this problem was beyond either the means of its victims or the resources of private enterprise, it might clearly have invoked the powers of government to attack that problem as such, and might have proposed to base such a policy on the acknowledged need, and on its own merits.

Such a statement might have been formulated in many different ways, but it would have been unmistakably a statement of housing policy. Whatever its language, it would have declared it to be inappropriate for a large part of the citizenry of the United States to be living in degrading and uncivilized circumstances beyond their power to remedy, and that, accordingly, as a matter of public policy the Government had determined to correct these conditions with all deliberate speed and by all appropriate means.

The committee, however, did nothing of the sort. Although it gave verbal recognition to the facts, its statement of "Findings and Policy" consisted in the main of a detailed rationale for raising the question at all. The "acute shortage of decent, safe, and sanitary dwellings within the financial reach of families of low income" was not found to be a public evil in and of itself, but instead was declared to be:

> Inimical to the general welfare of the Nation by:
>
> (a) encouraging the spread of disease and lowering the level of health, morale, and vitality of large portions of the American people;
>
> (b) increasing the hazards of fire, accidents, and natural calamities;
>
> (c) subjecting the moral standards of the young to bad influences;
>
> (d) impairing industrial and agricultural productive efficiency;
>
> (e) increasing the violation of the criminal laws of the United States and of the several States;
>
> (f) lowering the standards of living of large portions of the American people;
>
> (g) necessitating a vast and extraordinary expenditure of public funds, Federal, State, and local, for crime prevention, punishment and correction, fire protection, public-health service, and relief.[62]

As if uncertain whether this catalogue of evils was sufficiently imposing, the bill went on to say that failure to remedy the acute dwelling shortage ". . . has also produced stagnation of business activity in the construction, durable goods, and allied industries, thus impeding business activity throughout the Nation and resulting in widespread, prolonged and recurring unemployment with its injurious effects upon the general welfare of the Nation."

It is beside the point, of course, to acknowledge that the ills recited in the bill were quite real, and that each of them arguably was related to and perhaps in some measure resulted from the housing conditions of families of low or moderate income. The significance of the statement lies not in what it attempted to say, but in what it did not attempt to say: Namely, that widespread bad housing is a bad thing in and of

[61] Ibid., p. 11.

[62] S. 1685 as reported, Calendar #960, 75th Congress, 1st Session.

itself, and that if the people—individually or through their private institutions—cannot correct the conditions, the Government has a clear and natural duty to exercise its best efforts to do so. It seems inconceivable that, if this had been what the authors intended to say, they could have missed the mark so widely.

The language of "Findings and Policy" is quoted from S. 1685 as introduced by Senator Wagner. In reporting the bill, the Senate Committee on Education and Labor changed not so much as a comma.

The foregoing discussion, of course, is addressed to the legislative history and outcome of the 1937 act. It is emphatically not intended to suggest that individual members of the committee or the staff—and certainly not all of them—were indifferent to housing policy or unaware of the importance of housing as a problem in its own right.

Many motivations must have influenced the formulation of the language of the draft. Without doubt, the supporters of the bill were trying hard to endow it with attributes that other Senators would find appealing, or to which they could point to justify a favorable vote.

Similarly, these events occurred at a time when many New Deal measures had suffered severely at the hands of the courts. Clearly, therefore, the sponsors were also trying to build into the statutory language as many grounds as possible on which the Supreme Court could later base a favorable ruling under such provisions of the Constitution as the general welfare and commerce clauses.

When all this is said, however, it does not basically change the fact that the bill as presented to the Senate did not purport to rest upon or to set a national housing policy—and indeed housing as such was made almost to disappear among its manifold stated purposes.

Consideration on the Senate Floor

Although he was not a member of the committee that had reported the bill, Senator Wagner was its floor manager, in recognition of his standing as the senior sponsor and probably the best informed individual Senator as to the need for and the specific contents of the legislation, as well as concerning some of its more technical provisions.

Senator Wagner elected not to make an opening statement presenting the bill, with an outline of its philosophy, purposes, and program content; rather, after the briefest opening remarks he threw himself open to questions. Presumably Mr. Wagner had his own reasons for deciding on this approach, but our understanding of the thinking behind the 1937 act is the poorer for it. The debate that followed was general in the most literal sense. It leaped with little continuity from one question to the next, not on the basis of a sequential consideration or related problems, but in response to the particular interests of individual Senators as they took the floor. Some of it was repetitious, as questions were raised that had already been discussed at length while the questioner was absent from the chamber. Although some issues were national in scope, others dealt with State or local interests. (Senator McKellar of Tennessee, for example, insisted over protest on introducing an amendment that he admitted had nothing whatever to do with the subject matter of the bill, but that he hoped might solve a problem in connection with a small park in Knoxville.)

It may be best, therefore, to try to identify a limited number of significant themes which arose in the course of this rambling discussion, and to briefly characterize the reactions or policy declarations that they gave rise to.

The Question of Slum Clearance: The tenor of the debate makes it clear that a major issue in the minds of the Senators considering the bill was still—even after three years of discussion—whether they were being invited to pass a housing bill, or a slum clearance bill, or perhaps an amalgam of the two.

The ambivalence among the bill's supporters as to the purpose of the legislation they were supporting was not limited to the Senators, as has been noted in connection with testimony at the earlier hearings. The bill's managers were well aware of the fact. Thus at one point Mr. Walsh observed:

> . . . I think the junior Senator from New York will agree with me that there are two groups . . . of well intentioned, public-spirited, patriotic, deeply interested groups in this problem, who have two distinct points of view. One emphasized the point of view of building houses for people of low incomes. That group thinks in terms of building houses. That is commendable.
>
> The other group, unfortunately small in number and not so vocal, say, "Slum clearance! Slum clearance! Slum clearance!" That is what they want. They say the primary object of any movement of this kind is slum clearance, and in conjunction with this should be houses for rehousing those dehoused. I am in particular sympathy with the objectives of that group.[63]

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[63] 1937 *Congressional Record*, p. 10459.

The issue was not lightly taken. Senator Ellender, for instance, in pressing for more definitive requirements for the clearance of slums, told the Senate:

> The point I desire to emphasize is that the bill does not provide for mandatory slum clearance, when, as a matter of fact, the presence of slums is given as the main reason for this legislation.[64]

As a matter of fact, the bill before the Senate contained two relevant provisions under a general heading of "Standards" (S. 1685, section 15, previously cited). These were:

First, for projects involving new construction there would be arrangements for the elimination ". . . by demolition, condemnation, effective closing, reconstruction, remodeling, or repair . . ." of unsafe or insanitary dwelling units ". . . substantially equal in number . . ." to the new units to be constructed—subject, however, to a proviso noted below.

Second, for "slum clearance" projects, ". . . substantially all . . ." of the dispossessed inhabitants should be provided for by the development of sufficient low rent housing, either upon the site to be cleared, or ". . . in some other suitable locality." This requirement, too, had an escape clause.

These provisions failed to satisfy Senators who were primarily concerned with slum clearance on two grounds: First, that section 15 merely provided that in the making of loans, grants, or annual contributions the Authority should be "guided" by the considerations enumerated; and, second, that each of the cited requirements, if indeed they were requirements, left an ill-defined out for the Authority in any case where compliance might be awkward.

Thus, in the case of new construction, the elimination of a "substantially equal" number of units was permitted to be "deferred" in case of a ". . . shortage of housing of a low-rent character." Correspondingly, the duty to provide replacement housing applied ". . . unless the Authority shall be satisfied that proper provisions will be made for otherwise rehousing . . ." the inhabitants affected.

In vain, Senator Wagner sought to assure the Senate that the provisions were adequate and, in effect, mandatory. His critics were not reassured, insisting that the so-called standards merely provided "guidance," which the Authority might ignore, and that the requirements had ill-defined exception clauses under which they could be disregarded by the Authority as it might see fit.

[64] Ibid., p. 10359.

Seeking to convince Senator Ellender that the bill already dealt sufficiently with the problem to which he was addressing himself, Mr. Wagner told him:

> All that this provision means is that where there is a shortage of that kind, the old dwellings shall not simply be torn down and the people thrown out upon the street. We say simply defer that tearing down until we are able to build another unit, and provide for the slum dwellers still remaining there.

Mr. Ellender was not convinced:

> Mr. ELLENDER. So the Senator interprets the language of this particular section in that way, does he?
>
> Mr. WAGNER. Absolutely. That is all that it means, because we use the word "deferred," not "indefinitely postponed.
>
> Mr. ELLENDER. That is not my interpretation of the language referred to. It could, and would, in all probability, be interpreted to mean that so long as there is a shortage of housing, the present dwellings, the present slums, will remain. Suppose the funds run out, and there is still a shortage of housing. Does the Senator believe the slums will be cleared? How could the slums be cleared? [65]

Perhaps the strongest position on this point was taken by Mr. Walsh of Massachusetts—the former chairman of the Committee on Education and Labor—who had conducted the hearings in 1935 and 1936 (and, indeed, in 1937, due to the illness of the new chairman, Mr. Black). He began with a puzzling remark, especially in view of his purpose:

> Mr. President, first and foremost I wish to impress upon the Senate the fact that there is no need whatever of Federal legislation in order to abolish any slums or slum dwellings.[66]

Senator Walsh's further remarks make it clear that he was referring to the existence of power under State laws to condemn and demolish properties that were a menace to public health and safety.

Exactly why the Senator was anxious to impress this point on the record and the minds of his listeners he never said, for he went on to argue forcefully that slum clearance was, or should be, the principal if not the sole object and justification of the legislation. That part of his presentation ended thus:

> Mr. WALSH. . . . What can be done to make this bill be what the Senator from New York and I want it to be, a slum clearance bill, rather than a housing bill?
>
> Mr. WAGNER. I think that before we are through we will have such a bill.
>
> Mr. WALSH. I am sure we will.[67]

[65] Ibid., p. 10359.
[66] Ibid., p. 10457.
[67] Ibid., p. 10461.

How strongly Mr. Walsh felt on this matter —and, indeed, how deeply it conditioned his very support of the bill itself—may be judged by his emphatic statement to the Senate:

> I take the position that the Federal Government has no authority whatever to take 200 families in any community, unless they come from the slums and have the lowest incomes in the city, and put them in Government-erected homes for 50 percent of the normal rent a private enterprise or private owner would have to charge. If we are going into that business, I want all families to have that advantage and that subsidy; and that would mean, if I understand anything, that we should be right on the road to socialism and ultimately have complete Government ownership of all private dwelling property.[68]

In due course, Mr. Walsh made his point in the form of an amendment, which removed the subject from the heading of "Standards" and attached it directly to the authority to make annual contributions. It read thus:

> *Provided,* That no annual contributions shall be made, and the Authority shall enter into no contract guaranteeing any annual contribution in connection with the development of any low-rent housing project involving the construction of new dwellings, unless the project includes the elimination by demolition, condemnation, and effective closing, or the compulsory repair or improvement of unsafe and insanitary dwellings situated in the locality or metropolitan area, substantially equal in number to the number of newly constructed dwellings provided by the project.[69]

The amendment was agreed to.

The Question of Income Levels: Few questions were discussed at greater length—or more inconclusively—than that of the income levels to be served by the new public housing program.

Senator Wagner, in his whole discussion of the proposal, treated it as a measure directed toward the assistance primarily, if not solely, of families of extremely low income. Thus, when Mr. King of Utah inquired whether there was a provision to permit the low income tenants later to acquire title, should they find themselves in a position to do so, Mr. Wagner explained that there was not:

> The occupants of the houses are of the very low-income group. They cannot even afford to pay more than $2 or $3 or $4 or $5 per room. The moment they become affluent enough to afford to pay more than is provided for the low-income group, they cannot remain occupants of the houses. The authority would say, "You go. You are earning more money than are those in the low-income group, and you can no longer occupy these dwellings." So that there would never come a time when they would be in a position to acquire title.

The Senator from Utah was distressed by this reply, because of what he correctly perceived to be its long range policy implications. He inquired further:

> Mr. KING. Under that theory are we not discouraging home ownership, and making this one-third of the public to whom the Senator refers psychologically and otherwise of the opinion that they never can be home owners, that they are to be renters as long as they live?
>
> Mr. WAGNER. Just as soon as they earn enough, they can become home owners. . . .[70]

But they could not, it was clear, become owners of the units proposed to be constructed with assistance under the pending bill. To achieve the transition to homeownership, they would first have to move out.

Once again, perhaps the sternest view of the matter was taken by the formidable Mr. Walsh of Massachusetts. Explaining that he distrusted the discretion in tenant selection that was being left to the new local authorities, he said that he wanted ". . . the people who get this subsidy to be not the low income group but the lowest of the low income group . . . ," and he confronted the beleaguered Senator from New York with a blunt threat:

> Mr. WALSH. I shall not vote for the bill unless it is clear and unmistakable that the subsidy will be removed from any possibility of favoritism in its granting of subsidies. I insist its benefits reach the lowest-income group and that those of the lowest income get the tenements provided for in this measure.

Faced with this uncompromising stand on the part of the former chairman, Mr. Wagner conceded that an amendment might be arranged, though he did not concede that one was necessary, and the following interesting exchange took place:

> Mr. WALSH. I hope the Senator will keep in mind that our colloquy is not merely for the purpose of informing ourselves as to the views of each other, but to place in the RECORD our opinions in order that the RECORD will reveal that he and I again and again on the floor of the Senate pleaded that the poorest and lowliest people in the country should get the subsidies carried by the bill. It is not so much that the Senator differs with me or that I differ with him, but that we want the RECORD to show that it is the purpose and the intent of the Congress of the United States that the subsidies shall go to the most needy of our poor families.
>
> Mr. WAGNER. I am willing to have a mandatory provision that it shall be the duty of the board, in each case where a loan is made, that as a condition precedent to the making of the loan the lowest income group among the slum dwellers shall be first served before any other group. I think the objective is clearly stated, but we can make it clearer if that is desired.[71]

[68] Ibid., p. 10460.
[69] Ibid., p. 10478.
[70] Ibid., p. 10367.
[71] Ibid., p. 10377.

And a few minutes later:

> I do not want to interrupt the Senator in his presentation. As has been so often stated, he and I are together in this proposition; but to insure absolutely that none but the lowest-income group will secure occupancy of these homes I may say to the Senator that I am going to offer another amendment in which I shall provide that occupancy shall be confined to those who are in the lowest-income group. In other words, each area will be limited to the lowest-income group. We cannot very well go below that. I mean, that is absolute assurance.[72]
>
> Mr. WALSH. That will help.

And indeed, the next day Mr. Wagner proposed an amendment to the bill's definition of the term "families of low income," to specify that these words should mean families "who are in the lowest income group," in addition to the existing test. So that the definition read, "The term 'families of low income' means families who are in the lowest income group and who cannot afford to pay enough to cause private enterprise in their locality or metropolitan area to build an adequate supply of decent, safe, and sanitary dwellings for their use."

The question of the income levels to be served was also discussed at length in connection with another provision of the bill that attempted to get at the same problem by limiting the availability of the assisted housing to families whose "net income" at admission did not exceed 5 times the rental of the quarters to be furnished (or in the case of large families—3 or more minor dependents—6 times the rent).

Curiously, this provision was included in the proposed statutory definition of "low rent housing," rather than that of "families of low income," although clearly its purpose was to define such families, if only by indirection. Plainly the Senate understood that to be the case, and there was extended discussion as to whether a 5-times-the-rent rule would admit tenants whose incomes were too high to make them deserving of subsidy, at least by comparison with other possible applicants of lower income.

At one point, Mr. Walsh declared his intention to press for an amendment that would reduce the eligibility limit to 4 or even 3 times the rent, to guard against that possibility. Either he thought better of this idea or was dissuaded; the amendment was never introduced, and the provision remained unchanged in the bill as passed by the Senate.

There was a degree of uncertainty all along as to the effect of this amendment. Thus, when Senator Adams pointed out that one family might have no children and another many, or that a family of lower income than another might also consist of dissolute and disreputable people, Mr. Wagner replied:

> Of course, people of ill-repute will not be permitted to occupy the premises. . . .
>
> The amendment speaks for itself. . . . Questions of character, of course, will always have consideration.[73]

There was no evident foundation for this interpretation either in the language of the amendment or in its author's explanation of its effects. When Mr. Adams attempted to pursue the point, however, Senator Wagner cut him off with the rather curt observation, "I think the Senator raises a very insignificant consideration."

Curiously enough, no one brought into focus the question whether this requirement—if it meant anything like it appeared to mean, or was said to mean—could possibly work, given the financial structure and subsidy formula provided in the bill. This is the more surprising since it would seem obvious that those who constitute the "lowest of the low income group," in Mr. Walsh's phrase, are the families with no income at all, or virtually none. If occupancy of public housing were indeed to be restricted to them, it would follow a fortiori that the projects would have virtually no rental income—a result hopelessly out of kilter with the plan of the bill.

Senator Pepper of Florida came closest to the point, without quite making it. He pointed out that the amount of the subsidy in effect fixed the rent, and some low income families might not be able to pay the necessary amount. But in effect he turned the point around by saying such families would be excluded by the language of the bill. He suggested substituting "lower income" for "lowest." (A change which, of course, would not have solved the difficulty he had just identified.) Mr. Wagner resolved the problem by interpreting it out of existence, thus:

> Mr. WAGNER. There are some people whom we cannot possibly reach; I mean those who have no means to pay the rent minus the subsidy. This, after all, is a renting proposition.
>
> Mr. PEPPER. If that is what the Senator means, that is not what this paragraph will say.
>
> Mr. WAGNER. I am sure it will be so interpreted, because obviously this bill cannot provide housing for those who cannot pay the rent minus the subsidy allowed.
>
> Mr. PEPPER. Yes; and yet the language, if this amendment is adopted, will limit the availability of those quarters just to those people. That is not what the Senator had in mind.
>
> Mr. WAGNER. I doubt whether it would be so interpreted. I think it would be interpreted to mean the lowest income group that the bill can reach.

[72] Ibid., p. 10460.

[73] Ibid., p. 10479.

Mr. PEPPER. The Senator means then, if I may inquire further, the lowest income group which is able to pay the rentals which will be required by the authorities who administer this act?

Mr. WAGNER. Yes.[74]

It is difficult, to put it mildly, to reconcile this interpretation with Mr. Wagner's explanation of his own amendment when he was seeking to mollify a persistent Mr. Walsh:

Mr. WALSH. Mr. President, I understand that the Senator from New York is of the opinion that the adoption of the amendment will strengthen the bill and accomplish the purpose we have in mind, namely, that preference in the granting of the subsidies provided for and in the occupation of the tenements erected by the local housing authorities shall go to those families of the very lowest income groups.

Mr. WAGNER. That is exactly what the amendment provides.

Mr. WALSH. There is no longer any question as to the local authority having discretionary power to choose between a large number of persons of low income, but they must choose those with the lowest incomes.

Mr. WAGNER. Those with the lowest incomes.[75]

In fairness, Mr. Wagner was addressing himself in these exchanges to specific questions or criticisms. Yet it should be noted that despite the language of the definition proposed for low income families—the test of income was not in fact by any means all that he had in mind. Thus, his exchange at another point with the Senator from Idaho:

Mr. POPE. There is one place in my own town which is called a cardboard town. The small buildings are constructed out of cardboard, tin cans, or slabs which may be picked up, or anything else which will make some sort of habitation, and yet they are not really unsanitary. They are not dangerous to health and safety, but they are simply poor dwellings where people live.

Mr. WAGNER. This bill would not apply there, Mr. President, because we are not rehousing everybody who has a low income, but only persons of low income who live in unsanitary and unsafe and unhealthful conditions which are detrimental to morals, to health, and also to safety.

Mr. POPE. Then, in the Senator's judgment, the emphasis should be placed on safety, health, and morals in any situation?

Mr. WAGNER. Oh, absolutely! [76]

In any event, his amendment was agreed to, though the record makes it evident that the Senate was less than clear as to exactly what it was that it agreed to. And thereby an important, perhaps even a crucial, opportunity was passed up to launch the public housing program on a foundation of clear decisions and solid policy, rather than the ambiguities in which praiseworthy purposes are inclined to be wrapped.

The Question of What, Exactly, Would Be Accomplished: The record shows that the Senate felt uneasy, to say the least, about exactly what they were getting themselves and the country into, but that neither the advocates of the bill nor its opponents could figure how exactly to come to grips with the question.

It is obvious that Senator Wagner wanted a bill, and that to get one he was prepared if necessary to make concessions, as he repeatedly did. He consistently presented the proposal as one of great importance and urgency, yet he was anxious to avoid frightening the undecided or arming the opponents by stressing unduly the magnitude of the task or of the effort required to cope with it. Thus, when he was obliquely complimented by Senator Vandenberg for starting "conservatively," he replied, one may think, a bit grimly,

The Senator need not tell me that I am starting very conservatively, I know it. I am just touching the situation, and even that has been difficult. This is the third year of the attempt to secure legislation of this kind.[77]

Some insight into what Mr. Wagner might have liked to propose, had he thought it feasible or acceptable at the time, may be gained from his answer to Senator Borah:

Mr. BORAH. Is the Senator going to discuss the question of causes of slums? Why do we have these awful degraded conditions?

Mr. WAGNER. I think that is a very simple matter. It is because of the low incomes received by the individuals who live in the slums. That is the fundamental difficulty. If overnight we could increase their incomes by a more fair distribution of wealth of the country, we would not have any slums.[78] [A concept supported by many people today, and referred to variously as an incomes policy or income transfer approach.]

Mr. Tydings of Maryland was troubled conceptually by the idea of Government undertaking to pay part of the rent for the tenants of these projects over a long period of years. He told Senator Wagner:

Mr. TYDINGS. I want to say to the Senator from New York that so far as I am concerned my reluctance to support the measure, if such there is, comes from the proposal for subsidies on rents, rather than because of any other feature of the bill.

With a more valid claim to prescience than he made for himself at the time, he continued:

[74] Ibid., p. 10480.
[75] Ibid., p. 10479.
[76] Ibid., p. 10379.

[77] Ibid., p. 10366.
[78] Ibid., p. 10358.

I do not know how long it will be, if the measure's incorporated into law, and I do not want to invade the realms of prophecy, but I predict if it remains in the law and is employed, it will be the entering wedge to subsidies to a tremendous number of people who will not even live in slum-clearance projects, because once the principle has been adopted in national law it will be carried to the extreme limit.[79]

Conceding that something ought to be done about the slums, he said that he would prefer to ". . . vote for a grant and call it a day . . ." than to involve the Government in a commitment over 60 years. Finally he put the question bluntly, and received an unequivocal reply:

Mr. TYDINGS. Would the Senator consider it fatal to the bill if the provisions for rent subsidies should be stricken out and the ones relating to capital grants of assistance retained?

Mr. WALSH. Yes. I think the President would veto the bill and would reject it. Perhaps I should not say the President, but I think the administration would reject the bill and I think the Senator from New York would ask to have the bill defeated. Am I correct, may I ask the Senator from New York?

Mr. WAGNER. Yes.

The Senator from Maryland also pressed for some dimension as to the hoped for accomplishments of the program under the pending bill. He asked its manager:

Mr. TYDINGS. When the entire sum shall have been loaned, to what extent will that have solved the problem?

Mr. WAGNER. We would still have a great deal to do.

Mr. TYDINGS. Does the Senator think we would have solved one-fourth of it?

Mr. WAGNER. I doubt it.[80]

Mr. Wagner could have afforded to respond more definitely to the second question. He had himself estimated that there were at that time some 9 million families who were badly housed, and that the financial assistance provided in the bill might produce at most some 175,000 units, which he equated to adequate shelter for about 850,000 "persons." Since the low income population can be expected to grow at a rate at least as fast as that of the population in general, it would have been reasonable to ask whether, in fact, a program of the magnitude proposed would have any effect on the problem at all. No one asked that question directly, however.

The Senator from New York did not disguise the fact that his hopes for long term results rested not so much on what the bill would authorize, as on what it might trigger in the future. He told the Senate:

Mr. WAGNER. I am glad these questions are being asked because it shows what a modest beginning we are making in the venture. I want to have the opponents of the bill understand that the problem is much more tremendous than we are undertaking to take care of in the bill now under consideration. I know that in other countries public opinion has compelled the doing of more than this.[81]

A bit later, when Senator Pepper was emphasizing both the magnitude of the problem and his own support for the bill, he said:

Mr. WAGNER. I know the Senator's sympathy; but it also shows the insignificance of this proposed legislation. It is merely a start; but I hope public opinion will so approve it, if Congress sees fit to enact it into law, that we shall soon speed on to help the others.[82]

Those who opposed the legislation in principle were not, of course, too much troubled by problems with orders of magnitude. Mr. George of Georgia, for example, complained that the bill was ". . . founded upon the philosophy that there is in this country a group of low-income producers who cannot live in sanitary and reasonably comfortable houses unless the Government subsidizes them"[83]—a proposition that he obviously found implausible and unacceptable. He offered an amendment providing for the automatic expiration of the act at the end of three years in order to ". . . give the act full opportunity to demonstrate whether or not the philosophy is sound, and . . . the Government ought to commit itself to that doctrine." He urged the adoption of the amendment on the ground that:

If it is not adopted there will not hereafter go into housing any private capital. It will be the end of a private program for building houses in America. Private capital will withdraw from the field. The bill will end it, and we shall have state socialism now and forever if we do not limit the operations of this measure.

. . . Are we in any position to say or to know that this program is not experimental, and can we close our eyes to the obvious fact that, entering the field, we must occupy the whole of it, so far as the low-income producers are concerned, in every section of the country?

Mr. George's amendment was, in fact, very nearly nugatory because the bill provided for only three years of authority that when exhausted would automatically terminate the program as to new undertakings unless Congress should act further. The only practical effect of the amendment would have been that the new Authority would have ceased to exist after three years, requiring the Congress to designate some existing agency to carry to completion the contracts then in force. The amendment was re-

[79] Ibid., p. 10464.
[80] Ibid., p. 10371.

[81] Ibid., p. 10372.
[82] Ibid., p. 10378.
[83] Ibid., p. 10558.

jected largely on this ground, though it generated enough support to require a roll-call vote (33-47).[84]

The basic question of what the bill was all about—what policy it expressed and to what long range objectives it was addressed—was repeatedly raised and as often dropped after inconclusive discussion. Senator Wagner rested his hopes for more significant progress at some time in the future on the anticipated force of public opinion. The mood of much of the rest of the Senate was reflected in two general observations—one by an opponent of the bill, one a supporter.

Senator Byrd of Virginia, who had achieved some measure of fame through his relentless efforts at curtailment of virtually all kinds of Federal expenditure, opposed the bill and voted against it. He summarized his views thus:

> Mr. President, I think the Senate should understand that we are embarking on one of the most costly ventures ever undertaken in the history of our country. We are doing it with little consideration. I venture the assertion that aside from the Senator from New York [Mr. Wagner] and the Senator from Massachusetts [Mr. Walsh], no two other Members of this body understand the complicated provisions of the bill. I dislike to make that assertion, but I have sat here and attempted to understand it myself.[85]

Senator Borah, who was sympathetic toward the purposes of the bill and who in the end voted for it, permitted himself this uncomfortable assessment of its probable effects in an exchange with Mr. Tydings:

> Mr. TYDINGS. If the Senator will yield . . . the Senator knows that if we spend every single, solitary dollar of this money in New York, it would only provide for 175,000 families.
>
> Mr. BORAH. Exactly. I listened to that presentation very attentively because that, it seems to me, is the most powerful argument made against the measure. After we have done what we are proposing to do we have really gotten nowhere.[86]

The Matter of Cost Limitations: Another matter which greatly troubled the Senate was the question of how much public housing units which were to be subsidized in the manner proposed should be permitted to cost.

One important aspect of this problem related to the difficulty pointed out by a private real estate broker (See quotation from the testimony of Mr. Grimm, page XX.) much earlier, in his testimony before the Committee on Education and Labor, when he pointed out that it would not sit well with the taxpayer to find that ". . . the fruits of one's labor can purchase less desirable homes than are provided for those who cannot or will not earn or save as much."

Mr. Walsh put it this way, and even Mr. Wagner agreed without elaboration, that it was an issue of importance:

> . . . we have made some mistakes in Federal housing which we must avoid in this bill. We are providing for and giving subsidies to people who have gone into better houses built by the Federal Government than the average workingman enjoys. There is no question about that. We must avoid this in the future.
>
> Mr. WAGNER. Of course, that is so.[87]

This aspect of the matter may be viewed as essentially social and psychological, and in the broad sense political. However, the question of costs raised highly practical questions as well: Because costs would ultimately control rent levels, they would (under the five or six times rule) likewise indirectly control the income limits governing eligibility for admission; similarly, because the maximum amount to be contracted for was fixed, and because the subsidy was directly related to development costs, the allowable costs would not so indirectly control the number of units which could be provided at any given level of aggregate subsidy.

The debate, however, did not turn directly around these matters. Instead, the issue was joined by the Senate's most indefatigable advocate of governmental frugality, Mr. Byrd of Virginia, who introduced an amendment to insert the following provision:

> (6) No contract for loans, annual contributions, capital grants, sale, lease, mortgage, or any other agreement or instrument made pursuant to this act shall be entered into by the Authority with respect to any project costing more than $4,000 per family unit or more than $1,000 per room.[88]

The purpose of the amendment, he told the Senate, was ". . . to prevent the extravagance which has occurred in other homestead projects built throughout the country."

Mr. Wagner saw the effect of the amendment—and, although he did not quite say so in so many words, its intent—in quite different light. He told the Senate:

> Mr. WAGNER. Of course, those who are not in sympathy with our efforts to do something for the one-third of the people of the United States who are ill-housed, to give those unfortunate people who have not sufficient income to enable them to live in decent quarters a chance for life, will feel that the amendment of the Senator from Virginia ought to be adopted and the bill ought to be defeated. I

[84] Ibid., p. 10560.
[85] Ibid., p. 10551.
[86] Ibid., p. 10644.
[87] Ibid., p. 10376.
[88] Ibid., p. 10548.

say very candidly to the Senate that if the amendment of the Senator from Virginia is adopted it will kill the bill.[89]

Mr. LaFollette argued that if the Senate should adopt the Byrd amendment it would not only be treating the bill with hostility, but acting out of ignorance. He said:

. . . I contend that there are absolutely no data upon which the Senate can determine the cost per room or per family of the projects to be undertaken under the bill. If there are such data in existence, they have not been presented to the Senate. The statement of the author of the amendment was to the effect that he had taken the average of the figures given him in the debate a day or two ago by the Senator from New York. Of course, as everyone knows, the average represents a figure between the extremes, which may be as much as 50 percent above and 50 percent below the number fixed. Considering fluctuating building costs, for the Senate to write into a program which is to extend over a period of years a flat limitation of this character, in my opinion, would serve to frustrate and wholly defeat the objective which this bill has in mind. If that is what the Senate desires, I contend that it would be much better for a majority of the Senate to vote down the bill rather than to pass a measure which ostensibly is to inaugurate a long-range housing program, but which will contain in it a limitation that will prevent its achievement.[90]

The appearance that the Senate was about to come to grips with a basic issue proved illusory. There was more discussion about average costs versus ranges, and about the higher costs inevitably to be encountered in the larger cities, and similar matters. But eventually the debate turned into a confused and confusing argument over the question whether the $700 million authorized in loans to the local housing authorities was or was not secured, and would or would not be repaid. The sentiment of the Senate on the basic issues raised by the very concept of statutory cost limitations was never crystallized, except perhaps in the close vote by which the Byrd amendment was finally adopted—40–39, with 16 members not voting.

Others outside the Senate apparently shared the view that the true purpose of the Byrd amendment was to kill the program, if not the bill itself. A major lobbying effort to undo it was launched overnight, so conspicuously that a rather rancorous discussion broke out on the floor the next day, with members complaining that Senate pages were distributing the "propaganda" of a private organization to their desks. Senator Wagner attempted to assume responsibility for this as an effort on his own part to provide needed information on the issues, but the offended members were not appeased. Mr. McNary described the incident as ". . . the boldest attempt to influence legislation I have seen in 20 years in the Senate," and ". . . an insult to every member . . . ." He continued,

I absolve the Senator from New York, because he has not had many years of experience in this body, from causing the propaganda to be distributed. The trouble with the whole thing, however . . . is the audacity of this organization in attempting to influence legislation in this fashion.[91]

Strong language, for the Senate.

Whatever the proprieties of the matter, the effort stirred enough support that on the following day—two days after the original vote—the Senate took a fairly unusual step of entertaining a motion to reconsider the vote by which the Byrd amendment had been agreed to. Mr. Barkley notified the Senate that, if the amendment were to be reconsidered, it was his intention not to try to vote it down, but to offer a substitute which would have omitted any limitation on unit costs, and would have set a limit of $1,400 per room on development cost of assisted projects, excluding the cost of land and clearance. This was apparently the highest figure which the proponents of the program thought they could hope to get, and the lowest they thought would make the program workable in the larger cities. Mr. Barkley's substitute never reached a vote; the motion to reconsider was laid on the table by a margin of 44–39, with 12 not voting.[92]

Some Other Issues Briefly Noted: The matters discussed above were certainly the most significant policy questions to which the Senate addressed itself in the consideration of the bill, from the standpoint of national housing policy. There were, of course, a number of others, some of considerable importance. Of these, at least the following deserve brief mention:

Applicability in Rural Areas: The question was frequently raised whether the program authorized by the bill would extend to rural areas as well as to the cities, especially the larger cities. The Senate each time was assured that it would, though the discussion threw very little light on the circumstances in which the program might serve rural areas, and how it would actually operate in meeting rural needs. Mr. George of Georgia (who was opposed to the bill in any event) sought at one point to get some clarification on these questions:

Mr. GEORGE. I desire to ask the Senator from New York how this bill can be administered so far as rural homes are concerned?

[89] Ibid., p. 10552.
[90] Ibid., p. 10557.

[91] Ibid., p. 10635.
[92] Ibid., p. 10807.

Mr. WAGNER. In the same way that it is administered in the city slum areas.[93]

This response was not terribly illuminating, but it came about as close as anyone got to penetrating the problem of how, if at all, the proposed program would operate in areas which were actually rural—as distinguished from towns in which, even though small, areas had developed which would generally be agreed to be slums.

Financing: As noted above, there was a great deal of discussion of the financial structure of the program provided in the bill, much of it directed to the substantiality of the security provided for loans for the development of projects, and the probability that the Federal Government would actually recover these amounts. This aspect of the debate need not concern us further here, because as matters actually developed direct Federal loans were to play a progressively less and less significant role in program financing.

It is worth pausing to note, however, that even at this early date budget considerations were exercising an important influence on policy. It was mentioned earlier that the principal sponsors of the bill flatly refused to accept Mr. Tydings' proposal to eliminate the concept of annual contributions and proceed via one-time capital grants. In discussing this approach, the following significant exchange occurred:

Mr. WALSH. . . . it is important for the Senator to know that one of the reasons why there is a subsidy in the bill rather than an outright grant is because of a matter the Senator is very much interested in.

Mr. TYDINGS. I do not know what it is.

Mr. WALSH. Under the plan of the Senator we would have to appropriate annually large sums of money and we would put the Budget more out of balance. . . .

Mr. WALSH. I assume the financial provisions of the bill were deliberately and intentionally shaped and formulated so as to avoid immediate large appropriations from the Federal Treasury in the way of grants. Based upon the authorized appropriations for the first 3 years fixed in the bill, the outright grant from the Federal Treasury, which, of course, would have to be met at once, would have been $315,000,000. In view of the condition of the Budget the Senator can appreciate how reluctant the administration was to start it upon that basis.[94]

The whole history of the capital grant provisions suggests that they were left in the bill largely, if not entirely, as a gesture toward those who strongly favored this approach, both because of its simplicity and because it would minimize the necessity for continuing Federal supervision of the local housing agencies over a long period of time. It appears not to have been seriously thought that initial capital grants would actually be made in practice—as indeed they never were.

Administrative Matters: The Senate devoted a great deal of time to matters of organization and administration, which—important as they undoubtedly were—are tangential to this review. These included such matters as the most suitable number of members for the Board of Directors (reduced from five to three); the characterization of those types of appointment that would be, respectively, subject to the civil service laws or subject to confirmation by the Senate; and the appropriate scope of audit on the part of the Comptroller General. The latter point was especially controversial because the incumbent Comptroller General at that time was widely known for his exceedingly conservative views, and because he then had, as a matter of general practice, the power of prior- rather than post-review and approval of obligations and expenditures.

An amendment proposed by Mr. Barkley was adopted requiring the President's approval of proposed annual contributions contracts. Later, as the program grew and the President's workload became ever heavier, it became evident that this review step was more trouble than it was worth, and the function was delegated to the Housing Administrator (later, of course, the Secretary).[95]

State Limitations: Perhaps because of the uncertainty as to how—or even whether—the new program would operate in rural areas, there was considerable apprehension in the Senate lest all the aid provided go into a relatively few States with the largest cities and, hence, the largest needs. Mr. Tydings put it more bluntly than anyone else when he said:

I . . . predict that New York will receive practically all the money that this bill contains. [Laughter.] I make the prediction that with the bill in its present form, at least half of the money will find its way into New York City or the immediately surrounding area and that the municipality will not put up a red penny.[96]

This was a suggestion which Mr. Wagner rejected with some heat.

In lieu of a complex and elaborate State allocation system based on population, Mr. Tydings proposed a simple, or seemingly simple, provision declaring that not more than 10 percent of the funds provided in the bill could be spent within any one State.

[93] Ibid., p. 10362.
[94] Ibid., p. 10464.
[95] E.O. 11196, 2-2-65.
[96] 1937 *Congressional Record,* p. 10555.

The Senator from Maryland was clearly more interested in getting the principle of some sort of limitation into the law than in precisely what it provided. When it was pointed out to him that a 10 percent State limitation would go beyond protecting the States with lesser needs and would actually discriminate unjustifiably against New York, he first modified his amendment to increase the 10 percent limit to 15 percent, and later to raise that to 20 percent.

It must have been evident to all concerned that to have all the funds go—theoretically, at least—into five states was hardly a great improvement over having them go to two or three. Nevertheless, the supporters of the legislation gave up at that point, and the 20 percent limitation went into the bill—a decision they later had some cause to regret, since in conference the limit was reduced to the original figure of 10 percent.

Local Participation: As a final effort to tighten up what he regarded as the objectionably loose financial provisions of the bill, Mr. Tydings proposed an amendment which would have required that in connection with any project the State or some local political subdivision in which it was to be located must contribute or agree to contribute 5 percent of any loan, grant, or contribution made to the project. Mr. Wagner made no objection, and the amendment was agreed to.

With all these (and some other) matters disposed of one way or another, the Senate passed the bill and sent it to the House. Although the vote on final passage was 64–16, the tenor of the debate as a whole and the votes on the adoption and reconsideration of the Byrd amendment at least strongly suggest that sentiment in the Senate on the basic merits of the legislation was considerably more divided than its margin on this vote might seem to indicate.

Consideration in the House

The House Committee reported the bill with an amendment in the nature of a substitute which modified the Senate version in a number of particulars, some minor and some quite significant.[97] Probably the most important changes were the following:

1. Loans were limited to 85 percent of development or acquisition cost, and the authority for them reduced from $700 million to $500 million.

2. Total authority for annual contributions contracts was left at a final figure of $20 million per annum, but the rate of program growth was slowed by allowing only $5 million to become available in the first year, and $7.5 million in each of the two succeeding years (instead of $10 million in each of two years, as in the Senate version). Moreover, a requirement was added that each contract be reviewed for continued need at the end of 10 years, and each five year period thereafter.

3. The allowable ratio of tenants' income at admission to the rental was reduced from 5 times the rent (or 6 in the case of large families) to 4 and 5 respectively.

4. Annual contributions were required to be applied first ". . . toward any payment of interest or principal on any loan due to the Authority . . . ."

5. The Byrd amendment was modified by eliminating the ceiling on overall cost per unit, and raising the per room limitation from a maximum of $4,000 to a maximum average of $5,000. Additional language was added to the effect that such costs could not exceed those of units produced by private enterprise in the locality or metropolitan area, using similar building requirements and labor standards. Projects were also required to be not "of elaborate or expensive design and materials," and to promote economy both in construction and "administration."

6. The equivalent elimination requirement was modified to require that the arrangements for clearance of a substantially equal number of substandard dwellings in connection with any project involving new construction should be "satisfactory to the Authority." No provision was made for deferral of this requirement. The committee changed its view on this question, however, and during consideration on the floor a committee amendment was adopted that allowed deferral in the discretion of the Authority where it found the shortage of decent, safe, and sanitary housing for low income families to be such as to ". . . force dangerous overcrowding of such families."

The Senate bill with the committee's proposed substitute came to the floor after what dissatisfied members described as hasty and meager consideration.[98] Mr. Hancock of North Carolina who said that he had ". . . for several years ardently favored a genuine slum reclama-

[97] S. 1685 reported with amendment, Union Calendar #573; H. Rept. 1545, 75th Congress, 1st Session.

[98] 1937 *Congressional Record*, p. 11820.

tion and low-rent-housing program," recounted the lengthy consideration and study which the Committee had given the problems, and complained that:

> . . . suddenly last Friday afternoon, practically all of our work was set at naught by certain amendments proposed by the chairman at the request of the Housing Division of the Public Works Administration. The effect of these amendments could not be known until the bill was printed, for no member of the committee ever saw one of them, with the exception of the chairman, until the printed bills were available Monday morning of this week [After the bill had been reported].[99]

In language reminiscent of Senator Byrd, Mr. Hancock told the House:

> Even at this hour, I venture the assertion that there is not a member of the committee who would stand here in the well and tell you that he understood this bill in its present form.

The debate followed substantially similar lines to those of the Senate debate, reconsidering problems that had been extensively explored there as well as to some extent in hearings. Following the leadership of Chairman Steagall of the Committee, the House rejected by votes or on points of order a series of amendments, themselves mostly on familiar matters. (E.g., to restore Senate language authorizing certain nondwelling facilities in projects; to increase the income-rent eligibility ratio from 4 times rent to 5 times; to authorize 2 percent of available funds to be used for research and "experimental constructions"; to provide for preaudit by the General Accounting Office of transactions involving loans, grants, and annual contributions; to eliminate the President's prior approval of assistance to projects; to allow loans up to 100 percent of acquisition or development cost; to provide low interest rate loans for the construction of single family homes for owner occupancy; to set a 2-year limit on deferral of equivalent elimination; and to increase the State limitation from 10 percent to 15 percent.) A committee amendment authorizing deferral of equivalent elimination in circumstances which, in the determination of the Authority, might lead to "dangerous overcrowding" of low income families was agreed to. Significantly, unanimous consent was given to amend sections 10 and 11 of the bill (dealing, respectively, with annual contributions and capital grants) to insert the words "or slum clearance" in the phrase "low-cost housing project" wherever it appeared in those sections.[100]

[99] Ibid., p. 11831.
[100] Ibid., p. 11862.

One amendment which the House rejected at the instance of the committee is worthy of special note, since it reflects one of the few matters which engaged the serious (as distinguished from the formal) attention of the members while the bill was on the floor. It had to do, not with a question of housing policy or of slum clearance, but of the coverage of employees of the new Authority under the merit system, and the prerogatives of the Senate in the matter of approving certain classes of appointments.

The Senate bill had provided that the Authority might appoint employees, subject to the civil service laws and the Classification Act of 1923, as amended, except that without regard to those laws it could appoint and fix the compensation of attorneys, and—subject in this case to regulations to be issued by the Civil Service Commission—to appoint and fix the compensation of "officers and experts." All employees receiving compensation of $4,000 per annum or more were to be "subject to confirmation by the Senate." [101]

The House Committee rewrote this section to provide that the Authority, without regard to other laws on the subject, might appoint and fix the compensation of "officers, attorneys, experts, and employees." No provision for Senate confirmation was included.[102]

When this section was reached, a member of the minority (Mr. Wolcott of Michigan) offered an amendment to restore the Senate language. Chairman Steagall, explaining that the Committee's intent was to "expedite the organization" of the Authority, secured immediate approval of a motion closing debate on the section and all amendments to it. Thereupon, the House summarily rejected not only the Senate provision but a milder version offered by the Chairman of its Civil Service Committee, Mr. Ramspeck.[103] This abrupt and unusual rebuff to the Chairman of a major committee provoked Mrs. Rogers of Massachusetts into suggesting that the House should have some sort of memorial observance ". . . to pay tribute to the death of a great committee . . . the Committee on the Civil Service . . . . It has been choked to death."

Unlike the substantive amendments, which generated mainly familiar rhetoric on both sides, it is clear in the record that this matter involved strong feelings. Members in the minority—and, of course, Chairman Ramspeck—pleaded for fair

[101] S. 1685 reported with amendment, Union Calendar #573; H. Rept. 1545, 75th Congress, 1st Session, secs. 4(a) and (b).
[102] Ibid., Committee Amendment, sec. 4(a).
[103] 1937 *Congressional Record*, p. 11852.

treatment, and described the Committee's provision as a violation both of the Democratic platform and of the announced policy of President Roosevelt. Members of the majority, in at least as vehement terms, blamed their opposition for past and continuing political abuses. Mr. Fuller, speaking perhaps somewhat more bluntly than he might have but for the heat of the moment, told his colleagues on the other side of the aisle:

> Oh, you gentlemen over there on the Republican side make much ado about civil service. You want some more jobs. But let me tell you, you have all we are going to give you. We have made up our mind you are not going to have any more because you have taken all the spoils. [Applause.]
>
> You have received more political positions in the last few years than Democrats received under Republican administrations in the last 75 years. In the Alcoholic Unit of the Treasury Department there is not a Democrat holding a key position. [Applause.]
>
> This so-called merit system is owned, controlled, and dominated by Republicans—no wonder you holler for the merit system. They play the game and give us no chance in the world and cut our throats every time they get an opportunity. [Applause.] [104]

Whatever the interest of this controversy for the student of public administration and the civil service, its significance in this account is the perspective it yields on how far the attention of the House on that day lay from the enormously complex problems of launching a national program of subsidized housing—or what many of them, in defiance of simple common sense, considered to be to all intents and purposes the same thing: a national program of slum clearance.

It might be thought that the sharpness of the debate on the civil service was merely passing pique, rather than a main issue. Clearly, however, this was not the case: the one motion to recommit admitted under the rule governing debate on the bill was used, not to recommit (and thus defeat) the bill itself, but rather to recommit the bill with instructions to report it back to the House forthwith including a provision subjecting all employees of the Authority to the civil service and classification laws.[105] The motion was rejected by a heavily partisan vote, 221–140 and the bill then passed the House, 275–86. (In addition to the minority members, there were some who supported the motion in protest over the cavalier treatment of Chairman Ramspeck and the Committee on Civil Service.)

The conference between the two Houses on the 1937 bill was brief, (The bill was sent to conference on August 19, and the conference report was filed in the House on August 20.) but, if the reports of the conferees to their respective chambers are to be believed, rancorous.

Once again, the issues which generated strong feelings and hot debate between the conferees were not questions of housing policy. The numerous differences between the Senate and House bills on matters of substance apparently caused the conferees little difficulty. The sticking points were the provisions dealing with civil service and with the right of the Senate to confirm appointments to high-level positions.

Mr. Walsh, presenting the conference report to the Senate, described the situation that had confronted the Senate managers as follows:

> The House conferees pointed out that the only debate of serious purport in the other branch, when this bill was under consideration, was over the civil-service provision, that by an overwhelming vote the House voted the civil-service provision out of the bill. That information, of course, was presented to us, and the conferees on the part of the House said that it was useless to go back to the House unless we eliminated the civil-service provision completely.[106]

Finally a compromise was struck, but it was received with considerable disappointment in both Houses. (The compromise applied the civil service and classification laws to employees of the Authority, except for "officers, attorneys and experts," and for employees whose compensation exceeded $1,980 per annum. Senate confirmation was provided for appointments to positions carrying annual salary rates in excess of $7,500 per annum.)

In the Senate, Mr. Connally complained:

> I cannot understand the legislative state of mind of the House that would want to deny to the Senate the right of confirmation, because it inures to the benefit of the legislative branch.[107]

In the House, Mr. Fuller declared that the House conferees had flouted the will of the House as expressed in a record vote by making any concession at all to the Senate, and called for the rejection of the conference report.

As a matter of fact, there was sentiment in both chambers for rejecting the conference report and sending the issue back for further conference. On both sides, however, the proponents of such action were finally dissuaded on the basis that neither side could or would yield its position entirely, and that rejection of the compromise would in all probability result in the failure of the bill. In the end, therefore, the conference report was agreed to.

[104] Ibid., p. 11856.
[105] Ibid., p. 11873.
[106] Ibid., p. 12282.
[107] Ibid., p. 12287.

As to matters of substance, though they were hardly central to the controversy, the conference bill adhered with minor exceptions to the more restrictive provisions of the House bill. The House conferees did agree to a few concessions: The limit on loans at 85 percent of acquisition or development cost was raised to 90 percent, and the 25 percent local contribution which the House version provided for was reduced to 20 percent. The more liberal income-to-rent ratios of the Senate version were adopted. Still, the final bill was very much what the House had passed.

The focus of this inquiry, however, is not so much on what the Congress enacted—which is readily available in the statutes—as on what it was, if anything, that the Congress decided in 1937, specifically with regard to subsidizing housing for the poor in the United States. On this point, perhaps the final word should be left to Senator Walsh, who told the Senate—not in the course of its original consideration of the bill, but just prior to the adoption of the conference report—

> Mr. WALSH. Of course, the fact is fundamental to the whole discussion that this is not a housing bill.
>
> Mr. BANKHEAD. What is it?
>
> Mr. WALSH. It is a slum clearance bill. Some persons are trying to make it a housing bill, but it is not a housing bill.[108]

The 75th Congress had enacted a public law. What was left for the test of the future was whether, in so doing, it had enunciated a public policy.

The judgment of the future, as will be seen, proved to be that the Congress had agreed not upon a policy but upon a program; not upon an objective, but upon a technique. This crucial distinction reached its logical, and perhaps even its inevitable, end 36 years later, when the Nixon Administration—faced with each and all of the basic questions which the 75th Congress had bypassed and left unanswered—suspended all subsidized housing programs (pending further study).

Setting a Course for the Postwar Period

It appears that in enacting the U.S. Housing Act of 1937 the Congress had in mind creating a sort of American counterpart of the familiar group of publicly-owned and managed flats which had worked quite well in British villages and towns (and somewhat less well in the larger cities, where neighborhoods were less coherent and local governments more remote and impersonal).

It is a matter of speculation how this concept might have worked out if time and circumstance had permitted it to follow its own natural course. As events developed, this was not to be.

The new program got off to a relatively slow start, as most new programs do. The first actual appropriation for payment of annual contributions—in the amount of $5 million—was made for the fiscal year 1940. None of it was actually spent.

The reason for this extraordinary economy, according to the formal justification submitted to the House Committee on Appropriations, was that the newly-invented device of obtaining temporary (i.e., development) financing in the private market (instead of by borrowing from the Government) had made possible very substantial savings. It seems likely, however, that Administrator Straus' explanation was more to the point and more realistic. No contribution payments had been made, he told the committee, because projects had not been completed and occupied as rapidly as had been expected.

The public housing program was therefore still in its infancy when World War II broke out. In June of 1940, Public Law 671 (76th Congress) authorized the adaptation of the program to the support of the defense mobilization effort. In the following month, the Office of Defense Housing Coordinator was established in the Council of National Defense to plan a general defense housing program and coordinate its execution by private industry and by all the Government agencies with housing functions of one sort or another.

To the extent feasible, the Authority sought to keep the basic public housing program alive within the overriding framework of defense needs and priorities. Projects which seemed to offer little or no advantage to the defense effort were deferred (rather than canceled), and a relatively few occupied projects which were so situated as to have no significant defense applicability were continued in low rent occupancy. In the main, however, low income eligibility standards for admission were waived, and rents were raised to levels above those originally intended, but affordable by defense workers. Because such workers were generally rather well paid this frequently meant that full economic rents were charged. New projects were built to serve defense and war needs, though planned in the

[108] Ibid., p. 12282.

hope that at some unknown time in the future they could be restored to their originally intended use.

Thus it came about that, in 1944, when the Senate turned to a major effort at planning for the postwar period, it had as its main reference point for the whole difficult problem of housing lower income people a relatively new program, enacted by the Congress after long effort and much controversy, which was not only unproved but virtually untested as a means of solving the evils to which it was addressed—even if those could be identified with considerably more precision than, in fact, they had been.

One significant change, however, had occurred. As the war period drew to a close, several hundred local housing authorities had been organized and were staffed with architects, attorneys, social workers, managers, and maintenance crews. In short, the local authorities had substantial vested institutional interests not only in continuing to handle the projects already in being, but in resuming the program for which they had been created, and which had been preempted by the war.

The Senate Special Committee on Postwar Economic Policy and Planning established in 1944 a special Subcommittee on Housing and Urban Development, which was chaired by Senator Robert Taft, and included Senators Wagner and Ellender. (In fact, not the least significant accomplishment of this particular undertaking was to bring the immense prestige of Senator Taft to bear on the issues in a bipartisan alliance with Wagner and Ellender. They made a formidable trio.) After extensive study and hearings, the subcommittee prepared in August 1945 to state its conclusions and recommendations.

It began by noting that "From time to time, the Federal Government has established agencies to deal with one phase or another of the housing problem." It went on to note that:

> . . . These agencies have been created, and the legislative investigations accompanying their creation have usually been made, from the point of view of a particular situation often calling for an emergency solution.
>
> Thus, in order that private home mortgage institutions might more effectively meet the needs for home mortgage credit, the Home Loan Bank System was established. In the face of a general collapse of the mortgage credit structure, the Home Owners' Loan Corporation was established. In order to extend the field of mortgage credit and establish a new system of mortgage insurance, advocates of private housing secured the adoption of the National Housing Act, creating the Federal Housing Administration. In order to provide activity in the construction industry and to assist city dwellers of low income, the Public Works Administration, after experimentation with loans to private limited dividend companies, undertook the construction of public housing. Later, the interest in public housing led to the passage of the law setting up the United States Housing Authority. In each case, the need of the particular step was evident, but relation of each step to the whole was not clearly developed.[109]

(In point of fact, as noted earlier in this account, this is not precisely what occurred with regard to the initiation of the public housing program.)

Having thus called attention to the somewhat incoherent character of the growth of a Federal role in housing, the subcommittee went on to make some striking observations which suggested that it was laying the foundation for the formulation of a coherent housing policy for the Nation:

> From the social point of view, a supply of good housing, sufficient to meet the needs of all families, is essential to a sound and stable democracy.
>
> . . . [But] Up to the present time, we have never been able to approach the objective of an adequate supply of decent housing. . . .
>
> We can no longer accept these conditions as unavoidable. We cannot safely face the difficult undertakings of the years ahead, with the burden of hardship and discontent that bad housing imposes upon us. The issue must be faced and the task assumed. It is a task which cannot be performed in 1 year, nor perhaps in a decade, but one which as a nation we must devotedly pursue and accomplish as rapidly as proper use of our resources permits.

The writers of the report continued on a very upbeat note:

> The subcommittee believes that the means are available for the accomplishment. A nation inspired by victory, an industry alert to new responsibilities and new opportunities can, with the cooperation of government, solve this problem. The subcommittee is confident that this can be done without departure from democratic procedure or violence to an enterprise system based on private initiative.

In the light of this preamble, it is more than a little disappointing to have to record that the breadth of vision and the confidence in the feasibility and the outcome of a public policy on housing, which glowed so brightly on page 3 of this report, began to dim very strikingly as early as page 7.

In the very first sentence of their discussion of the proper responsibility in this area of the Federal Government, the authors led off with the astonishing and unqualified statement: "Housing is fundamentally a local problem." Without pausing to comment on the fact that this assertion was plainly in violent conflict with what they had already said—and indeed, called into question their legitimate interest in making such a report at all—they hurried on to surround any prospective Federal role with metes and bounds. Thus:

[109] All quotations on pages in this section, unless otherwise noted, are from the *Report, Postwar Housing,* Subcommittee on Housing and Urban Redevelopment, Aug. 1, 1945 (Committee Print).

The first responsibility for its solution rests upon the community where it is to be located. This subcommittee has carefully considered the place of the Federal Government in respect to the housing situation and is greatly concerned that it should not invade the proper functions of State or local government or of private enterprise.

The basic stance which the subcommittee had put forward under the heading of "Considerations of Policy" was already tottering, but the subcommittee was not yet done with demolishing the structure it had so recently erected. Federal housing programs employing various mortgage credit devices had been found generally acceptable, it suggested, not because they dealt with housing, but because they dealt with money. Their argument continues:

General problems of banking and finance have always been the concern of the Federal Government. Abuses which arise in that field have, from the beginning of the Republic, been a concern of Federal legislation, and banking institutions have been subjected to rigorous regulation. Capital is extremely liquid, and it is important that capital existing in one State be readily available in every other State where it may be needed.

In the establishment of the home-loan banks and the Federal Housing Administration, the Federal Government undertook to provide conditions under which money seeking investment would flow easily into home construction. It was made possible to provide loans up to 80 percent, and even 90 percent, of the total value of dwelling units to spread the payment over a long period of years and to reduce the rate of interest, with a most substantial effect upon the total carrying charge to the owner. This activity of the Federal Government has met with almost universal approval and should be continued and expanded, providing it is kept on a sound financial basis.

The subcommittee observed glumly, however, "The entrance of the Federal Government into public housing has produced a much greater controversy."

Even in so starkly simple a matter as the need for public subsidy, the subcommittee had difficulty in articulating any such broad and far-sighted approach as it had called for but a few pages earlier. ". . . With a better balance between housing cost and family income," it wrote,

it would be easier to market a satisfactory volume of housing through the normal channels of private enterprise. But the evidence indicates that for a substantial portion of our population this balance does not exist.

Yet from this clear and indisputable proposition the report managed, not to deduce that a program of public subsidies would be essential if there were to be that supply of good housing available to all families that they had declared to be "essential to a sound and stable democracy"—but to conclude instead that something really ought to be done about housing costs—thus:

If we are to solve the housing problem, we must not only reach and maintain a high level of income but, so far as possible bring about a reduction in the cost of housing—the cost of financing, the cost of labor, the cost of materials, and the cost of putting labor and materials together.

Through the Federal home loan bank and the Federal Housing Administration, the cost of home financing has been substantially reduced. It is questionable that this cost can be further lowered at this time and still keep funds available for investment. It may be expected, however, that American ingenuity, operating through the construction industry, can find methods of reducing building costs as it has reduced costs in the manufacture of automobiles and other mass-production products.

There was, of course, no shred of evidence before the subcommittee that this would or could be done, let alone that there was anyone available with any concrete idea about how to do it. Later in its report, the subcommittee suggested increased efforts in research. (In this respect, the subcommittee's treatment differed little from similar occasions in subsequent years, when this formulation was advanced over and over again, each time as if it were a novel solution to a novel problem. See, e.g., the Housing Expediter's program in 1946; the Housing Acts of 1948 and 1949; various subsequent research enactments; and, most recently, Operation Breakthrough.)

As deeply as it had already marched into this bog, however, the subcommittee could hardly leave the matter there with a straight face. Reluctantly it concluded:

. . . With the best that may be accomplished, however, we shall for the present continue to face a condition which the relationship between cost and income will, in all probability, hamper the construction and sale, or rent, of a sufficient number of houses to meet the potential demand. Government policy, consequently, must be developed in the light of this circumstance.

The Need for Subsidized Housing

Having thus painted itself into a corner, the subcommittee was prepared to acknowledge, and even proclaim, the necessity for at least some subsidized housing—with what degree of discomfort can be judged at least in part from the rhetoric in which their conclusions were couched:

. . . With the revival of construction, many of these families [living in substandard shelter] should be able to find used houses, depreciated in value, but still in good condition. Many other families will be able to find new housing in outlying communities.

And finally, after having been poised so long upon the diving board of this particular policy, the leap:

But, recognizing all this, the subcommittee is strongly of the opinion that the present housing situation cannot be satisfactorily dealt with except by the gradual elimination of slum housing and the provision of a reasonable percentage of subsidized housing to replace it.

This was hardly rhetoric calculated to stir men to action, but it did at least acknowledge that there was a problem which needed to be met—even though it must have occurred to many contemporary readers that what a "reasonable percentage" might be was a matter on which reasonable, and even unreasonable, men would almost surely differ.

The Methodology of Subsidy

As in earlier hearings, many different means of bringing a public subsidy to bear upon the rent bill of a private family were offered to the subcommittee, and no doubt considered by it, at least in some measure. It seems clear, however, that the context of this consideration was not an approach to the problem de novo, but in terms of a comparison of other possibilities to what was assumed to be an existing and workable device already in hand. Here again, the tenor of the subcommittee's language is even more revealing of its line of thought than are the specific conclusions.

Specifically, the subcommittee report dealt with the two most commonly advocated alternative subsidy methods—what it called "rent certificates" (now more frequently referred to as "housing allowances"), and "subsidies to private owners" (more recently, and perhaps somewhat more obliquely, called "interest rate subsidies"). It rejected both—but in each case with reservations. Thus, with respect to the first, the subcommittee said:

It has been argued before the subcommittee that such families should be assisted by rent certificates just as grocery stamps have been furnished to needy families. The number of families entitled to rent certificates upon any such basis would be infinitely larger than those requiring other relief. It is not at all certain that such a plan would bring about improvement in the bad housing accommodations that now exist. In fact, the scheme might work to maintain the profitability of slum areas and, consequently, to retard their elimination. It would certainly require a detailed regulation of private rental quarters both as to condition and rent.

And as regards the other plan:

The subcommittee has considered the practicability of providing low-rent housing through subsidies to private owners of rental housing projects instead of to public authorities. It is conceivable that in time such a plan might be developed, if the need for subsidy is long continued. For the present, it seems evident that a Federal subsidy per family to a private owner would have to be larger than in the case of public housing, even though private costs might be somewhat lower. This is largely because the public housing authorities get two aids not readily available to private owners—local tax exemption and an interest rate based on a tax-free security.

Then followed the conclusion, which it is hard to believe had not been in the minds of the authors throughout their study:

. . . It is the conclusion of the subcommittee that the principle and methods now in existence for granting aid be continued, at least for the present, in preference to some new and untried plan.

The authors of the report did not think it necessary to point out that the "principle and methods" then in existence themselves constituted, at least in their American variant, "a new and untried plan."

Having committed itself both to a program and a method, the subcommittee was at pains to stress how narrow was the commitment they were prepared to undertake:

In facing the necessity for public housing, the subcommittee does not feel that the Government should attempt to provide for all families now living in substandard shelter . . . .

. . . the continuation of the public housing program must be subject to certain definite conditions in order that it may not become competitive with private enterprise . . . .

The subcommittee wishes to emphasize that public housing is only justified as long as private industry is not able to provide for the lower-income families. Emphasis must be kept upon the objective of broadening the scope of private enterprise through improvement of family income and reduction of housing cost. Public housing programs should be regularly reviewed and modified in the light of changing conditions in the general economy and in the construction industry.

And, lest any reader might have been inattentive or remarkably thick, the authors took the precaution of adding, only one page later, as part of a "Statement of the Policy of the Federal Government":

The provision of housing in the United States is declared to be primarily and predominantly the function of private investment and finance, private construction, and private ownership and management. Public intervention must be designed and administered so as to stimulate and supplement, not to impede or supplant, private operations.

They also went on to spell out the various "definite conditions" to which they had referred, of which the last and most stringent was that ". . . in establishing the rentals on new projects, . . . [a spread should be maintained between them and private rentals] . . . not less than 20 percent of the lowest rentals being currently charged for safe and sanitary private dwellings." Thus the "20 percent Gap" took definite (though not final) form.

There remained only the question of attaching some dimension to the program being proposed. The subcommittee suggested 500,000 units, over a 4-year period.

One hardly needs to be a socialist of even the mildest persuasion to reflect that this degree of priority for profits over purposes suggests a higher commitment to caution than to construction so far as housing for the lower income strata is concerned. This is all the more true in light of the fact that there was a good deal of evidence that large segments of private enterprise regarded the whole subject with massive indifference. Of those actively concerned, some were quite ready to admit that they had no hope of providing decent housing at prices the poor could afford to pay without the help of public subsidy. A not inconsiderable number were a good deal less concerned with protecting their preferential right to try, than with preserving their right to continue to provide the poor with substandard housing, under highly profitable arrangements.

Nevertheless, this was the reading of the Subcommittee on Housing and Urban Development as to the price that would have to be paid even for the modest undertaking they felt might be accepted. These were not hard or self-interested men. They included the three most convinced, energetic, and sympathetic members of the Senate. It would be a self-confident historian indeed who would undertake to pronounce that their reading of the political situation was wrong. Whether they were prescient enough to know how high that price would ultimately prove to be is another matter.

The President's Advisory Committee—1953

The whole subject of subsidized housing—along with many others—received yet another full dress review from the President's Advisory Committee on Government Housing Policies and Programs, established by President Eisenhower in 1953.

The committee reached no striking or novel conclusions. The public housing program established by the 1937 act, it concluded, was needed and should be continued. The Subcommittee on Housing for Low Income Families said in its report that the only alternatives that had been suggested in the course of their study were "rent certificate" plans, in a number of varying forms. All of these they found objectionable in themselves for one reason or another, and less desirable than the existing program. The size and rate of the public housing program, they concluded, were matters to be determined by the Administration and the Congress.[110]

Efforts to Help the Middle or Moderate Income Level

Ever since the enactment of the low rent public housing program in 1937, there had grown up a sort of uneasiness, both in Congress and among many private groups, about the logical inconsistency of a Government housing policy, or policies, under which substantial subsidies were made available to people of very low income, and many forms of assistance were extended to those whose incomes were competitive in the private market, while no Federal aid of any effective sort was afforded to so-called "middle income" families. (Or, as they were variously called, "moderate income" families, or families of "modest" income.) While this term was never very precisely defined, such families conceptually were thought to be those whose incomes were somewhat too high to permit them to be eligible for public housing, yet not high enough for them to afford adequate private housing.

Originally it had been supposed that these were the families whose housing needs would be met by the "trickle-down" process—that is, they would be able to acquire older but still sound housing that had depreciated to prices within their means, and that would become available as the original (and, presumably, more prosperous) owners upgraded their own accommodations.

Time and experience, however, appeared to raise serious question as to whether the trickle-down theory, as appealing as it was on paper, actually offered much relief in practice. There were at least two important practical flaws in the idea.

The first was the fact that the growth of the population and of the number of families proved to be of an order of magnitude roughly similar to that of the supply of housing (although somewhat different in timing during various intervals). The result was that, while the number of standard housing units in the national stock did indeed increase, so did the number of would-be claimants, and the relative position of the middle income group failed to improve significantly.

The second (and not altogether unrelated) problem was that inflation in residential real es-

[110] *Government Housing Policies and Programs*, Report of the President's Advisory Committee, U.S. Government Printing Office, December 1953.

tate values at least kept pace with and often outstripped that in the general economy. Consequently, older housing still in good basic condition tended not only to maintain its value, but often went up in price. Thus, such housing, so to speak, seemed to trickle sideways or even up, rather than down.

The uncomfortable nature of this dilemma was not only more sharply defined but also more clearly highlighted with the enactment of the "20 percent gap" formula in the public housing program—a provision added in the Housing Act of 1949 that expressly required the demonstration of a gap of at least 20 percent between the upper rental limits for admission to proposed low rent housing, and the lowest rentals at which private enterprise unaided by subsidy was providing in the area a "substantial supply" of decent, safe, and sanitary housing. This requirement was intended to overcome or at least mitigate the fears of private developers that public housing might reach and even overlap with their markets. Nevertheless, it had the effect of arbitrarily excluding a segment of undeniably low income families from the benefits of the program.

In practical application, the requirement meant that in a community where a monthly income of $200 (for example) was the minimum necessary to command decent, safe, and sanitary housing (and to actually have some hope of finding it), a family with an income of $160 a month would be eligible for full subsidy, while a similar family with an income of $165 a month (or, in theory, even $161) could get nothing, and might even stand to benefit substantially from a small cut in pay.

Rising pressure for legislation to relieve this anomaly resulted in a major legislative proposal made and vigorously supported by the executive branch in 1950. It would have authorized a Government mixed-ownership corporation to make direct loans, at less than market rates, to cooperatives and other nonprofit corporations for providing housing to middle income families. Such families were described as families of average workingmen or persons having cash incomes between $2,800 and $4,400 a year.

That legislation was defeated by a close vote on the Senate floor, primarily because of the prevailing fear that it would infringe excessively on private mortgage lenders over too broad a range of housing activity. Subsequently during the 1950's, special mortgage insurance and loan programs, or other aids were enacted for various groups having special housing needs (e.g., the elderly), but none for middle income families generally.

The Below-Market Program of FHA Section 221(d)(3)

The Housing Act of 1961 included enactment of the first subsidized housing program for middle or moderate income families, known as the below-market interest rate program of FHA section 221(d)(3).[111]

In addition to the awkward problems of equity to the excluded group of families in between the economic levels of public and acceptable private housing, there were at least three other considerations that played a part in the decisions of the administration and the Congress to take this step:

Decline in Housing Production: For 1960, the year prior to the enactment of section 221(d)(3), home building had been on the decline, dropping to 1,258,000 starts—18 percent below the previous year.[112] A significant reduction occurred in mortgage lending, and by March 1961, about one out of every five construction workers was unemployed.[113] These circumstances contributed heavily to the belief that further legislation was desirable to stimulate housing production for moderate income families. The Senate committee, for instance, after discussing the need for action to stimulate a distressed housing economy, referred to moderate income families, one may think not altogether philanthropically, as ". . . a large untapped market heretofore largely overlooked and neglected."[114]

Central City Housing Needs: Previous housing programs had proved inadequate to materially improve the blighted conditions of central cities throughout the nation. There was increasing recognition of that problem, and demands were being made by cities and other organizations for more effective solutions involving additional Federal assistance.

Political Considerations: The section 221(d)(3) program was proposed by the incoming Kennedy administration among its major housing recommendations embodied in the "Housing Bill

[111] Sec. 221(d)(3) of the National Housing Act, as amended by sec. 101(a) of the Housing Act of 1961.

[112] "Housing Legislation of 1961—Review of Federal Housing Programs," a committee document printed as an appendix to hearings by the Subcommittee on Housing of the Senate Committee on Banking and Currency, 87th Congress, on various housing bills, Apr. 4 to 20, 1961, p. 1.

[113] Testimony of Secretary Weaver at hearings by the Subcommittee on Housing of the House Committee on Banking and Currency, 87th Congress, on H.R. 6028 and other housing bills, Apr. 24 to May 5, 1961, p. 45.

[114] S. Rept. 281, 87th Congress, 1st Session, p. 3.

of 1961"—one of its major domestic efforts. That bill was comprehensive and constituted one of the most important housing measures ever proposed by the executive branch. The part of the bill relating to housing for middle income families—including the new section 221(d)(3)—was placed at the beginning of the bill, as the main thrust of the legislation. It thereby lent a significance or "glamor" to the legislation considered beneficial from a public relations and political standpoint.

Purpose and Provisions of Section 221(d)(3): To provide important new housing assistance to families of low and moderate income, the Housing Act of 1961 conferred on that general category the special mortgage insurance advantages previously applicable only to housing for families displaced by urban renewal or other governmental action (section 221), and added substantially greater benefits for all low and moderate income families. Subsection (d)(3) was the part of the revised 221 which established the new subsidy program for rental housing.

A part of the new legislation (section 221(d)(2)) consisted of special mortgage insurance on very liberal terms for home purchasers, but without provision for overt subsidy. Section 221(d)(3), to assist rental housing, embodied a form of subsidy considered essential to bring rentals within the reach of those who could not afford to purchase homes, even with the new special insurance terms proposed. It was intended primarily for moderate income families living in central cities where high land costs made it impractical to provide single family homes.[115]

As noted above, another express purpose of all of this legislation was the stimulation and acceleration of housing construction as a means of alleviating the then existing depression in the home building and related industries.[116]

In presenting the legislation to the Congress as part of the proposed 1961 act, Housing and Home Finance Administrator Weaver used the term "moderate income" families instead of the term "middle income" families that had been in common use. The Administrator described that group of families as those with incomes between $4,000 and $6,000. There were then estimated to be some 11 million families in the country within that range. In general, those were thought to fall in the range of incomes too high for public housing but too low for paying rents in decent private housing.

[115] Testimony cited in footnote 112, supra, p. 101.
[116] Ibid., p. 98.

Perhaps the key decisions on this legislation dealt with the form and extent of the subsidy to be used to reach that income group. The form was very important, as well as the amount of the subsidy, as a means of obtaining acceptance in the Congress and avoiding the antagonisms that had defeated the middle income housing program in 1950.

Accordingly, the form of the new subsidy program was modeled on or adapted from the successful experience under the special assistance functions of the Federal National Mortgage Association, (now handled by the Government National Mortgage Association in HUD), which had often been well accepted by the Congress. Under those functions, insured mortgages were purchased by FNMA at par, or otherwise above-market prices, where necessary to encourage lenders to participate in certain housing programs with special social objectives. The private lender was induced to originate the loan at a below-market rate on the basis of a commitment that he could sell the loan when completed to the FNMA at a price acceptable to him. The ultimate objective was intended to be a lower cost to the home purchaser or tenant resulting from the lower burden of debt service.

This special assistance technique was embodied in the new program, with an additional feature that amounted to an overt subsidy. The FHA was authorized to insure and the FNMA to purchase mortgages bearing an interest rate (as provided in the 1961 enactment) as low as the average market yield on all outstanding, marketable obligations of the United States (plus ⅛ percent) that at that time amounted to 3⅛ percent.

In addition, the statute authorized the FHA insurance to be written under the program at a reduced premium or without premium charge, and authorized appropriations to the section 221 Housing Insurance Fund to reimburse it for any resulting net losses.

The Government's financial losses through the absence of premium charges and through the purchase of mortgages with interest rates well below market rates constituted the subsidy to the financing of the projects under section 221(d)(3). In a sense, this amounted to an indirect Federal loan program through private lenders, with interest rates designed to reduce debt service (charges to borrowers) and provide lower rentals for tenants.

The statute contained no provision prescribing a formula for the specific rentals to be charged or the income limits to be applied. The only requirement in this regard was that "low and moderate income families displaced by urban renewal or other governmental action shall be eligible for occupancy in accordance with such regulations and procedures as may be prescribed by the (FHA) Commissioner." It should be noted, however, that the statute utilized most of the provisions of the then existing section 221 which had been designed to serve families displaced by urban renewal or other governmental action, and maximum rentals had been established for eligible families under that authority pursuant to a similar broad discretion. The report on the legislation by the Senate Committee on Banking and Currency contained this related legislative history:[117]

In all cases where the interest rate is below the market or where the FHA insurance premium is waived, occupancy of the projects would be limited to families and individuals whose incomes exclude them from standard housing in the private market. This limitation would be achieved through regulatory requirements which would necessarily differ depending on whether the borrower is providing nonprofit rental housing, cooperative housing, or limited profit rental housing. However, there would be no evictions required by Federal law on the grounds that a family's income had risen during occupancy. This is a matter which would be left to the discretion of the organization owning the project.

This last point was an important departure from the practice in the low rent public housing program, where tenants whose incomes rose above applicable fixed limits were required to leave the projects and, if necessary, evicted by legal process. This was one of the features of public housing which gave rise to serious misgivings in many minds about its long-term social effects.

In practice, section 221(d)(3) income limits were established administratively at roughly the local median income limit for a given size family.

As a further incentive to participation in this new rental program, the maximum insurance mortgage amount could be 100 percent of replacement cost in the case of new construction. In the case of rehabilitation, the maximum mortgage amount (100 percent) was based on value, as in other FHA programs, but a modification was introduced to encourage further participation. Instead of the mortgages being based simply on the value of the property after improvement, it was based on the value of the property before improvement plus the estimated cost of the improvement. As additional incentives, maximum mortgage amounts and terms could be made more liberal than previously, and the FHA was authorized to agree to pay insurance claims in cash instead of in debentures.

Because of the subsidy feature of the program, an eligible mortgagor-builder was required under the original legislation to be a public body (other than one receiving Federal aid solely for public housing), a cooperative, a limited dividend corporation, or a regulated or supervised private nonprofit corporation. Later, however, the Housing Act of 1964 (section 114(a)) also made eligible other mortgagors "approved by the (FHA) Commissioner."

Because the 221(d)(3) program was designed primarily for central cities, and to help meet the cities' problems of blight, the previous requirement for a "workable program" under section 221 was made applicable to the new rental program (but not for mortgage insurance assistance for single-family homes, which was regarded as a program more useful for suburban development). Under that workable program requirement, (d)(3) housing could not be built in a city unless it had adopted an "official plan of action" for effectively dealing with the problems of urban slums and blight within the community, and for the establishment and preservation of well-organized neighborhoods of decent homes and suitable living environments.

Because of the innovative features of the new program, it was proposed and enacted as "experimental," with a termination date of July 1, 1965. The date has been extended periodically to the present time.

Operations Under Section 221(d)(3): As a production incentive, the (d)(3) program was substantially successful. Administrator Weaver testified at hearings in 1965 that the program moved more rapidly than any other FHA had initiated, and that about 90,000 units had been or were then in the process of being financed under the program.[118] The provisions authorizing this program were among a number of liberalizing amendments of special FHA programs which helped boost all FHA operations to over $7 billion during 1963.

Problems developed in reaching the family income level desired under the program. The Administrator testified that from the very start this program only took the top of the moderate income market. He said the median income of the families in (d)(3) projects in 1965 was about

[117] S. Rept. 281, supra, p. 8.

[118] Hearings before a subcommittee of the Senate Committee on Banking and Currency, 89th Congress, on Housing Legislation of 1965 (S. 1354 and other bills) Apr. 1, to 9, 1965, p. 16.

$5,000. Testimony by the National Association of Housing and Redevelopment officials at the same hearing [119] indicated that reports showed median rentals under the program were about $20 per month below median rentals for the FHA regular market rate programs. For a 2-bedroom unit under (d)(3) that was estimated to be between $120 and $130 per month.

The problems in reaching lower income families under the program were aggravated by rising interest rates. An effort to obtain amendatory relief was sought by the Administrator within the executive branch. He pointed out that the (d)(3) mortgage interest rate, based on a Federal going rate formula, had increased gradually from 3⅛ percent to 3⅞ percent, and threatened soon to go to 4 percent. Each increase necessarily meant higher debt service and rentals, and therefore higher income groups which could be served.

The administration did not recommend a change in the rate, choosing to rely instead upon a rent supplement program it was proposing at that time to reach the families it wished to assist, as discussed later. However, the Congress (in the Housing and Urban Development Act of 1965) fixed the interest rate at 3 percent, in lieu of the formula tying the rate to that on Federal borrowing.[120]

The lowering of the interest rate in that way assisted in reaching lower income families, but it also made the program more vulnerable to later attack. As long as the program rate was tied to the rate on Federal borrowing, it was more analogous to the regular, accepted operations under the Government's special assistance functions. Although complete recovery of the Government's investment in the mortgages could not be expected, the fluctuating mortgage rates under the original formula maintained a consistent amount of Federal subsidy by being geared to the cost of money to the Government. In fact, it could be argued that the Government's total loss was only the amount that would otherwise be charged as a premium for the insurance. A fixed 3-percent rate, however, meant that an overt subsidy was also clearly provided as a result of the interest rate on the mortgage.

Another problem involving rentals arose after some of the projects had been in operation a short time. No adjustment had been made in tenants' rents as a result of increases in their incomes, and thus they continued to receive the full subsidy benefit. As indicated, the legislative history stated that tenants need not be evicted because of their increased incomes. Occupancy by some high income tenants in projects resulted in substantial adverse publicity. Accordingly, a procedure was adopted to raise rentals when tenant incomes increased above a certain level.

As the (d)(3) program progressed, it became more and more evident that it had an inherent vulnerability which would eventually lead to its curtailment and termination. That was its budget impact. Mortgages under the program were bought by FNMA as soon as completed and insured, and were necessarily held by FNMA. Under the rules governing such matters, the Federal budget was increased by the entire amount of FNMA's mortgage purchases. Since the program does not generate offsetting mortgage sales, and no account is taken of future receipts to be generated by the portfolio, the budget impact on one particular year could be significant.

In this respect, the 221(d)(3) program might be said to be a victim of its own success. Had it proved ineffective and unattractive in the market, production and hence budget impact would have remained small and the program would have attracted little attention from this standpoint. However, in the measure that it took hold and expanded into a major activity—which is to say, in the measure that it began to achieve the purposes for which it had been enacted—its budget impact grew until it became first uncomfortably and then painfully large.

As early as 1965, the executive branch was exercising budget controls over the volume of new 221(d)(3) housing to be initiated, and proposing a new program intended to result in private, rather than Government mortgage investment in moderate income housing. It was hoped that this program would reduce the demand for (d)(3), if not replace it altogether. In 1968, the executive branch sought and obtained legislation that it used to supersede (d)(3) altogether. These programs are discussed in following sections.

The Rent Supplement Program

In 1965, the executive branch tried again to find a means for achieving a more balanced continuum of Federal aids for the housing of families whose incomes were below those adequately served in the general private market. This new effort was called a "rent supplement" program, and was recommended by the President in a special Presidential message on problems of

[119] Ibid., p. 310.
[120] Sec. 102(b) of the Housing and Urban Development Act of 1965.

housing and of the cities.[121] It was to have a turbulent and, in some respects, curious history.

It will be recalled that by 1965 the Federal fiscal authorities were already uncomfortable, to say the least, over the budgetary impact generated by the growing program under section 221(d)(3). Moreover, since the below-market interest rate (BMIR) of that program was tied to long term Treasury borrowing rates by formula, and since the latter were steadily rising, it had become abundantly clear that the BMIR program under (d)(3) could at best be relied on to provide some relief in the uppermost band of what might be called the lower middle income group—or, to put it differently, those who fell in the top part of the 20 percent gap that had been decreed between public housing and standard housing in the private market.

To bring achievable rent levels under this program farther down into the gap zone, it would have been necessary to deepen the subsidy by reducing the interest rate. This, of course, would also have had the effect of giving the program a sharp stimulus to expand, thus further increasing its demands on the budget—an unacceptable course, at least from the viewpoint of the Treasury and Budget officials.

There was yet another, and related, consideration in attempting to formulate a new approach. Somewhat earlier, the Bureau of the Budget had entered into an informal but binding understanding with the Chairman of the Appropriations Committee of the House to the effect that, in return for the committee refraining from efforts to block certain legislation then pending, the executive branch would in the future submit all new program proposals in a form amenable to control through the annual appropriations process—in a word, to renounce "back-door financing."

To avoid a digression, it may be as well to define this term here. "Back-door financing" is a pejorative expression, as used in congressional circles, intended to suggest that the program operator or administrator involved has been provided a key to the back door of the Treasury. It is applied to any form of statutory authorization (e.g., contract authority) under which an executive official is empowered to enter into firm and binding contracts on behalf of the United States without the intervention of a second consideration of the matter in an appropriation measure, following and based upon the authorizing legislation.

(It will be recognized that many, if not most, of the major problems in housing and urban development had been originally launched on the basis of so-called back-door financing—including, for example, low rent public housing and urban renewal, as well as a number of others. The arguments for and against these forms of authorization, while exceedingly interesting, are beyond the scope of the present inquiry.)

Thus, any new program proposal, in order to pass muster even within the executive branch, would have to satisfy three standards:

1. It would have to keep faith with the Appropriations Committee by providing program control through the appropriations process;

2. It would have to have a relatively minor budget impact, at least in the early years; and

3. It would have to offer some hope that it might absorb the BMIR program, and thus fend off or at least temper its rising demands on the budget.

The new rent supplement proposal met all three of these standards admirably.

The administration bill was directed quite explicitly at the 20 percent gap. Indeed, a "qualified tenant" (i.e., one qualified for assistance under the bill) was defined as follows:

> As used in this section, a "qualified tenant" means any individual or family who has, pursuant to criteria and procedures established by the Administrator, been determined—
>
> (1) to have an income below the amount required to obtain standard privately owned housing in the area that is conventionally financed or that is financed with a market interest rate mortgage insured under said section 221(d)(3), but above the amount which would be necessary for low-income families generally to obtain admission to public housing dwellings, in the same or a similar area, of a size comparable to the dwelling of the housing owner which is occupied, or to be occupied, by the qualified tenant; . . .[122]

The definition went on to limit eligibility, within these income brackets, to four specified groups:

- The elderly;
- The physically handicapped;
- Those displaced from their homes by governmental action; and
- Those occupying substandard housing.

The categories are perhaps not quite so restrictive as they appear at first glance, since the fourth class—within the established income boundaries—can reasonably be thought to be

[121] H. Doc. 99, 89th Congress, 1st Session.

[122] H.R. 5840, 89th Congress, 1st Session, sec. 101(c).

roughly equivalent to "everybody else in actual need of subsidy assistance." Clearly, there would be little reason to make a subsidy available to a family even of eligible income that, through some happy circumstance, was already adequately housed without such assistance.

Eligible sponsors were restricted to private nonprofit, cooperative, or limited dividend organizations. The financing vehicle for a project was to be a mortgage insured under 221(d)(3) at a market interest rate. The subsidy formula provided that a "qualified tenant" would have to pay 20 percent—or 25 percent, in the case of a tenant under a lease-purchase agreement—of his income toward the economic rent of the unit he would occupy, with the Federal Government contributing a "supplement" amounting to the difference.

There was, in fact, nothing that was terribly new or startling about this proposal. It was one of the possible forms of subsidy pointed out by Dr. Wood some 30 years earlier, and it closely resembled some of the variations on the "rent certificate" theme which had been offered to the Taft Subcommittee in the middle 1940's. Given this background, the hubbub which resulted from the rent supplement proposal can only be described as astonishing.

Matters started off quietly enough with the presentation of the proposal in hearings before the Housing Subcommittee of the House Committee on Banking and Currency. Administrator Weaver's testimony in support of the bill was courteously received and duly complimented. In the course of it he made the basic nature of the plan quite clear. Pointing out that a few specific previous actions had been helpful to lower middle income people on a limited scale—direct low-interest loans for the elderly, for example—he continued:

> As helpful as these programs have been, they reach only a small part of the middle-income families. Of the approximately 1.6 million housing starts last year, only a small proportion were units assisted under Federal or State programs designed to help these families.
>
> This can be compared with about 4 million of the Nation's families who are within the income range where they are unable to afford decent housing, but have incomes above those permitted for admission to public housing. Of these families, almost half are elderly or handicapped, and the others all live in substandard housing. There are also an estimated 300,000 families who will be displaced from their homes by governmental action over the next 4 years and many of them, too, will be in this income range.
>
> It is this group of approximately 4 million families to which the proposed new program is directed.[123]

[123] Hearings before the Subcommittee on Housing, House Committee on Banking and Currency, on H.R. 5840 and related bills, Mar. 25-31, 1965, p. 168.

And somewhat later he went on to say, in response to a question by the Chairman:

> Mr. BARRETT. Doctor, would you say now we are talking about the "rich poor"?
>
> Mr. WEAVER. Some people would say so. It is a dubious distinction I would say. We are trying to get a program that will come down and substantially close the gap between where section 221(d)(3) begins and where public housing ends.[124]

There were only mild hints of the explosion which was soon to occur. Mrs. Sullivan voiced her "suspicion" that perhaps the program had gotten by the Bureau of the Budget because of its minimum initial impact on the budget. (The Administrator acknowledged that this factor had not hurt the program's reception.) She went on to inquire:

> Mrs. SULLIVAN. In the long run, would it not be more costly for the Government?
>
> Mr. WEAVER. It could be, but I think there are other compensations . . . .[125]

Mr. Fino observed that ". . . the thing that concerns me is the favoring of a small number of middle-class people over others," [126] and went on to suggest that the needs of lower income people were much greater than those of the bracket toward which the program was directed.

The National Association of Home Builders and the AFL-CIO both endorsed the program in principle, while objecting to the concept that it should be substituted for that under section 221(d)(3). Perhaps the strongest language was that used by the National Association of Housing and Redevelopment Officials (NAHRO) that described the proposed rent supplement program as ". . . at best . . . administratively cumbersome and socially indefensible." [127] Significantly, no doubt, a disproportionate share of the hearing was devoted to rent supplements, considering the length and sweep of the 1965 bill.

Little in the record, however, set the stage for the committee report, in which the opponents of the rent supplement proposal burst out with 16 pages of minority views, which, for sheer violence and vituperation, were probably not unprecedented but were at least unusual. The tone is suggested by the introduction to the minority report, which began as follows:

> MINORITY VIEWS
> THE ADMINISTRATION'S RENT SUPPLEMENT PROPOSAL
> Introduction
>
> The Administration's rent supplement proposal con-

[124] Ibid., p. 230.
[125] Ibid., p. 234.
[126] Ibid., p. 232.
[127] Ibid., p. 427.

tained in section 101 of this bill is foreign to American concepts.

The proposal kills the incentive of the American family to improve its living accommodations by its own efforts.

It kills the incentive for homeownership; it makes renters wards of the Government.

It is a system of economic integration of housing through Government subsidy.

It is the way of the socialistic state. [128]

The spirit of the discussion which followed did not greatly depart from the hyperbole of the introduction. For example, the minority elaborated a most implausible set of assumptions pursuant to which, they insisted, a welfare family might under the bill occupy a $100,000 penthouse renting for $800 a month rent-free, with the Government paying the entire bill (see *Report,* op. cit., p. 178). This led them to characterize the proposal, variously, as "fantastic," "ridiculous," and "absurd."

The extraordinary violence of the minority attack, in turn, provoked the committee leadership into the very unusual step of issuing a formal rebuttal, in the form of a Committee Print. While perhaps a bit less tendentious in tone than the minority report, it was hardly a bland document. Cast in the form of a restatement of the minority contentions, each followed by a discussion under the heading ANSWER, the response to one contention began with the one-sentence paragraph, "This is patently ridiculous." Three others began with single sentence statements asserting bluntly, "This is false." Even the title was hardly calculated to be soothing in its effect on the opposition. It read:

CORRECTION OF MISLEADING AND FALSE STATEMENTS CONCERNING RENT SUPPLEMENT PROGRAM MADE IN MINORITY REPORT ON THE HOUSING AND URBAN DEVELOPMENT ACT OF 1965—H.R. 7984[129]

The sharpness of these reactions was all the more surprising in view of the fact that—although the committee report hardly mentioned the subject in either the majority or minority views—the committee had reported out a bill which differed quite drastically from what the administration had recommended.

Thus, the committee took what had been the subsidy formula in the original bill, and made it also the eligibility formula. The gap concept between public and private housing was dropped altogether, and eligibility was made to rest on a family's inability to obtain adequate housing in the private market at a rent not exceeding 25 percent of its income—not, it will be noted, the 20 percent figure proposed in the administration bill. The lease-purchase feature, involving a higher percentage commitment of income, was dropped.

Thus, the committee had operated on the administration's floor-and-ceiling concept of eligibility for the new program, first by slightly lowering the ceiling (through the shift from 20 percent of income to 25 percent), and second by eliminating the floor altogether.

These changes offered some comfort to those who saw the new program as a general adventure into subsidization of the middle class. By the same token, they further heightened the alarm of the dedicated proponents and practitioners of the low rent public housing program, who saw the rent supplement program more and more, not as a threat to 221(d) (3) but to their own special preserve. In this general atmosphere of rancor, accusation, and counteraccusation, it required an extraordinary effort on the part of the administration and the bill's other supporters to secure its passage by a narrow margin in the House.

Meanwhile, all was far from peaceful in the Senate. Senator Paul Douglas of Illinois made it very clear that he was by no means prepared to embark on a subsidy program even for lower middle income people from which the still more needy families of genuinely low income would be excluded. As the bill emerged from the Senate committee, the income ceiling was once again redefined—this time to say that no one would be eligible whose income exceeded the maximum limits applicable to public housing projects in the same area. Again, there was no floor.

Clearly, the Housing Administrator was in an awkward position. It would be difficult to oppose his own program merely on the ground that it had been modified to make it available to people even more needy than those for whom it had been designed. In the end, he accepted the changes with the best grace possible, and the final bill reported out of conference contained substantially the Senate provisions. (A number of other changes were made in the course of congressional consideration. Some were relatively unimportant, and some highly technical. They are omitted here in the interests of brevity, and of clarity as regards the key issues.)

Even after final acceptance of the conference report—again after a legislative struggle of unusual intensity—the problems of the new program were far from over. By the terms of the

[128] H. Rept. 365, 89th Congress, 1st Session p. 176.

[129] House Committee on Banking and Currency, Committee Print, June 11, 1965.

act, it could not actually begin operations until there was a release of contract authority; and this required action in an appropriation measure. In one of the budget messages which were collectively to become the Second Supplemental Appropriation Act, 1966,[130] the administration requested approval of authority to enter into contracts requiring rent supplement payments up to $30 million per annum (the full amount of the first year's authority carried in the 1965 act). The reception of this request was cool and skeptical, and it was apparent that acceptance of the rent supplement program was far from a settled matter.

It is hazardous to try to read too deeply between the lines, and yet it is quite clear even from what appears on the formal record that emotions and apprehensions were at work, which people were reluctant to spell out in detail in public debate. It is not too speculative to suggest that the rent supplement program aroused deep apprehensions in middle class neighborhoods, especially in the suburbs. Many people feared that—given the flexibility with which private enterprise can operate, and given the stimulus of the profits to be made out of a new housing program backed by highly favorable financial arrangements—private entrepreneurs would move inconspicuously to obtain control of available sites and bring about projects that would introduce undesirable elements into their neighborhoods.

The expression "undesirable elements" is employed with deliberation, and should not be mistaken for a euphemism for race. The characteristics that make one individual or family "undesirable" from the standpoint of another as a neighbor—as distinguished from fellow citizen—vary over an extreme range as among individuals, families, communities, and even neighborhoods. Racial bias can and often does figure strongly in such judgments. There are many other characteristics, however, that may lead to roughly similar reactions. These may include, for example, other kinds of ethnic differences or groupings such as national origin or language identification, religious ties, widely disparate income levels, or simply widely varying cultural backgrounds or life styles.

All these factors were simmering beneath the surface at the time that the Appropriations Committees were considering whether to let the rent supplement program start, or not. In the end, the House committee reduced the initial release of contract authority from the $30 million requested to $12 million, and inserted language effectively restricting rent supplement projects to those that were "part of" a local workable program, or that were undertaken pursuant to "local official approval" of participation in the program.

The language was somewhat awkward, for parliamentary reasons too technical to go into here, but the meaning was clear: The committee had said that—while they were not prepared to go quite as far as requiring the local referendum on each project, which some had proposed—at least no rent supplement project could suddenly blossom in any neighborhood without the local community having been afforded the opportunity to exercise a veto over it.

The Housing and Home Finance Agency (HHFA) dutifully, if not too hopefully, asked the Senate Appropriations Committee to remove this restriction. The Agency argued reasonably enough, that such a control was inappropriate to a program to be carried out by private sponsors and managers, rather than by public bodies. Local land use, zoning, and code controls should be sufficient, the Agency said. The attention of the Senate, however, was not focused on this question, but on the broader question of whether to initiate the program at all. The Senate committee struck the item out of the bill entirely, arguing for reconsideration at a later date in connection with the regular annual budget. The House provision—allowing $12 million and including the restrictive language—was restored on the Senate floor by a vote of 46–45. By adopting the House provision without change, the Senate avoided sending this item to conference—a step that, under the circumstances, would have been fraught with hazard and uncertainty.

Thus, at the extreme end of the runway, by a margin of one vote, the rent supplement program had shakily become airborne. It is reasonable to speculate that, had that vote gone the other way, the program might never have started at all.

The final outcome left no one victorious, or even fully satisfied. The administration, which had started out to achieve a means of redressing the balance of equity by affording some effective assistance to disadvantaged families in the 20 percent gap no man's land, had ended up with a different formula for subsidizing families eligible for low rent public housing. The best available face was put on this result by referring to the new "program" as a "useful supplement" to conventional public housing, though that was not at all what it had started out to be.

[130] Second Supplemental Appropriations Act, 1966, P.L. 89-426.

The builders and mortgage lenders who had begun to do a thriving business under section 221(d)(3) were confronted with a new annual subsidy device, which, only too clearly, the Bureau of the Budget and other fiscal authorities of the executive branch were still determined to use to choke off the steady growth of the former program with all deliberate speed.

The local housing and redevelopment officials, who for more than a generation had pinned their hopes for adequately housing the poor on the low rent public housing program, felt more threatened by the bill as finally enacted than as introduced—and with reason, because there was no income floor built into the program, and because in many ways it was mechanically simpler than the program under the U.S. Housing Act of 1937, even with its various special features such as leasing and turnkey construction.

Finally, those who were apprehensive about a threat to stable, homogeneous, middle-class neighborhoods, or about the possible impacts of such a program on their schools, public facilities, and property taxes, could hardly feel greatly reassured. The Congress had assuaged its own conscience by confining the new form of subsidy to the same general income class as was served by public housing, but by the same token it had increased the probability that the program, to the extent that it became operative, would tend to channel doubtful or undesirable elements into or near their communities. And the veto provision added in the appropriation act was at best uncertain, difficult to organize, and unfamiliar to most local people.

Not surprisingly, everyone was relieved that the battle was over, but the shouts of victory were, to say the least, subdued.

The Programs Under FHA Sections 235 and 236

In 1968, the executive branch made one more try at finding a formula agreeable to Congress which would extend some assistance to families in the middle income range who were unable, on the one hand, to compete effectively in the private market, and who, on the other, were disqualified by statute or regulations from taking advantage of existing programs of housing assistance. This effort resulted in the enactment of the FHA programs under sections 235 and 236, but the final enactments were quite different from what the administration had set out to achieve.

It is of some interest to note that the subsidy technique proposed in the 1968 legislation had its origin to a large extent in a 1967 proposal put forward by a minority Senator—Mr. Percy of Illinois—in a quite different legislative form. Mr. Percy's bill was intended to provide a mechanism for assisting low income families in achieving homeownership. His was not a lonely voice at the time—indeed, all 36 Republican Senators registered themselves as cosponsors of the bill, and several majority members (including Clark, Mondale, and Ribicoff) introduced related proposals.

There were serious technical and administrative problems with the Percy proposal and it was HUD Secretary Weaver who was called upon to oppose it on behalf of the administration. The central points he made were that the special, quasi-governmental nonprofit foundation which was to administer the program was an awkward and ill-defined institution; that the subsidy plan itself was unduly complex and cumbersome; and that the scheme involved tax provisions which were highly technical and difficult to assess in terms of their ultimate effects. In addition, the Secretary sounded a warning which he had voiced publicly more than once in the past: Many low income families lack the experience and background necessary for successful homeownership, and the provisions of the bill did not provide adequately for helping them make the transition from transient renters or roomers to property owners and taxpayers.

The Secretary's criticisms were sufficiently trenchant to assure that the Percy bill, with all its support, could not pass in its original form. Yet there was enough support for the underlying idea that the staff of the Senate Banking and Currency Committee was directed to work with Department staff in an effort to develop a proposal which would embody the basic objectives, and overcome some of the weaknesses in the original plan. The result was a bill accepted and reported by the full committee that utilized FHA mortgage insurance and an interest rate subsidy, and that, in fact, closely resembled the section 235 proposal which followed the year after. However, by this time it was too late in the session for such a major new departure, and the Senate leadership persuaded the sponsors of the bill to let the matter go over until the next session of Congress.

In 1968, the executive branch proposed one of the most comprehensive, complex, and sweeping bills ever written concerning housing and urban development. Included in the bill was a new FHA section 235, closely patterned after the final 1967 version of the bill referred to above, and providing for homeownership by low income families to be achieved through a Federal subsidy covering the difference between what 20 percent of an eligible family's income would cover of the necessary monthly payments on a modest home, and the full payments required to carry the purchase. The proposal included a built-in limit that the family's payment at 20 percent of income must be at least sufficient to carry the cost if the mortgage were written at a 1-percent interest rate.

In the 1968 bill, however, this homeownership proposal was carried a step farther, and was adapted to provide the mechanism of a rental subsidy program offered as a new FHA section 236. This section envisioned a subsidy paid by the Government to the mortgagor on a 236 project in an amount equal to the difference between the economic rent attributable to a unit, and the actual rent received from a tenant paying 25 percent of family income—with a limit fixed by the requirement that the tenant's payment must be enough to meet an economic rent for the unit computed on the basis of a 1-percent interest rate.

The bill provided an elaborate—perhaps even over-elaborate—device for adjusting the subsidy to the actual income of a particular tenant population. For each unit, the owner was required to establish two rentals: A "basic rental charge," representing the rent required to operate the project if it were financed by a mortgage bearing a 1-percent interest rate; and a "fair market rental charge," representing the rent required at the actual interest rate to be paid on the mortgage. Periodically, the Government was to pay to the mortgagee, on behalf of the owner, an amount equal to the difference between these two rent rolls.

The rent paid by each tenant was to be 25 percent of family income, which had to be at least equal to the basic rental charge. Hence, in practice the great majority of tenants would be paying a rental amount falling somewhere between the "basic" rent and the fair market rent. To avoid oversubsidization, therefore, the bill provided that the owner would set aside and rebate to the Secretary all rentals collected in excess of the basic rents. These amounts the Secretary was authorized to deposit into a revolving fund that would be available for future payments.

The bill was silent as to what would happen in the case of vacant units. This became a significant problem when regulations for the program were drafted. Some officials of the Department felt that the owner-sponsor should be permitted to deduct vacancy losses in computing the amount to be rebated to the Secretary, while others felt that this would amount to diverting subsidy funds to support the owner and the insurance fund, rather than the low and moderate income tenants. In the end, the latter view prevailed and the regulations required the project to absorb vacancy losses rather than offset them against the rebate due on account of occupied units.

Perhaps because it had been so badly burned in connection with the rent supplement program, when it had defined the families to be assisted so explicitly as those falling within the 20 percent gap, the Department was vague about the income levels the new program was to serve. The bill merely provided that a participating project owner must ". . . operate the project in accordance with such requirements with respect to tenant eligibility and rents as the Secretary may prescribe." The Secretary merely described the proposal as aimed at "families of low and moderate income"—clearly, a phrase by no means self-defining.

The Secretary's explanatory statement limited itself to observing that:

> The Secretary would establish maximum family income limits for eligibility for admission to this new housing, just as he does now for the 221(d)(3) and 202 programs. These limits, dependent on family size, would be determined on the general basis of the cost, in the area, of providing standard rental or cooperative housing of modest but adequate construction.[131]

This explanation really did not throw too much light on the subject of the income levels expected to benefit from the program.

Upper and lower income limits for rental housing assistance were not specifically stated in the bill, but were provided indirectly by the subsidy formula itself. The upper limit was established by the fact that a family with a high enough income that 25 percent would cover the fair market rental charge could receive no subsidy. Correspondingly, as a lower limit, a family would not be eligible for admission unless 25 percent of its income were at least equal to the "basic" rental charge.

While avoiding any categorical description of the income groups to be served by the new program, Secretary Weaver was quite explicit in

[131] Hearings before Subcommittee on Housing and Urban Affairs, Senate Committee on Banking and Currency, 90th Congress, 1st Session, Mar. 5-20, 1968, p. 73.

saying that it was expected to replace—not supplement—the BMIR program under 221(d)(3) and the program of 3-percent direct loans for housing the elderly and handicapped, under section 202 of the Housing Act of 1959.[132] He also hinted rather broadly that he was at least not adamantly opposed to some more specific identification of or limitation on those to be assisted.

Senator Tower had observed:

Mr. Secretary, in our hearings back last July you made this statement: "In many instances, including some of the bills that are before us now, proposals speak about low-income families and then actually provide a program feasible only for moderate-income families. I have a feeling we ought to distinguish what we are talking about." I agree with that statement.

Now, I personally feel that low income has been merged into moderate income to the detriment of the low-income families, and I feel our interest ought to be concentrated in the low-income family.[133]

There followed a further interchange with the Senator, in which the Secretary's response, while hardly definitive, certainly seems to acknowledge the possibility of alternative approaches:

Senator TOWER. Now, Senator Percy proposed this formula of 70 percent of 221(d)(3), which I think would have the effect of channeling the programing toward the low-income family. This is something that I know that you have complained about, and all of us have been concerned about, is the way this thing tends to surface and gravitate toward the higher income family, and I want to make sure that we get it down toward the low-income family.

Mr. WEAVER. Let me say that the purpose in presenting this as it is now presented, rather than in following the 70 percent, was exactly what is now being done. That is, I wanted to get into the record what was involved, so that a decision would be made in terms of the relative costs and in terms of the relative alternatives which remain between the two methods. The program can work with either method. The only difference from the program's objective is that by having the more liberal upper limits, you have the possibility of getting a greater volume quicker and also of providing relatively small subsidies to those who need less help but who still need some help in order to obtain decent housing. But it does not destroy the program. It limits it. It does have some implications on who participates, as I have indicated, and on volume.[134]

As consideration of the bill progressed, the Congress proved to be still not of a mood to turn the Department loose to work in the general vineyard of "low and moderate income" housing. The House and Senate (The Senate formula followed the 70 percent-of-221(d)(3) approach which Senator Percy had proposed the previous year.) each evolved its own formula for defining eligible income levels, and while they were not the same it was the evident purpose of both approaches to confine the new subsidy program to the lower income families, and to set at least some boundaries to the slippery expression "moderate income." Despite the size of the total bill and the multiplicity of subjects it covered, the accommodation of these formulas proved to be one of the most contentious issues in conference.

After a vast amount of back-stage pulling and hauling, in the course of which it more than once appeared possible that the whole proposal would founder in the complexities that had developed around the subject of interest subsidies to rental housing, a compromise was finally struck. Perhaps the simplest way to summarize the contending points of view and the final outcome is to look to the Statement of the Managers on the conference report which finally emerged. They explained the matter as follows:

Rental and Cooperative Housing

(b) Family income ceiling.—The Senate bill limited eligibility to families with incomes less than 70 percent of section 221(d)(3) below market interest rate levels, except that 20 percent of the funds could be used for families with incomes exceeding that limit. The House amendment limited initial eligibility to families with incomes less than 130 percent of income levels for continued occupancy in the area which can be established pursuant to public housing law.

The conference substitute provides the following income limits: For 80 percent of the funds authorized the income limit is 135 percent of the public housing level in the area for initial occupancy, plus $300 per minor child. For the remaining 20 percent of the funds authorized the income limit is 90 percent of the maximum level established under the below market interest rate program in the area, plus $300 per minor child.

The conference substitute also requires an annual report by the Secretary to the Banking and Currency Committees of the Senate and House on how the subsidy program is operated with respect to the income limits provided in the conference substitute.[135]

If this formula, or combination of formulas, seems bewildering to the reader, it was to prove even more so to the program administrators. Indeed, it may fairly be doubted—without in the least impugning their intentions or good faith—whether anyone actually knows or could determine, within reasonable levels of effort, whether these statutory standards have been exactly adhered to in practice or not.

In any event, the bruised and embattled administration was by now prepared to accept any settlement of this problem that the Congress could agree upon. Thus the bill was enacted, and yet another subsidized housing program for low

[132] Ibid., p. 9.
[133] Ibid., pp. 26-27.
[134] Ibid., p. 28.
[135] H. Rept. 90-175.

income families was launched—this one with some unknown degree of effect upon at least the lower tiers of the income levels hitherto excluded from such assistance.

It must be recalled, of course, that these substantial new subsidy programs—sections 235 and 236—were only parts of a tremendous omnibus bill which also did a great many other things, some of them of a closely related nature. Not only did the act reaffirm the National Housing Goal of 1949, but quantified it to call for the production of 26 million units over a 10-year period, of which 6 million were to be subsidized units for low and moderate income families and individuals. In addition—and again among still other things—the 1968 act:

- Reduced the interest rate (to 1 percent) and increased the authorization for the "experimental" low income homeownership program under section 221(h);
- Increased the authorizations then outstanding for both the rent supplement program and the low rent public housing program;
- Authorized similar interest subsidies in connection with insured loans under the rural housing program;
- Established a National Home Ownership Foundation (which later Congress was to prove unwilling to fund);
- Established a special form of FHA insurance for low income families who ordinarily would be considered inadequate credit risks, together with counselling services for both these families and for tenants of low rent public housing (an activity where the reluctance of the Congress to appropriate proved to be matched only by the reluctance of the Department to get into such a program); and so on.

The very proliferation of gadgetry suggested, and the dire struggle over section 236 confirmed, that after more than 30 years of study, effort, hearings, and legislation the executive branch and the Congress were no closer than when they started to having a clear notion of what they wanted to do about housing, and how they wanted to go about it. Further proof that this was indeed the case was not long in coming.

The Freeze, and What Has Followed

The Housing Act of 1968 was the last great legislative explosion in housing and community development to come out of the Democratic administration that came to an end that year.

When a new Republican administration assumed office, its initial disposition was to apply what it hoped would prove to be improved management techniques to the execution of all the programs it had inherited, and especially to press for expanded production of housing, especially subsidized housing for low and moderate income families. Initially, these efforts met with considerable success. From the fiscal year 1969 to 1972, total housing production increased by about 40 percent, but production of subsidized housing (including by rehabilitation) more than doubled.[136]

That this was a spectacular increase in production, especially of subsidized housing, is beyond question. It is doubtful whether any analytical technique exists which could assess how much of this increase was due to the efforts of the administration; how much to the relatively favorable conditions that then prevailed in the mortgage market, and the relatively abundant availability of mortgage funds; and how much to the natural growth curve characteristic of most major new programs after the inevitable shakedown period which involves the writing and issuance of regulations, the design and distribution of forms and operating procedures, and the necessary period for builders, lenders, and local officals to become familiar with these materials.

When the *Fourth Annual Report on National Housing Goals* was submitted in June 1972, the administration was still reporting with understandable satisfaction on these accomplishments. Nevertheless, a note of doubt was beginning to creep into its discussion of where the Federal Government had led itself, or permitted itself to be led, in the whole housing problem, and what sort of future it ought to envision (see, *Fourth Annual Report,* supra, Chapter IX). By the end of 1972, it was evident that the administration was engaged in an agonizing reappraisal of the whole subject of subsidized housing programs.

In January 1973, the blow fell. The administration announced the abrupt suspension of all subsidized housing programs (and, for good measure, a number of nonhousing subsidy programs, such as open space land grants, water and sewer grants, etc.).

The 1973 Housing Goals Report, retaining its curious mixture of pride in past accomplishment and alarm at the results, explained the thinking behind this drastic measure as follows:

> In 1968, the Congress determined that the [housing] goal could be substantially achieved within the succeeding

[136] *Fifth Annual Report on National Housing Goals,* H. Doc. No. 93-141, Table 1.

decade if 26 million units were constructed or rehabilitated, six million of these for low and moderate income families. On June 30, 1973, the mid-point in the decade was reached and the housing produced in the first five years amounted to 11,936,800 units—an amount in excess of the target set in the Second Report for the first half of the FY 1969–1978 goal decade. (The term "production" in the context of the Housing Goal refers collectively to conventional housing units "started," mobile homes "shipped," and subsidized rehabilitation "begun.")

This extraordinary achievement was made possible by total housing production during the past three fiscal years which reached record high levels—a level in 1973 that was twice the average for the preceding 21 years. In FY 1973—which ended June 30, 1973—total housing production was almost *3.0 million units*—including 2,330,900 housing starts, 615,000 mobile home shipments, and 43,300 subsidized rehabilitated units. [Strictly speaking, these figures are not altogether comparable because the original goal figure of 26 million units did not include mobile homes.]

By mid-point in the goal decade the Federal Government will have aided the construction or rehabilitation of almost 1.8 million units for low and moderate income families, as well as providing subsidy assistance to an additional 218,000 families in existing units not requiring substantial rehabilitation. This represents housing assistance for more families in the last five years than the cumulative total provided during the entire 34-year history of our national housing programs before this Administration took office.

At the same time, however, there has been mounting evidence of basic defects in some of the federal housing assistance programs. To achieve the high levels of subsidized production, financing techniques were devised which in a real sense "mortgage the future" by committing the Federal Government and future generations of taxpayers over possibly as long as the next 40 years to bear costs now estimated for HUD and USDA programs at between $65 billion and $85 billion—even if not a single new unit were to be added in the last half of the goal decade. Additional costs are borne by the taxpayer due to the various tax incentives designed to encourage the construction and rehabilitation of these housing units for low and moderate income families. With regard to the latter category of costs, the Administration has proposed to the Congress revisions in the tax laws to limit the extent to which certain tax losses associated with housing investments can be used to offset unrelated income.

In addition to the concern about the costs, there has been mounting evidence of basic defects in *some* of our housing programs. It has been clear for some time that all too frequently the neediest have not been the primary beneficiaries of *some* of the programs. The programs also do not treat all families equitably since only a modest proportion of the families eligible for subsidies—that is, whose incomes qualify them according to the law to receive housing assistance—actually receive them.

On January 5 of this year new activity under federally subsidized housing programs was temporarily suspended . . . .[137]

The 1974 budget gave the rationale for the administration's abrupt across-the-board holding action in somewhat blunter language:

. . . Among the activities covered by this head [in the Budget] are commitments to provide housing under the homeownership assistance, rental housing assistance, rent supplement, and low-rent public housing programs.

Under these and other subsidy programs the Federal Government has committed itself to long-term housing assistance payments which will cost the Federal taxpayer in the range of $57 billion to $82 billion in direct subsidy payments alone, as well as additional sums for various tax subsidies. These programs have not produced results commensurate with the costs to the taxpayer. Instead, the statutory programs have:

(a) Provided a fortunate few with new housing through subsidies totaling $700 to $3,000 annually, while other families in the same income range pay more for unsubsidized housing that is not new;

(b) Provided windfall profits and tax shelters to intermediaries in the housing and financial sectors;

(c) Created strong pressures for builders, developers, suppliers, and laborers to inflate construction and land costs, causing subsidized housing to cost more than comparable unsubsidized housing; and

(d) Placed families in homes which they cannot afford to maintain, thus severely straining the family budget.

The Administration is evaluating alternative means for enabling families and individuals to afford adequate housing on their own. During this review, the Federal Government will continue to honor statutory and other commitments made under the low-rent public housing, rent supplements, homeownership assistance, and rental housing assistance programs. However, no new commitments under those programs will be made.[138]

There followed an extensive series of studies within the executive branch, in the course of which virtually all housing programs of the Federal Government were reviewed from the point of view of the management, economic, financial, and social problems they presented. The scope and content of those studies, however, are beyond the purview of the present review.

In a special message on housing sent to the Congress on September 19, 1973, the President, in search of what he called a "better approach" to Federally subsidized housing, suggested what he characterized as a "new approach." It was, in fact, one of the proposals and counterproposals which had led finally to the enactment of the original 1937 act—namely, cash allowances for housing for the poor. (It will be recalled that it was Mr. Pederson of the New York Council of Real Estate Associations who told the Senate committee in 1936, "The root of the evil is the people do not earn enough to live in what the proponents of this bill call decent housing accommodations.") The relevant portion of the message argued as follows:

Leaders of all political persuasions and from all levels of government have given a great deal of thought in recent years to the problem of low-income housing. Many of them agree that the Federally-subsidized housing approach has

[137] Ibid., pp. 2-3.

[138] *Budget of the United States for the Fiscal Year 1974*, p. 475.

failed. And many of them also agree on the reasons for that failure.

The main flaw they point to in the old approach is its underlying assumption that the basic problem of the poor is a lack of housing rather than a lack of income. Instead of treating the root cause of the problem—the inability to pay for housing—the Government has been attacking the symptom. We have been helping the builders directly and the poor only indirectly, rather than providing assistance directly to low income families.

In place of this old approach, many people have suggested a new approach—direct cash assistance. Under this approach, instead of providing a poor family with a place to live, the Federal Government would provide qualified recipients with an appropriate housing payment and would then let them choose their own homes on the private market. The payment would be carefully scaled to make up the difference between what a family could afford on its own for housing and the cost of safe and sanitary housing in that geographic area. This plan would give the poor the freedom and responsibility to make their own choices about housing—and it would eventually get the Federal Government out of the housing business.

Not surprisingly, our recent housing study indicates what others have been saying: of the policy alternatives available, the most promising way to achieve decent housing for all of our families at an acceptable cost appears to be direct cash assistance.

Our best information to date indicates that direct cash assistance will in the long run be the most equitable, least expensive approach to achieving our goal of a decent home for all Americans—a goal I am committed to meeting.

A general approach to cash allowances, however, the President indicated, would require more time for study and refinement of an approach.

For immediate action in connection with subsidized housing, he made only two proposals: First, a continued and strengthened experimental program of "housing allowances" (i.e., a field test of variations of the cash allowance device); and second, an expanded program under section 23 of the U.S. Housing Act of 1937, including an effort to expand its use to new as well as existing housing. This program, he said, could ". . . be administered in a way which carries out some of the principles of direct cash assistance."

Since these two programs, themselves hitherto rather limited in scope and size, are all that now remains of the once imposing structure of federally subsidized housing programs, a word about each of them is in order.

Experimental Housing Allowance Program

Apart from a limited public housing effort under section 23, the major remaining thrust of the present administration in the field of low income housing is represented by the Experimental Housing Allowance Program.

As the President indicated in his September 19 message, some work had already been initiated pursuant to section 504 of the Housing Act of 1970 which authorized housing allowance experiments involving over 18,000 families and costing over $150 million. (Also, two local Model Cities agencies (in Kansas City, Mo. and Wilmington, Del.) began programs in late 1970 to demonstrate the potential of housing allowances as a means of providing decent housing.) A broadening of that authority was requested. It was stated that the data emerging from those experiments and further expected steps should furnish the information needed to make a final decision on this approach late in 1974 or early in 1975.

Prior to the President's message cited above, the Department of Housing and Urban Development had submitted in May 1973 the *First Annual Report of the Experimental Housing Allowance Program,* which analyzed the several aspects of housing allowances, the background of the experimental program, and the experiments under way to answer the questions and solve the problems arising in the formulation of a national program.

The report made clear that the concept of housing allowances is not a new one, having been considered and proposed by many as an alternative to public housing since before the enactment of the Housing Act of 1937. In fact, it was rejected by the 1953 President's Advisory Committee on Government Housing Policies and Programs. Opposition to it has generally been based on the belief it would degrade the recipients; that it would not add to the housing supply, especially for needy groups such as elderly or large families; and that there is no possible way of limiting the scale of the program—that is, all the eligibles in the nation would have to receive benefits, which would be too costly.

The report outlined the concept to be tested. For that purpose, a housing allowance was considered to be a series of regular periodic payments made directly to an eligible family (or individual) unable to afford a decent home in a suitable living environment. Factors to be used in determining the amount of the allowance were family size and income, and the cost of a standard, existing house or apartment located in a modest neighborhood. The allowance had to be used to pay rent or homeownership payments. By paying allowances directly to the family, it was to be given a choice in selecting the house or apartment it wished, and to have the purchasing power to enter the market for decent housing. Few restrictions would be placed on a family's choice. One possible restriction to be evaluated is whether the unit chose should meet basic minimum housing standards.

The housing allowance program would rely on the market supply of existing housing. It would be expected to provide incentives for rehabilitation and maintenance of the existing housing stock, as those receiving allowances increase the market demand for standard housing units.

Three Sets of Experiments: The basic questions raised by housing allowances are being tested in three sets of experiments, each designed to get at a principal cluster of issues:

- How do families use their allowances? (Demand Experiment)
- How does the housing market respond to allowances? (Supply Experiment)
- How can allowances be administered? (Administrative Agency Experiment)

These are being conducted with the assistance of private firms and institutions.

The Demand Experiment: The objective of the demand experiment is to examine how households use their housing allowances.

This experiment is being carried out over a 3-year period in 2 metropolitan areas having over 500,000 population each (Pittsburgh, Pa. and Phoenix, Ariz.). This minimum size is necessary to assure that the families receiving allowances are relatively few in order to avoid the increased housing demand they represent from having a significant effect on the housing market. About 1,600 families are involved in the Pittsburgh area.

Under this demand experiment, the principal questions of interest are: The participation rates of eligible households; changes in their expenditures for housing; the quality of housing they obtain; the location of the housing they select; the satisfaction of the households with their choices; and the housing allowance costs incurred by the Government.

The experiment is also attempting to evaluate the effect of different forms of housing allowances on the above types of household choices. Thus, two kinds of formulas for making allowances are being tested. One is a "housing gap" formula, where the allowance is made equal to the difference between the fair market rent for a modest existing house or apartment in the area (appropriate to the size of the family) and a specified percentage of family income. The second formula is based on "percentage of rent," and the Government pays some predetermined fraction of the family's actual rent expenditure up to a specific maximum amount.

Another set of alternatives in the program being tested is the attainment of minimum standard housing through (a) an inspection of each unit to determine whether it meets defined standards, or (b) a minimum rent expenditure requirement, which assumes a close correlation between rent and the quality of housing.

To help determine national characteristics of the program, such as total cost, data on family incomes and prices are being obtained for specific groups of families.

After eligible families are identified through a survey process, an assignment process is used to obtain similar groupings of families to be offered each of the allowance plans. Each family accepting receives counseling assistance and will be interviewed semiannually or annually during the duration of the experiment. At the end of the experiment the Government will make its best effort to provide regular program subsidies to the families to minimize disruption.

The Supply Experiment: This experiment is designed to analyze housing market response to a substantial addition of low income housing demand likely to be caused by an allowance program on a national scale.

The supply experiment is being conducted in two contrasting medium-sized metropolitan areas of approximately 200,000 to 250,000 population (Green Bay, Wisc. and Saginaw, Mich.), each selected to represent an important class of metropolitan areas in the nation. One has a rapidly growing central city and a low incidence of minorities. The other is a metropolitan area with a slower growing central city and a representative minority population. The experiment involves 4,000 to 8,000 families in each area.

In each area, HUD is making experimental housing allowances available to low income residents. Eligibility rules and the allowance formula are the same for both areas. Data relating to specific households and structures are being collected to answer four categories of research questions:

1. How will owners and developers of rental housing respond to attempts of allowance recipients to increase their housing consumption? What mix of price increases and housing improvements will result? Will the increased demand be absorbed by price increases or by quantity increases?

2. How will mortgage lenders, real estate brokers, and building service, repair, and remod-

eling contractors respond to an allowance program? Will they help or resist attempts by allowance recipients to obtain better housing or improve their properties?

3. In seeking better housing, will many allowance recipients relocate within the metropolitan area and, if so, what types of neighborhoods will they seek and succeed in entering?

4. How will nonrecipients of housing allowances—particularly those with incomes just above the eligibility limit—be affected by, and respond to, the program? Will any resulting price increases affect them?

Data for analyzing the above questions will be obtained by monitoring the housing markets for each area for 5 years. That will include annual formal surveys covering a sample of residential structures in each area; a study of administrative records on the characteristics and housing choices of all those enrolled in the allowance program; and a regular flow of information from a resident observer.

The Administrative Agency Experiment: This experiment is designed to determine how best to administer an allowance program, and to analyze the effectiveness of various types of local agency in doing so.

The Administrative Agency Experiment is being conducted through eight agencies of various types (two local housing authorities, two metropolitan area county government agencies, two State community development agencies, and two welfare agencies). The eight agencies are located throughout the nation in cities, towns, counties, and rural areas of different sizes (75,000 to 500,000). The number of allowance recipients in each area (from 500 to 900) is considered large enough to provide a realistic basis for evaluating administrative organization and performance of functions, but small enough, relative to the local market area, to avoid rent increases from the added housing demand created by the allowances.

The principal evaluation concerns of the experiment are the efficiency and effectiveness of the local agencies and their methods in administering housing allowances. Accordingly, they are given broad latitude in designing the administrative features of their programs, subject only to what program definitions are necessary to assist in formulating a national approach. For example, each agency has to use the "housing gap" formula discussed above.

This experiment is designed to focus on four major concerns:

1. The administrative costs of the programs. How are these costs best allocated to maximize program efficiency and effectiveness?

2. The scope of services and methods of delivering such a program. What is the appropriate mix of administrative and organizational arrangements and services for operating the program that provides the most administrative simplicity, efficiency, free housing choice, and privacy for the recipient?

3. The capability of such a program to treat people in equal need equally. How equitable is a housing allowance program?

4. The amount of control over such a program that is necessary to assure funds are used for the purpose intended. How, and to what extent, can potential diversion of allowance funds by beneficiaries, landlords, market intermediaries, and administrators be minimized?

A principal question toward which all three sets of experiments are directed is the overall cost of various housing allowance programs, as their feasibility is dependent upon a realistic Federal expenditure.

Conceivably a program could be administered on a first come, first served or other priority-setting basis. However, a universal entitlement of all income-eligible families would in all probability follow the pattern of most of the nation's income transfer programs aimed at providing a minimum level of income or services (such as welfare payments, food stamps, and Medicaid). Good data on the costs of such a housing allowance program do not exist now because of the tremendous variety of possible factors and constraints in the program, and the uncertainty as to the willingness of eligible families to participate, and the income and other characteristics and desires of those who will participate.

The Section 23 Leased Housing Program

Section 23 was originally added to the U.S. Housing Act of 1937 by the Housing Act of 1961 (Public Law 87–70), in order to provide an alternative means of housing low income families through the use of vacancies in existing structures in a particular community. In essence, the local housing authority was authorized to lease units in existing structures and to arrange for their occupancy by eligible tenants from the public housing waiting lists. The local authority would select tenants; fix the amount of rent the tenants would pay; agree upon a total rent based on comparable accommodations in the area; and could receive annual contributions to make up the difference between the total rental charge and the rent paid by the tenant, not to exceed the rate of contributions on a comparable new public housing unit in the area.

After the freeze on subsidized housing programs generally, the administration turned to section 23, not only as a means for continuing to lease existing units, but also as a vehicle for encouraging the construction of new housing for low and moderate income families. Precisely why this program—which had never figured largely in the total low and moderate income production picture—was selected to be rescued from oblivion is not altogether clear. Perhaps the fact that it had originally been sponsored by a senior Republican member of the Housing Subcommittee in the House, Mr. Widnall, had some bearing. Certainly, the section 23 device had regularly enjoyed more Republican support than most of the other subsidy devices.

Probably, however, the main reason for the decision was the suggestion included in the President's September 19 message that the section 23 program could be ". . . administered in a way which carries out some of the principles of cash assistance."

In its 1974 legislative proposals (see, H.R. 10688, 93rd Congress, 1st Session), the Department proposed certain modifications designed to make section 23 an even more strictly private enterprise program than before, and presumably to encourage its use in the provision of new housing as well as the leasing of housing in existing structures. Among these changes were the following:

1. With respect to leasing units in newly built structures, the Secretary was authorized to dispense with the intermediary role of the local housing authority and deal directly with the owner. The bill provided that assistance payments could not be made with respect to more than 20 percent of the units in a single structure, ". . . except as otherwise provided by the Secretary."

2. The bill also provided that such units should be ineligible, not only for any other form of assistance under the act, but also for FHA mortgage insurance.

Tenants were to be selected by the owner who would also be responsible for management. Thus, the "revised" program envisioned would be purely a private enterprise affair, save for the role of the Government in leasing some number of units and agreeing to pay stipulated amounts of subsidy to make them available to low and moderate income families.

The prospects for reception of these proposals both by the Congress and the market were, to say the least, uncertain. A limit of 20 percent on the number of units in a project that could be assisted appeared sufficient to create a degree of uncertainty for a potential sponsor, even coupled with the Secretary's authority (but not duty) to waive this limit. And it appeared far from assured that financing would be readily available in the private market for these projects in the absence of FHA mortgage insurance. As a matter of fact, without any special public statement on the subject, the Department has abandoned this feature of its proposal and is no longer urging its inclusion in the legislation.

In any event, in its 1974 and 1975 budget programs the Department placed heavy reliance on its only remaining active subsidy program. It projected a total of more than 400,000 units of new and existing housing to be provided under the revised section 23—a number vastly in excess of any previous production experience (about 5–10,000 units per year), and one which few informed outside observers felt was realistically within the realm of the achievable.

A Brief Review of Some Unsettled Problems

To those who have followed thus far the development of executive and legislative attitudes toward subsidizing housing over the years since the early 1930's, it will be evident that certain major problems have surfaced over and over again as recurring themes. Time and again they have influenced, sometimes decisively, the actions that were taken, or that the Executive or the Congress declined to take.

While they cover a wide range of matters, these persistent problems appear to have one thing in common: namely, that they never seem to get settled, regardless of how often they are argued over and compromised in one temporary format or another. It may be as well, therefore, to briefly review a few of the more important such questions because there seems to be no present reason to believe that they will not arise to plague the decision-making process in the future as they have in the past.

The Problem of the Budget

It is a matter of opinion whether the enormous impact of Federal budget considerations on the formulation of public policy rests on valid reasons, or on factors that are mainly psychological, emotional, or political. That the impact is a reality no informed person can doubt.

To understand the kinds of issues that arise in this area, it is important to bear in mind that the budget still retains much of its original character as an annual cash flow statement—reporting on receipts from and payments to the public for the previous year, and estimating those for the current and following years. No distinction is recognized beween out-of-pocket expenses for current operations and outlays which are in the nature of recoverable investments, or still others which, like research and development, may lead to future increase in wealth or value.

The budget is neither designed for nor well suited to the purpose of disclosing costs, however that slippery word may be defined. Thus it is not only possible, but it rather frequently occurs, that a less efficient or more costly means of accomplishing a given end may have a "favorable" budgetary effect, or, conversely, a more efficient or less costly approach may be rejected because of its ostensibly unfavorable budget effect.

An example may be useful to clarify the above. The Housing Act of 1959 authorized a program of long term loans at below-market interest rates (originally a formula rate, but in 1965 fixed at 3 percent) to certain eligible sponsors to assist in meeting the housing needs of the elderly and handicapped. In the opinion, at least of the participants in and beneficiaries of the program, it was highly successful. It made for large expenditure figures in the budget, however, inasmuch as the entire amount of the loan disbursement appears as an expenditure in the year in which it is made. In budget parlance, amounts actually paid out (checks written) during a fiscal year are called "expenditures"; amounts actually taken in as a result of operations are "receipts"; and net of these two figures is called "outlays" and may carry either a (+) or (−) sign, the latter denoting net budgetary receipts.

The FHA section 236 subsidized rental housing program for low and moderate income levels was established in 1968. Under this approach, the Government's expense takes the form of annual subsidy payments throughout the life of the mortgage. While loans for housing the elderly and handicapped were fully repayable with interest (although at a rate below that prevailing in the private market at the time the loan was made), the annual subsidies are not, of course. Nevertheless, it was decided that future projects for the elderly and handicapped would be financed under the 236 method of subsidy, even though it appears to have been undisputed that the eventual cost of this method to the Government would be appreciably greater.

The nature of the point involved was not wholly lost on the Committees when the section 235 and 236 programs were under consideration in 1968. Secretary Weaver observed in this connection:

> Both programs, by relying on the private market for mortgage financing, should be able to obtain more regular funding because they would not be dependent on the vagaries of the Federal budget.[139]

Commenting on this aspect of the bill, the Minority Views in the House Committee report remarked:

> Undeniably the bill is big.
>
> Parts of it are also bad.
>
> Too many of our existing housing programs are the result of budgetary gimickry. In order to reduce the impact of a program on the present administration's budget, the costs are spread over as many as 40 years. This may be good public relations and good politics but it is bad economics. It increases substantially the financing costs of housing obtained under the program. It misleads the public as to the true cost of the program with only one-fortieth of the cost showing in the first year, but thirty-nine fortieths hidden in the future—much worse than a hidden iceberg and potentially more dangerous to our future fiscal stability.[140]

The chief, if not sole, advantage of the annual subsidy method is indeed that the immediate budget effect of the program is almost entirely avoided, while its effects in any single future year are also minimized, at least for the near future. Thus, in the first year, the large capital expenditure (represented by disbursement of the loan) disappears and is replaced by a figure representing only the first year's subsidy—a very modest figure in any event, and frequently zero, since the project may be barely commencing operations. Similarly, any future budget will show the subsidy payments only for that year, and nothing need be said either about payments in the past or those remaining for future years, or about the missing receipts from repayments and

[139] Hearings before the Subcommittee on Housing and Urban Affairs, Senate Banking and Currency Committee, 1968, supra, p. 9.

[140] H. Rept. 1585, 90th Congress, 2nd Session, p. 338.

interest which would have been realized from a loan, had one been made.

If this approach seems shortsighted and even improvident, it must be remembered that in the never-ending struggle between those who think the budget (or some item in it) too high and those who find it too low, the immediate budget advantage is almost invariably sought. It is easy to let future budget directors and Congresses worry about future years. Both the executive branch and the Congress play this game, although the technicians in the executive branch generally understand its intricacies better, and have the additional advantage of having designed the budget in the first place.

Because the problems of the budgetary treatment of various kinds of transactions and their resulting effects on the budget surplus or deficit are themselves complex, technical, and not widely understood, the following table has been provided to illustrate how the budget treats the various types of housing subsidy.

Effects of Budget Considerations on Policy —Examples

The following are a few examples—by no means an exhaustive list—of major decisions of policy affecting housing subsidy programs which have been largely determined by budget considerations:

Public Housing Annual Contributions v. Capital Grants: The U.S. Housing Act of 1937, as enacted, authorized (and still does) initial capital grants, as an alternative to annual contributions, to achieve low rents. Though vastly simpler and less costly administratively, and almost certainly equally effective and cheaper over the life of the program, this authority has never been used. As noted in an earlier chapter, the sponsors of the measure apparently never seriously supposed that it would be. The objection, of course, is that the construction of any substantial number of units by this method would involve very large initial appropriations and expenditures.

Budgetary Effects of Various Type of Housing Subsidy

(1) Type of Subsidy	(2) Budget Expenditure Recognized	(3) Budget Receipt Recognized	(4) Timing of Budget Effect
Annual grants or payments	Amount paid in year	None	Spread over period of contract or program
Operating subsidies	Amount paid in year	None	In year, when paid
Initial capital grants	Full amount when paid	None	Immediate on payment
Direct loans	Amount of loan disbursed in year	Amortization and interest received in year	Immediate on payment as to outlays; receipts spread over term of loan
Guaranteed loans	Payments under guarantee, in year made	Guarantee fees in year in which received; realization of guarantors' rights, if any	Indeterminate
Mortgage insurance	Claims paid in years; operating expenses; costs of acquiring, managing, rehabilitating and disposing of properties, securing defaulted loans; interest on debentures and other borrowings	Fees and premiums received in year; rents and revenues from acquired properties; amortization and interest on mortgages held, proceeds of properties and mortgages sold	Net of (2) and (3) in each year
Tax exemption	None	None	None recognized
Mortgage purchases	Operating expenses including payments for points absorbed plus cost of mortgages bought	Operating receipts plus proceeds of mortgages sold	Net of (2) and (3) in each year

Public Housing, Private Financing: In the early years, public housing projects were initially financed by means of direct Federal loans. The long term (so-called "permanent") financing, however, has from the inception been financed (largely, and more recently, entirely) by local housing authority tax-exempt obligations, sold in the private market on the security of a pledge of the guaranteed payment of Federal annual contributions as needed in sufficient amounts to assure their repayment. For all but the initial period, construction (also called "temporary") financing has been similarly accomplished in the private market, on the basis of shorter term notes carrying the same benefits.

There has been remarkably widespread agreement that, whatever the effects of the public housing program in other respects, this method of financing has been an outstanding success. It is difficult to find any other basis for this judgment than the fact that it utilized "private" rather than "public" funds, and that it has kept the very large amounts required for the development of these projects from being visible in the Federal budget. (Inasmuch as Treasury bills, notes, and bonds are also sold in the private markets to raise funds for the Government's requirements, this distinction may appear to be more mystical than substantive. It becomes all the more tenuous when it is recalled that in 1961 the guarantee of annual contributions was broadened to a guarantee of the local authority obligations, and declared to be incontestable in the hands of the bondholders. Thus, with respect to the real debt obligation and the repayment of the bonds, the Treasury, to all intents and purposes, is the borrower and debtor, and the local authority is little more than a fiscal agent (section 302(b), Public Law 70, 87th Congress).)

Certainly the guaranteed tax-exempt method of financing is enormously expensive, even though the low rates of interest made possible by it create an appearance of savings during construction. It is difficult to get precise statistics on who holds (and has held) this type of debt. However, it is obvious enough that tax-exempt income has its greatest value to taxpayers in the higher income and tax brackets. Giving due weight to this factor, almost any reasonable set of assumptions one may make will lead to the conclusion that the cost to the Government of this method of financing over the life of the program has greatly exceeded—and will continue to exceed—the total amount of all annual contributions which have been or will be paid to achieve and maintain low rents.

Below-Market Mortgages for Middle Income Housing—Section 221(d)(3): In 1961, as described earlier in this account, the Congress authorized a new program to assist middle income families by insuring mortgages bearing interest rates well below those available in the private market (originally at a rate based on a Government obligation yield formula, but later—in 1965—pegged at a flat 3 percent). This resulted in reduced debt service charges for projects so financed, and thus permitted lower rentals.

The problem, paradoxically, resulted from the fact that the program was successful. Since all these mortgages, when completed and insured, were promptly bought by FNMA (now the Government National Mortgage Association (GNMA)) under the special assistance functions (without which arrangement the private mortgagees would not have originated them in the first place), the below-market program soon began to show large budget expenditures for mortgage purchases. Accordingly, in 1968, when the annual interest rate subsidy approach was authorized under FHA section 236, the below-market program under (d)(3) was effectively superseded and soon terminated.

This was not, however, a simple case of exchanging one set of subsidy mechanics for another, for two reasons. In the first place, the 221(d)(3) machinery had been fully worked out in the marketplace by then, and it was well understood by sponsors, builders, and mortgage lenders. By contrast, section 236 was entirely new and had to go through a long development and shakedown period. Second, and even more important, section 236 was addressed to quite a different income spectrum, and a high percentage of the families who could benefit under the below-market method were ineligible under the new plan. Thus, in order to achieve an immediate budgetary convenience, the Government gave up not only an established and successful program, but its only effective tool for assisting a range of families with incomes lying between those served by subsidized programs for the low income group and those effectively served in the private market.

Conversion of Other Direct Loans to Annual Grants or Subsidy Payments: It has already been pointed out that the program of direct loans to assist in providing housing for the elderly and handicapped was dropped after the enactment of FHA section 236, in favor of the system of annual subsidy payments provided for in that section.

A similar fate befell the college housing loan program, which was instituted on the initiative of Congress in 1950 to help meet the acute shortage of student accommodations at colleges and universities. Originally, such projects were financed with direct Federal loans at a favorable interest rate (first a formula rate, but later pegged at 3 percent), secured by serial bonds maturing over a long period, most frequently 40 years. The program was strikingly successful and highly popular—and, by the same token, soon began to generate large expenditures for the purchase of bonds. Accordingly, in 1968, Congress was asked to and did provide authority for an alternative approach, in the form of an annual interest rate grant to pay the difference between the actual rates carried by the bonds when sold in the private market and the program rate of 3 percent. This was almost certainly a more costly way of achieving the same result, but it had the budgetary advantage of greatly shrinking immediate budgetary impact.

When the annual grant authority became available, the use of the direct loan method was virtually abandoned. The college housing program has since been terminated entirely, but this action was justified on policy grounds related to aid to higher education, rather than budget considerations.

The history of the rural housing program follows the same pattern. Launched in 1949 as a direct loan program, it was converted in 1965 to an "insured" loan system—a complex and indirect system for using annual appropriations to compensate for the cost of funds raised in the private market. That this is an expensive way of doing business is suggested by comparing the earned surplus of about $250 million, which the smaller program of direct loans to veterans has built up over the period of its operations, with the annual appropriations which are now made to restore losses in the Rural Housing Insurance Fund. There was no premium or similar charge in this program. The surplus results from the fact that funds provided by the Treasury during a period when Government borrowing rates were low, were not only loaned but later repaid and reloaned at substantially higher rates. The appropriation requested for this purpose in the 1975 budget is almost $125 million.

The GNMA Tandem Plans: Such novel forms of mortgage insurance as the subsidized programs under sections 235 and 236 would seem to fit neatly the original purpose of the GNMA special assistance functions—to provide support for mortgage lending, pending the establishment of general market acceptance of these investments. Such special assistance support has indeed been provided, but it has been largely under the GNMA-FNMA tandem arrangement, in which GNMA (in effect) simultaneously buys the mortgage at one price and resells it to FNMA at a lower price. The advantage is that the full price paid for the mortgage never appears as a budget expenditure.

The disadvantage, once again, is the costly nature of the operation. Prior to the development of the tandem device, the special assistance fund had built up a substantial earned surplus or reserve. The 1975 budget, after applying the entire reserve to losses sustained under the tandem operation, requests an appropriation to the fund of some $279 million for the restoration of remaining losses. Further such appropriations are anticipated in future years.

The Budget as a Program Constraint

Apart from their influence on choices as to basic policy and method in subsidized housing programs, budget considerations have also exercised a major restraining impact on program volume and thus on the rate of delivery of such assistance to the families intended to be benefited by the programs.

It can be stated as a simple rule of thumb that so long as any of these programs had a substantial and immediate impact on the Federal budget, it was kept under close budget restrictions which were related primarily to overall budget policy rather than to housing objectives as such. It is unnecessary to review the details of the various programs here, but this general rule in operation was clearly visible in the rapid rise in both authorizations requested for, and production of, subsidized housing in the years immediately following the changes by which their budget impacts were either effectively eliminated or greatly reduced or deferred.

Finally, it should be observed that these changes probably have not ended budgetary restraint but postponed it. Now that housing subsidy costs for programs administered by HUD have been consolidated into a single annual appropriation, which in the 1975 budget has reached a level of $2,425 million (with 30-odd years left to go on commitments already undertaken), there is widespread concern about the long term as well as in the immediate future.

The Budget and the Problem of Equity

Budgetary constraints do not necessarily create, but certainly sharpen, the difficult questions of equity that arise when programs directed at national needs are carried out only on a limited scale. Briefly stated, the problem is that a relatively small and more or less randomly selected sample of the eligible individuals and families receive the full benefits of the program, while a much larger number of equally eligible people receive nothing. The nature of the difficulty is obvious, and hardly requires illustration.

Problem of the Public Sector v. the Private Sector

It is a very prevalent notion in our culture that the organization of production and distribution with principal reliance on private enterprise (not infrequently itself referred to as "the American system," although it is not at all peculiar to this country) is in some way inseparably related to the American system of government. This idea has very little specific foundation in the Constitution, which contents itself with such matters as barring the impairment of contracts and protecting property from expropriation without due process of law and just compensation. Nevertheless, it is so deeply rooted in our national attitudes as to have become a sort of philosophical principle, which proposes that government should not undertake any activity that competes with, or threatens, or might threaten or inhibit private enterprise, except in case of extreme public urgency, as in time of war.

Every departure from this principle—whether with regard to the manufacture and distribution of electric power, the regulation of the securities markets and trade practices, the imposition of taxes on incomes of individuals and corporations, or the distribution of surplus agricultural products for school lunches—has met with the most strenuous and sometimes passionate opposition. A cultural conviction is a political force. The matter of housing subsidies has been no exception.

As noted at the beginning of this study, at its inception in the PWA housing program of the mid-1930's, federally subsidized housing was entirely in the public sector—that is, with public planning, design, financing, construction, ownership, management, and subsidy. As the years passed, the Congress has been responsive at various times and in various ways to continuing pressure to establish and then to enlarge a role for private enterprise, and correspondingly to shrink the role of government. At the other end of the spectrum lies the proposed section 23 leasing approach with private planning, design, and construction, private ownership, and private management—leaving to the public sector only the provision of the subsidy and perhaps a modicum of supervision to assure financial integrity and adherence to the statutory purpose.

A number of intermediate combinations can be found that may be conveniently arranged according to the degree in which these essential functions have shifted from public to private handling:

1. All basic functions public, except for financing in the private market (on the security of an unconditional Federal guarantee) of the obligations, plus tax exemption—as in the conventional low rent public housing program under the U.S. Housing Act of 1937.

2. Most basic functions public, but with private design, construction, and financing—as in turnkey public housing (new construction).

3. Private design, financing, construction, and ownership—as in the original section 23 public housing leasing program.

4. Private design, financing, construction, ownership, and management—as in the rent supplement program.

It should be noted that none of these transfers from public to private activity has been wholly free from controversy. Thus:

- Private financing of public housing has been praised as using private capital rather than "taxpayers' funds"; it has sometimes been criticized as being cumbersome, poorly managed, and an unwarranted tax advantage for the wealthy.
- Private design and construction, as in the turnkey approach, have been praised as contributing to innovation, efficiency, and economy; on the other hand, this method has been objected to as affording excessive opportunities for collusion, hidden costs, and shoddy construction.
- Use of the FHA as the conduit or mechanism for actual delivery of a public subsidy through private channels—has been praised for administrative simplicity and avoidanne of duplication and overlapping of government activities; but on the other side, it has been bitterly objected to as a distortion of what some consider to be FHA's "basic mission" of insuring economically sound unsubsidized loans in the private

market. It has been argued further that the movement of subsidy funds through private hands is an invitation to fraud and misuse.

It seems fair to conclude that after all the debate, controversy, and compromise, there still exists no firm concept supported by a general consensus as to what respective roles the private and public sectors can best serve, or ought to serve, in connection with subsidized housing. On any new proposal, the same issues are almost certain to be raised and contended over again, as zealously as though they had not been thrashed out a dozen times before.

The Problem of Appropriate Government Levels

Just as there have been many shifts of concept concerning what are the appropriate roles respectively of the public and private sectors in subsidized housing, so has there been uncertainty as to the appropriate distribution of public functions among the various levels of government—Federal, State and local.

It is well to recall that many of the social purpose public programs which were started during the depression years—subsidized housing among them—were also started at a time when it was a widely accepted view that local units of government were, by and large, weak and inefficient, venal and often corrupt, and insensitive to local needs not backed by concentrated economic or political power. State legislatures were considered in many cases to be dominated by conservative rural constituencies, and to be indifferent to the problems of the cities and urban areas. Moreover, it was felt that the increasing mobility of the population—combined with these weaknesses of local government—had transformed many once local problems—such as unemployment, bad housing, poverty, etc.—into national problems. From such considerations it was deduced that if any effective attack were to be made on these national ills, it was essential that the Federal Government take the responsibility and the initiative.

It was in this context that, as noted earlier, the first major low rent housing effort was launched by PWA as a purely Federal enterprise, until terminated as a result of adverse court decisions and other problems. It was in this context also that the broader program under the U.S. Housing Act of 1937 was initiated, even though it was to operate through local public agencies.

The local authority device was generally recommended and adopted as the eligible local agency, in large part because—as an autonomous public corporation created under State law—it could at that time borrow money more conveniently without regard to local debt limitations than other available instrumentalities. But there were also considerations related to the prevailing view of the role of local government. Thus, it was thought that an independent local authority would largely serve to immunize the public housing program from political interference by the mayor and city council. Similarly, since it would operate independently of the State government (except for necessary enabling legislation), it would be relatively free from harassment or interference by the Governor, the State legislature, and the various departments of State government.

Much has changed in the years that followed. State and local governments have greatly expanded, not only in functions but in staff. Professional and technical expertise, once rare, is now widely available at these levels. Many States have initiated housing and urban development programs of their own. Constitutional requirements as defined in Supreme Court decisions relating to representation in State legislatures have done much to modify their rural bias and open them up to consideration of urban problems.

At the same time, there has emerged a growing apprehension over the concentration of functions and power at the Federal level. Especially under the present Administration, there has emerged a philosophy almost the reverse of that under which these programs started—that it is the Federal Government that is remote from local problems, inclined to be dictatorial, inefficient, and bogged down in red tape; that it is local government that is on the scene, and sensitive and responsive to local needs.

Hence there has grown up a major effort to disentangle the Federal Government from as many decisionmaking and operating matters as possible, and to return these functions to State governments and to elected officials at the community level, through revenue sharing and restructuring of the lines of decision and the location of final authority. It is perhaps a mild irony that almost precisely the opposite philosophy in 1937 produced, in the local housing authorities, the most experienced and knowledgeable local agencies available to give effect to this new approach in the area of federally assisted housing.

Problem of Identifying the Poor

It is a remarkable fact that the Federal Government's commitment to housing subsidies for low income families was undertaken and carried on for many years without any explicit answer being given to what would appear to be the obvious first question—namely, what is a "low" income as distinguished from some other degree or measure of income?

This problem was first confronted in the original PWA program, even before the U.S. Housing Act of 1937. Lacking a cash subsidy, PWA computed what might be called an economic rent, based on a detailed computation of replacement cost, derived by depreciating all the major elements of a project over their assumed useful lives. Because PWA could not afford to house tenants who could not pay the resulting rents, and because it seemed poor public relations to house those who could pay more, admissions were confined to families whose incomes were closely related to that rent-paying capability, assuming the use of 20 percent of family income for that purpose.

In the later low rent public housing program, this problem was approached by way of establishing a negative proposition: the eligible poor were first said to be those in the "lowest income" group. Because this clearly did not mean very much, they were later defined as those who could not afford housing except at rents 20 percent below those at which standard private housing was available. In other words, the poor were defined as being those of the poor who were demonstrably poorer than others of the poor. This definition was not only less than satisfactory but also manifestly unfair. Nevertheless, it remains in the law to this day.

Various efforts were made in later years to clarify these concepts, but with no great success. There was some attempt to evolve a three-part classification: Families (or individuals) of low income, who should be provided for through public housing; families of middle income, for whom some other and lesser type of Federal support might be justified; and families of "higher" income, who presumably could fend adequately for themselves in the market.

The term "middle" income was fairly quickly abandoned, in part because no one could answer the question, "middle of what?" and partly because, in any event, most people thought of middle income families as being reasonably well off, and not properly dependent on Government assistance in meeting their ordinary needs. When the below-market program under Section 221 (d)(3) was authorized in 1961, the Congress required the projects to be made available to ". . . low and moderate income families . . . ," but did not define these terms, leaving that to regulations to be issued by the Secretary (then Administrator). The latter in turn approached the problem indirectly, by issuing regulations establishing design and cost standards by areas for the structures that could be accepted for mortgage insurance, and then attempting to relate eligibility to the ability to meet the resulting rent levels.

The collective term "families of low and moderate income" later came into general usage. However, when Congress rejected the administration proposal that annual subsidies in the form of rent supplements be used as a means of assisting those whose incomes were above public housing levels, and insisted that these devices be supplementary to the public housing program, the distinction between "low" and "moderate" income was greatly obscured, if not obliterated. As matters now stand, the term "families of low and moderate income" has become accepted, all-but-universal usage. Because the phrase has no defined meaning, however, the present situation is that, for the purposes of housing subsidy, the poor are defined as being those who are eligible for the benefits of the various housing assistance programs, rather than the other way around. (The latest—and one hopes, the final—attempt to define the term came with section 236, in which Congress declared that particular segment of the poor to consist, to the extent of 80 percent, of people who were approximately one-third better off than the occupants of public housing, but might include up to 20 percent who were not more than 90 percent as well off as occupants of housing under 221(d)(3). It seems unlikely that this extraordinary effort will ever be surpassed.)

It is of interest to note that this brings us back, for all intents and purposes, to where the PWA started, before the public housing program was even authorized.

Meanwhile, there was imported into the law as a means of setting an eligibility test a concept which had originated in the low rent public housing program, briefly to limit eligibility, but later and principally to establish the actual rent to be paid by an eligible family while occupying a public housing unit. The public housing rule was that such families should pay at least 20 percent of income (as defined for that purpose).

In the rent supplement program (1965) and later in the programs under sections 235 and 236 (1968), this rule of thumb on setting rent levels was transformed into an eligibility standard, though the proportion was raised to 25 percent. Given the economic rent necessary on an assisted unit, an eligible family was in effect defined as one that, after applying 25 percent of its income to rent, still required the authorized subsidy in order to meet the economic rent charge. (The comparable figure in the homeownership program under section 235 is 20 percent. The five point differential is presumed to allow for such expenses of ownership (as distinguished from rental occupancy) as real property taxes, water and sewer charges, etc.) Conversely, the limit on assistance to the family was established at that amount which, together with 25 percent of the family's income, would be sufficient to cover the economic rent.

The 25 percent standard has little to support it other than the sanction of acceptance and practice. It seems apparent that the proportion of the family budget that can reasonably be allocated to rent in the case of a family with children is appreciably different from that which might be suitable for a young couple without children, or an elderly couple whose family responsibilities have been discharged. Be that as it may, the 25 percent rule is all we have under existing law, and indeed remains the pivotal concept in the whole housing assistance approach of the Federal Government.

Even this standard, it should be noted, has not been as uniformly applied as one might suppose. While the percentage has remained fixed, the definition of "income" has not, so that the actual rent burden of identically situated families may vary appreciably from one program to another.

In 1969, the old public housing rule was turned precisely upside down by the Brooke amendment (Public Law 91–152), which wrote into the law a provision that rents charged occupants in public housing may not exceed 25 percent of income (as defined by the Secretary). Although this provision was undoubtedly intended to benefit public housing tenants by removing some inequities, it proved to be an unintended disaster to the program. This was because the amendment failed to include its necessary corollary, which would have been to require the amendment of all existing and future annual contributions contracts to provide subsidies in lieu of the lost rent. The result was a financial and management crisis of national proportions in the program, in spite of subsequent amendments which were intended to relieve these problems. It remains to be seen whether the resulting financial problems can be successfully resolved.

Absence of a National Commitment

The problems of meeting the housing needs of the poor and near poor are inherently complex and difficult, even in a society of considerable affluence—perhaps especially in such a society. At the very least, some agreement must be reached on such matters as who is to be subsidized; by what methods and in what amounts; and to what standard of housing the subsidies are to be related. None of these questions is easy, nor does any ready answer to any of them command such a preponderance of opinion as to be assured of general acceptance.

It may be, however, that many of the perplexities and difficulties that have beset public housing and other forms of Federal housing subsidy over the years are due to the fact that there has never been a firm and binding national commitment to the proposition that all Americans, rich and poor alike, must and shall be decently housed, regardless of what that entails. Such national commitments are not unknown. For example, a judgment was arrived at long ago that illiteracy is intolerable in a civilized society, let alone one whose dependence on technology was constantly increasing. The national commitment to a system of universal free public education for all has never since been seriously questioned. There is a vast amount of agonizing and debate over how education is to be paid for, but none at all as to whether it shall be, or to whom it shall be made available.

Nor are such general commitments unprecedented in connection with subsidized housing in other developed countries confronted with similar problems. In West Germany, for example, a decision was reached after the devastation of World War II that as a matter of public policy the Government would take whatever steps were necessary to provide sufficient housing to enable everyone, regardless of income, to live in at least minimum standard shelter. In fairness, it should be pointed out that the devastation itself in some measure made this decision easier to come to. The residential areas of most major and many minor cities had been all but obliterated by intense bombing, fire storms, and the like. Thus the nation faced, in any event, the unavoidable necessity of an enormous public program of rebuilding. This being said, however, it would seem an inadmissible assumption that devastation and defeat in war are the necessary prerequisites for a decision that decent housing for all should be provided as a matter of public policy. It was fully recognized that this would involve a heavy commitment of public resources, but this was not considered important enough to defeat the public purpose. Accordingly, it was done, and the very general use of housing subsidies that was found to be necessary is accepted as a matter of course, and carries no social stigma whatever.

We in the United States, on the other hand, have always felt it necessary to rationalize or justify housing subsidies for those of low income on other or collateral grounds. (Indeed, we feel uncomfortable with this forthright term, and tend to resort to less explicit alternatives, such as "housing assistance.") For example, it was long believed and widely argued that to move slum dwellers into decent, safe, and sanitary housing (sometimes even over their protest) would tend to make them better citizens, and to reduce juvenile delinquency and crime and other social evils. Time and experience have heavily eroded the factual basis for this argument, and it is less widely heard today. But it has been replaced with other propositions serving a similar function.

Many of the arguments in support of present programs can be boiled down to the assertion that the poor should receive housing subsidies, not so much because they are living in substandard housing, as because they are poor. Substandard housing is itself a term which has never been satisfactorily defined and has changed meanings as the quality of housing in general has improved. Having been ill-used in so many ways by the rest of society, they deserve at least this much by way of partially redressing the balance. Whatever the merits of this proposition in equity, it is clearly addressed not so much to the question of how the poor are in fact now housed, as to how the poor deserve to be treated.

It is conceivable that this way of looking at the matter may account for the view—rather widely held today—that housing subsidies in general should be considered as welfare measures rather than as housing programs. In any event, it is clear that a strikingly different result is reached if the problem of housing low income people is viewed as being entirely a matter of housing policy, having absolutely nothing to do with welfare.

The Early Priorities

In this context, it is worth recalling that the Federal Government's first venture into this area during the Depression was not really a housing program at all in the strict sense, but part of a broader program of the Public Works Administration to stimulate construction and reduce unemployment. Thus Congress authorized, as part of "a comprehensive program of public works,"

> . . . for construction, reconstruction, alteration or repair under public regulation or control of low cost housing and slum clearance projects . . . .

Two points are noteworthy in connection with the quoted language: First, that the words foreshadowing a larger policy than economic recovery are not those relating to construction, reconstruction, etc., but rather those contemplating "public regulation or control"; and second, that the authorizing language treated "low cost housing" and "slum clearance" projects as concepts of equal standing, if indeed not virtually interchangeable.

As we have seen, these concepts were transferred virtually intact into the public housing program initiated under the U.S. Housing Act of 1937.[141] In reciting the national policy and purpose behind the act, the Congress named as its first aim ". . . to alleviate present and recurring unemployment." In addition, the act was intended to "remedy" the unsafe and insanitary housing conditions of—and the acute shortage of decent, safe, and sanitary housing for—families of low income that are "injurious to the health, safety and morals of the citizens of the Nation."

Thus, the priorities which were then recognized by the Congress were these:

- To relieve unemployment;
- To abate a general nuisance; and
- Incident to these, to improve the housing conditions of at least some low income families on grounds of health, safety, and morals.

The 1937 act, like the PWA program, covered both housing and slum clearance—again treated as being in effect a single purpose. The only distinction made between the two was the introduction of annual contributions (or capital grants) for low rent housing projects. It is clear in context that this was not viewed as a major distinction in itself, but simply as the device to assure that such projects would retain their initial character over an extended period of time.

[141] Public Law 412, 75th Congress.

The act did, however, make a change in terminology which is of some importance: It substituted the expression "low rent" housing for "low cost" housing. It is regrettable that careless usage in later years has all but obliterated this very basic distinction.

"A Matter of Simple Justice"

In reporting the bill which became the Housing Act of 1948, after some 3 years of comprehensive hearings pursued largely at the instance of the late Senator Robert Taft, the Senate committee gave clear indication that the Congress was beginning to see these priorities in a somewhat different light.[142] Acknowledging that:

> There is no doubt that much difficulty could be avoided and the passage of this bill considerably eased, if we were to eliminate provisions for public housing for families of low income,

the Committee went on to say:

> But the committee does not see how, *as a matter of simple justice,* it can recommend a housing program which would aid all groups of our citizenry except the very one which is most in need of aid. (Emphasis added)

The difference of Congress about seeming to give offense to private enterprise is well illustrated in the following language from the same report:

> It is abundantly clear to the committee that private enterprise must supply the great bulk of our housing need. It is equally clear that there is a *relatively small but important* part of this need which cannot be met by private enterprise. (Ibid., p. 11, emphasis added.)

The word "small" needs to be read in the context of the next paragraph, in which the Committee observed that there were at that time some 6 million substandard housing units, mainly occupied by people of low income.

The bill proposed by the committee would have authorized an additional program of 500,000 units of public housing spread over a 4-year period. Agreement on such a program was not reached. However, and it was dropped from the bill finally enacted—simply justice yielding, in the end, to legislative feasibility.

In 1949, the Senate committee proposed and the Congress approved an even larger program —810,000 units, spread over a slightly longer period. They did not, however, attach a clearly defined national housing objective to this authorization, quite possibly because none had been formulated and agreed upon. Rather, they described it as a "minimum" program, without being specific as to the standard of measure. Clearly, what may be minimum from one point of view, may be adequate from another, and even excessive from still another.

That Congress viewed the 1949 program as a qualified undertaking, and not a commitment to the achievement of an agreed-upon purpose, is clearly evidenced by what followed. The act had authorized Federal support for new public housing at a rate of 135,000 units per year (which could be increased to as many as 200,000 by the President on a finding of need to stimulate and support the general economy). (As a practical matter, as has been pointed out, these levels were unrealistically high, taking into account the capabilities of the local housing authorities with respect to selecting and acquiring suitable sites and bringing new projects into the program.) By 1951, Congress (in its action on annual appropriations) cut this level back to 50,000 units per year,[143] and in the following year reduced that level to 35,000.[144]

"Policy" v. Commitment

The Housing Act of 1949 did write into law an idea that had been expressed earlier in less formal terms. It declared as a matter of national policy that the general welfare and security of the Nation, and the "health and living standards of its people," require, among other things, "the realization as soon as feasible of the goal of a decent home and a suitable living environment for every American family . . . ."

Successive budgets, and authorizing or appropriation actions of the Congress, made it clear that a declaration of policy is not the same thing as a commitment to its realization—at least within a discrete time frame. Both the executive branch and the Congress treated this formal declaration more as a source of rhetorical or political precedent for particular proposals than as a binding requirement bearing upon those responsible for deciding what should be done. "As soon as feasible" is obviously, at best a vague standard, and, as noted above, Congress began very quickly to retreat from the levels of public housing that had been authorized in the same act that contained the declaration of policy.

Between 1949 and 1968, the executive and the Congress continued to experiment with various ways of articulating the public purpose of housing subsidy programs, but with indecisive

[142] S. Rept. 140, 80th Congress, 1st Session.

[143] Public Law 137, 82nd Congress.
[144] Public Law 455, 83rd Congress.

results. For example, in 1961 (when the below-market program under FHA section 221(d)(3) was initiated), the legislative committees explained that it had not one purpose, but three purposes—namely, to reach the "largest unfilled demand" then existing in the housing market; to enlarge the role of private enterprise in subsidized housing; and to stimulate construction and alleviate what was described as a "depression in the homebuilding and related industries.[145]

Thus, as in the thirties, the moving forces were not considered to be public policy or public necessity, but rather the specific political and economic problems current at the time. Unemployment, for example, was no longer so serious a matter, and thus disappeared from the formulation of purpose. The housing industry was then in difficulty, however, so that stimulation of construction—in this case specifically of housing construction—remained a central point of emphasis.

As for the National Housing Policy, the Senate committee limited itself to remarking that in acting upon the bill it had:

> . . . been mindful and most conscious of the national housing policy set forth in the Housing Act of 1949, *more particularly that part of the policy which states "private enterprise shall be encouraged to serve as large a part of the total need as it can."* (Emphasis added.)

"National Goal" v. Commitment

Perhaps the nearest approach to the formulation of a general commitment came in the Housing and Urban Development Act of 1968. In that act, the Congress not only reaffirmed the 1949 statement of "policy," and its standing as a "national housing goal," but went further to give it the appearance of concrete dimensions both in numbers and in time, declaring:

> . . . that it [the goal] can be substantially achieved within the next decade by the construction or rehabilitation of twenty-six million housing units, *six million of these for low and moderate income families.* (Emphasis added.)

Some measure of the distinction between declaring a goal and undertaking to meet it can be discerned in the 1968 act itself. Thus, the new housing subsidy programs which it contained (principally FHA sections 235 and 236) were authorized at limited maximum amounts for 3 years—not 10.

A Speculative End-Note

One conclusion almost irresistibly emerges from this review of four decades of American undertakings, experiments, and improvisations in the field of subsidized housing. That conclusion is that from the very outset the public and the Congress failed to reach—indeed, failed even to recognize the necessity to reach—a basic policy decision as to what, if anything, the Nation intended to do about the housing of its people. The question was not merely left undecided; it was hardly even mentioned. At no point was it made the central issue, which had to be wrestled with until somehow settled.

This fateful ambiguity is evident in the earliest considerations of the problem—the object was said to be to stimulate private investment; it was to generate employment in the construction trades; it was to abate health hazards; it was to contribute to orderly urban development; it was to combat juvenile delinquency; it was to relieve the revenue problems of overburdened central city areas. In short, it was to serve any of a vast variety of purposes that were dear to their supporters, but that were not, in and of themselves, housing purposes. Indeed, it is rare to find in all the vast record of the subject anyone who advanced the proposition that, as a matter simply of a healthy society, it would be well to take such steps as might be necessary to assure housing for everyone, regardless of income or other (in these terms) irrelevant considerations.

Nor has that original omission been made good in the years that followed. The National Housing Policy formulated by Congress in 1949, viewed objectively, is not so much a policy as a rhetorical flourish, and the legislative record since 1949 makes it clear that it has been so recognized. It was better described by the 1968 Act as a "goal"—and it is significant, surely, that the determination to achieve the goal in 10 years lasted barely half the original 10-year period.

In short, the historical record compels us step by step to the conclusion that we have never had a national housing policy, and do not have one now. We have had instead a miscellaneous and often changing bundle of housing programs, some relatively effective and others not, supported with varying degrees of enthusiasm by different Congresses and different administrations from time to time. The whole is less than the sum of its parts.

It is legitimate to ask why this should be so. We contradict the premises of our own political system if we lay the blame at the door of the Congress. While individual members of Congress may be biased or callous or indifferent or shortsighted, it is an essential premise of our system that the institution that is Congress is none of

[145] See, e.g., S. Rept. 281, 87th Congress, 2nd Session.

these, and that over time, within the limits of human fallibility, it faithfully reflects the views and values of our society.

The simplest explanation, therefore, may be that the American people have never felt all that strongly about housing as such. Perhaps that is because we have always considered ourselves to be, relatively speaking, well housed as a national community—notwithstanding the deplorable conditions under which everyone recognizes many people are compelled to live. Perhaps it is because other economic and social objectives have commanded a higher priority. Perhaps it is both.

Even the periodic crises that overtake the housing industry in periods of violent market distortion are not perceived by the public generally as housing crises, but as economic crises for homebuilders and residential mortgage lenders. The crises provoke us to emergency measures not to house the people but to put construction labor back to work, to keep homebuilders from going out of business, and to preserve the solvency of our thrift institutions.

It is easy to call to mind examples of major social change that have come about because the public at large had made a decision that they must. The adoption of a universal income tax; the repeal of the 18th Amendment; the right of the working man to organize; even the abandonment without victory of the last two great wars in which the country has engaged—these are but a few instances of enormous changes that have been effected because they had become social imperatives.

Even today, we may be seeing such a social imperative taking form among us—not on the subject of housing, but on that of food. There are at least some signs that American society is reaching a state of mind that will not tolerate hunger or gross malnutrition in our affluent nation, regardless of the mechanics by which wealth happens to be distributed at a particular time. If that decision hardens, we can be sure that a system of food distribution will be evolved that will feed everyone adequately. The public attitude would then be, if that means universal food stamps (or some other device), so be it. And the means will be found, or if necessary, invented.

When, or even whether, some such cultural decision may be reached on housing we have no means of knowing. There is nothing inherently mysterious about either the economics or the technology of shelter. If it becomes a settled policy of American society that adequate housing shall be available to all, there can be no reasonable doubt that it would be made available, and probably in considerably less than a lifetime. This would require widespread adjustments in our institutions and practices, to be sure, as all major decisions do. They would be made.

Meantime, we would do well to reflect upon some of the lessons that experience should by now have impressed upon us. Perhaps the first and simplest of these is that the profit system, operating according to its own principles and mechanisms, has not been able to provide decent housing for the poor in any developed country. It has not been able to do so here, and will not be able to do so in the future. This simple statement of fact may offend some, but we do ourselves no favor by entertaining the delusion that our particular system of production and distribution, whatever its merits, is without faults or limitations.

The second and equally important conclusion to which our past experience seems to point is that there are no partial solutions to "the housing problem." The very nature of the problem is such that it can be solved as a whole, or not at all. If a higher percentage of the population is adequately housed than formerly was the case, that is improvement of a sort, to be sure. But that is a matter of statistics, not solutions.

A program—or a series of programs—that helps some of the poor and ignores the rest is bound to fail, first because it is inequitable, and second because it offends against common sense. Manifestly, it is impossible to rehouse all of the ill-housed poor simultaneously, but the commitment to the last family housed must be as binding as that to the first, otherwise the enterprise is doomed.

Impact of Judicial and Administrative Decisions on Legislative Policy Development and Implementation of Housing Programs

By Milton P. Semer, Julian H. Zimmerman, Ashley Foard, and John M. Frantz
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Introduction

The extensive research and review effort undertaken by the Department of Housing and Urban Development beginning in 1973 was intended to recapitulate and evaluate the involvement of the Federal Government in housing programs, including those providing subsidized housing for low and moderate income families, over the period since that involvement first became substantial and with the enactment of the series of major housing statutes of the early and middle 1930's. With that object in view, it focussed heavily on the legislative history of the various programs to which the Federal Government has, from time to time, addressed itself, and on their political origins (using that term in its nonpartisan sense), their financial soundness, and their social and economic efficacy in achieving their several objectives.

Such a focus was clearly appropriate in terms of the basic purpose, which was to let the events and experience of the past shed such light as they might on the problems involved in developing workable and desirable policies to govern the future Federal role in the national housing scene. It was also recognized, however, that in our scheme of government, the decisions of the courts, and even the decisions of administrative officers in the executive branch, may often have as much influence on shaping the course of events as the more widely noticed decisions of the Congress.

The accompanying report, therefore, attempts to provide for the serious student of housing policy two additional perspectives: first, a review of the main lines of judicial decision that have had an influence—sometimes a decisive influence—on the development of Federal housing policy; and second, some significant illustrations of the ways, often unforeseen, in which the exercise of administrative judgment and discretion by the responsible officials of the executive branch have served to enlarge, diminish, or give new dimensions to the bare outlines of a legislative enactment.

So far as is possible in an area where so many issues are in litigation and when new decisions and new precedents are made so frequently, the first part of this study is current as of the date of its submission—roughly, through early summer 1974.

The field of administrative policymaking and regulation is so vast that the second part of the study can proceed only by way of a selection of significant examples. In this area, an effort has been made to select a considerable number of instances; each different from the others, and yet each illustrative of the broad and sometimes completely unpredictable reach of administrative decisionmaking—and, in consequence, of the heavy burden of analysis and forethought that must rest on program administrators when they are called upon (as frequently they must be) to decide new, ground-breaking questions.

Impact of Judicial Decisions

The variety of specific ways in which court decisions can affect housing legislation and its implementation are as numerous as the various aspects of applicable statutory authorities and their related regulations and administrative actions. Because of the nature of the judicial process, the impact of court decisions is quite different from that of legislative or administrative actions. It is generally less regular and more uncertain. Because courts decide only when issues are raised by litigants, a program may escape judicial action for long periods of time or entirely. Another distinctive characteristic that impresses itself upon the layman is the tendency of the impact of judicial decisions to be negative rather than affirmative. Often, however, a decision that is negative in a particular case may be important for the affirmative legislative or administrative action which that decision makes possible—as will be shown.

There never has been broader scope to litigation in this field than during the last few years, due in large part to the many ramifications and the pervasiveness of equal opportunity cases.

The several hundred pending cases involving HUD or its programs far exceed the volume of litigation only a few years ago.

To explain some of the major judicial impacts on housing legislation and its implementation, they are categorized in the discussion that follows. To an extent, these categories are necessarily arbitrary, and the establishment of a principle of law by one decision may affect the subject matter under more than one category.

Determining the Validity of a Program In Whole or In Part

All housing programs and many other Federal aid programs were of uncertain constitutionality until the U.S. Supreme Court decision of *United States* v. *Butler* [1] in 1935, which decided that the power of the Federal Government to tax and spend for the general welfare under the U.S. Constitution (Article 1, Section 8, Clause 1) is not limited to the enumerated legislative fields specified in other provisions of the Constitution. Until then, there had been a sharp division among scholars.

In general, housing programs fared better than a number of new programs authorized in other fields during the early 1930's which were terminated pursuant to Supreme Court decisions holding them unconstitutional. Such decisions exemplify the most dramatic judicial impact—more traumatic by far than the current suspension of housing subsidy programs.

Not all housing programs were to escape such drastic impact, however. The PWA program of direct Federal construction of low rent public housing (discussed in the preceding report on housing subsidies) fell victim to the Federal court of appeals decision of *United States* v. *Certain Land in the City of Louisville, Jefferson County, Kentucky*,[2] which held in 1936 that the general welfare clause in the U.S. Constitution does not authorize condemnation of private property for low cost housing and slum clearance. Provisions of the National Industrial Recovery Act on eminent domain as applied to such housing were declared unconstitutional. It was held that housing is not a "public use," as required for eminent domain, on the grounds that benefits of employment and aid to a limited group of low income people did not constitute a public use. That decision was before the *Butler* decision, and lawyers today are in general agreement that the *Louisville* decision would not be followed now.

At the time of the decision, the PWA housing program was in full operation with an allocation of about $400 million—equal to several times that amount today. The decision stopped all projects requiring use of eminent domain, and further projects were not undertaken. As a result of the decision (and other factors) an entirely new program was developed and enacted as the Housing Act of 1937.

The new program launched under that act was dependent on court decisions, but of a different kind. Because the program operated through financial assistance to local public bodies, which had to undertake eminent domain to acquire land for the low rent housing and had to have tax exemption of the property under State law, the supreme courts of the various States had to determine the validity of such steps under their respective State constitutions. After carefully planned and timed presentations, favorable decisions were obtained in the supreme courts of most States. A similar practice was followed later in getting judicial approval of urban redevelopment projects. The citations to these State court decisions are contained in two pamphlets on the subject (each of some 50 pages) issued in 1971 by the Office of General Counsel of HUD. Those favorable State court decisions were essential to the continuation of the low rent public housing and the urban redevelopment programs.

The broadest, and indeed the leading, case dealing with these constitutional issues was *Samuel Berman* v. *Andrew Parker*.[3] Although this case raised issues similar to those presented in the State litigation discussed above, it was decided in the Federal courts because it arose in the District of Columbia. The decision of the Supreme Court in that case upheld the urban redevelopment program in the District of Columbia and had important housing implications and influence on similar decisions in the States. It was here that the Court said it is for the legislature, rather than the courts, to determine whether a housing project is desirable, and that the legislature can, for the public welfare, determine that:

> . . . a community should be beautiful as well as healthy, spacious as well as clean, well-balanced as well as carefully patrolled.

In a different program area, the Federal Home Loan Bank System suffered a setback in

[1] *United States* v. *William Butler*, 297 U.S. 1 (1935)

[2] *United States* v. *Certain Land in the City of Louisville, Jefferson County, Kentucky*, 78 Fed. 2d 684, *certiorari granted* 296 U.S. 567, appeal dismissed 297 U.S. 726 (1936)

[3] *Samuel Berman* v. *Andrew Parker*, 348 U.S. 26 (1954)

1935 when the U.S. Supreme Court held unconstitutional a provision of the Home Owners Loan Act [Sec. 5(i)] to the extent that it purported to authorize a State-chartered building and loan association to convert to a federally chartered association, contrary to the laws of the State—*Hopkins Federal Savings and Loan Association* v. *Cleary*.[4]

Determining the Scope of a Program

Judicial decisions have a heavy impact on housing programs or other programs in cases where constitutional questions exist as to their scope or the manner in which they are being administered. The most difficult problem for the administrator of the program often does not arise because of a specific controlling decision, but because of the paucity of decisions, which leaves the door open for controversy.

An outstanding example of that situation arose in the program of direct loans to colleges for dormitory facilities, authorized by Congress in 1950. A large portion of all prospective borrowers were church-related institutions. During the early part of the program, there were no court decisions involving similar facts upon which to rely as to the application of the "establishment of religion" prohibition in the First Amendment to the Constitution. Therefore, it was necessary to make the best judgment possible regarding its application to the college housing loan program from court decisions in other fields, particularly governmental aid to parochial elementary schools. Those decisions themselves were divided depending on the degree of Government involvement and school benefit, as distinguished from the secular aid to students in the school. Accordingly, the administrative decision was made, and always followed, to proceed with loans for dormitories of church-related colleges, except divinity schools.

That administrative decision did not remove the controversy, however, and the agency was criticized, sometimes severely, by a few congressional leaders for not assisting divinity schools, and by other individuals for assisting any church-related schools. Much later (in 1971), the agency position was confirmed, in effect, by the Supreme Court of the United States in *Eleanor Taft Tilton* v. *Elliot Richardson*,[5] which upheld construction grants for academic facilities of church-related colleges if not to be used by a divinity school or for other sectarian purpose.

The direct loan program for housing for the elderly and handicapped, as well as Federal aid for certain facilities under the model cities and urban renewal programs, have presented similar First Amendment issues. Generally, these also have had to be resolved on the basis of judicial decisions involving analogous but somewhat different program operations. However, land in urban renewal projects sold to church-related universities for educational purposes had been held not to violate the First Amendment. This was on the basis that each university, although benefiting from the urban renewal process, paid for the land on the basis of its value at the time of purchase. (*64th St. Residences, Inc.* v. *City of New York*, 150 N.E. 2nd 396(1958) certiorari denied sub. nom.; *Harris* v. *City of New York*, 357 U.S. 907(1958); *Kintzele* v. *City of St. Louis*, 347 S.W. 2nd 695 (1961).)

Judicial decisions may have an impact not only on the scope of an authorized program, but may similarly affect the scope of a program being proposed in legislation. For example, a proposed program may be narrowed to avoid conflict with constitutional obstacles as defined by the courts in other connections. On the other hand, judicial decisions may lead to proposals for extending the scope of a program.

An example of the latter is the specific authorization for HUD to reimburse certain homeowners for construction defects in certain properties covered by FHA mortgage insurance. Following legal principles well established by the courts, the FHA previously had assumed no liability to a homeowner for such defects. That position was, in effect, confirmed by the Supreme Court decision in *United States* v. *Neustadt*,[6] in which the Court held that FHA was not liable for serious structural defects in an existing house with mortgage insurance, even though FHA had given the purchaser an inaccurate statement of appraised value. The case had been brought under the Federal Torts Claims Act, which the Court held not applicable. It also indicated that the Congress had not intended the FHA to be a warrantor of construction.

While it would probably be an exaggeration to say that this decision led directly to the decision of the Congress in 1964 to place FHA in the position of warrantor in certain limited situations, there can be no doubt that it helped to focus attention on the plight of the homeowner and thus played a substantial, if indirect, part in this significant development in the mortgage insurance system.

[4] *Hopkins Federal Savings and Loan Association* v. *Cleary*, 296 U.S. 315 (1935)

[5] *Eleanor Taft Tilton* v. *Elliot Richardson*, 403 U.S. 672 (1971)

[6] *United States* v. *Neustadt*, 366 U.S. 696 (1961)

That the courts are not inclined to broaden FHA's responsibility beyond the specific area spelled out by Congress is illustrated by recent decisions of Federal district courts (*Dorothy Jackson* v. *George Romney*[7] and *Davis* v. *Romney*[8]), which held that HUD was not liable for defects in existing housing with mortgage insurance under sec. 221(d)(2) of the National Housing Act, even though the property was in violation of local housing codes, contrary to that statute. The decision of a Federal district court in *Luke Bailey* v. *George Romney,*[9] however, held differently, where HUD was specifically authorized by statute to compensate purchasers of existing housing covered by mortgage insurance under sec. 235 in instances where the housing has serious defects. The court held that the implementing regulation of HUD was too restrictive as to the defects covered, and enjoined HUD from such restrictive usage.

Drawing yet another distinction, a Federal district court held in *Lillie Green* v. *James Lynn*[10] that the same statute authorized, but did not mandate, HUD to make payments to purchasers because of serious defects in such housing. It also held that the manner and amount of such expenditures were clearly within the discretion of HUD. The plaintiff had not contended that HUD refused to act, but only that HUD had not acted with sufficient promptness and diligence to meet the plaintiff's demands. The court did not discuss *Luke Bailey* v. *George Romney,* but could have distinguished it on the grounds that it dealt with the validity of the applicable HUD regulation, and the statute does provide that the Secretary "shall" issue a regulation prescribing the terms and conditions of making the payments. The recent decision in the case of *Beatrice Nash* v. *George Romney*[11] held definitely that the Congress never intended purchasers of homes assisted under the National Housing Act to have judicial redress for inadequate housing.

In the preparation of legislation for any Federal aid program, it is essential to tailor its scope, as well as its other provisions, to conform to judicial interpretations of constitutional restrictions. In the public housing program, as well as in other development aid programs dependent on local agency functions, it is also essential that the Federal legislation be drawn with adequate recognition of the impact on such local functions of State constitutional provisions as interpreted by the courts.

Shaping Federal Government Activities to Make Housing Benefits Available to All on an Equal Basis

It is well recognized that the radical changes in the Federal housing programs with respect to nondiscrimination and equal opportunity resulted primarily from the changes in judicial decisions on the subject, and constituted one of the major features in recent developments in the whole civil rights area.

Early Judicial Forces: Housing programs started from a low base in this field. In planning the old PWA public housing projects, care was taken to assure that they would not be inconsistent with the spirit of the "separate but equal" requirements of State laws, which followed the old 1896 decision of *Plessy* v. *Ferguson.*[12] FHA took the flat position until about 1950 that it had no statutory or other responsibility to act positively on the matter. As late as 1955, a Federal court held in *Arthur L. Johnson* v. *Levitt and Sons, Inc.*[13] that the FHA and VA had no statutory or other duty to assure that housing built with the assistance of FHA-insured or VA-guaranteed mortgages was sold to persons of all races. That was held notwithstanding the fact that the project involved was a very large development constituting a "new community" and subject to many other Federal controls.

In the field of housing, the court decisions on civil rights did not so much force Federal executive action, but opened the way for Federal action by creating a general climate that favored all kinds of nondiscrimination efforts. That climate was brought about largely by court decisions on nonhousing matters. There had been a few early housing-related decisions, however, bearing directly on this change of attitudes. In 1917, the Supreme Court in *Buchanan* v. *Warley*[14] held discriminatory zoning to be unconstitutional. In 1948, the Court decided the famous *Shelley* v. *Kraemer*[15] case, holding that racially restrictive covenants are unenforceable. It was in 1950, after the latter decision, that FHA and VA stopped insuring or guaranteeing a mort-

[7] *Dorothy Jackson* v. *George Romney*, 355 Fed. Supp. 737 (1973)
[8] *Rubylee Davis et al.* v. *George Romney et al.*, 355 Fed. Supp. 29 (1973); United States Court of Appeals, 3rd Circuit (No. 73-1249) (1974).
[9] *Luke Bailey* v. *George Romney*, 359 Fed. Supp. 596 (1973)
[10] *Lillie Mae Green et al.* v. *James Lynn et al.*, (U.S.D.C., Southern Distirct of Ohio, Eastern Division, No. 73-141) (1973)
[11] *Beatrice Nash et al.* v. *George Romney et al.*, (U.S.D.C., Central District of Calif., No. 72-1313-RJK) (1973)

[12] *Plessy* v. *Ferguson*, 163 U.S. 537 (1896)
[13] *Arthur L. Johnson* v. *Levitt & Sons, Inc.*, 131 Fed. Supp. 114 (1955).
[14] *Buchanan* v. *Warley*, 245 U.S. 60 (1917)
[15] *Shelley* v. *Kraemer*, 334 U.S. 1 (1948)

gage on property subject to a racial covenant imposed after February 15, 1950. (That restriction was removed after the Civil Rights Act of 1968 and *Jones* v. *Mayer Co.* 392 U.S. 409 (1967) made the restriction unnecessary.)

As with other civil rights developments, the rapidly changing climate for progress dated from the landmark case of *Brown* v. *Board of Education*[16] in 1954, outlawing the "separate but equal" doctrine as applied to public schools. There followed a flood of court decisions—that has not yet abated—relating to equal opportunity in housing. *Brown* v. *Board of Education* was the forerunner of many actions by the States and each of the three branches of the Federal Government that led ultimately to the enactment of many State fair housing laws, the issuance of the executive order on equal opportunity in housing (E.O. 11063) (discussed later in this report), and the enactment of the Civil Rights Act of 1964 and the Civil Rights Act of 1968 (containing a Federal "Fair Housing Law").

In the well-known case of *Jones* v. *Mayer Co.*, id. the Supreme Court decided in 1968 that an old civil rights statute (1866) prohibited the racially motivated refusal of a private housing developer to sell a home to a Negro. The statute was held to be a valid exercise of the power of the Congress to enforce the Thirteenth Amendment (the antislavery amendment) to the Constitution. The significance of this decision was its scope, applying to all housing, regardless of Federal involvement. It paralleled the Civil Rights Act of 1968, which contained enforcement powers not otherwise available under the decision.

Recent Judicial Program Requirements: A new era in equal opportunity court decisions began in 1970, when a Federal court ordered HUD to adopt:

> . . . some institutionalized method whereby, in considering site selection or type selection [of housing], it has before it the relevant racial and socio-economic information necessary for compliance with its duties under the 1964 and 1968 Civil Rights Acts. (*Shannon* v. *United States Department of Housing and Urban Development*[17])

That case involved a change in an urban renewal plan to permit a rent supplement housing project in place of housing with lesser density. The racial issue was over the increased concentration of blacks in the area in violation of Federal civil rights requirements. As a result of that decision, and after prolonged and intense consideration, HUD issued detailed "Project Selection Criteria" for its subsidized housing programs. These included criteria designed to give preference to housing that is outside of areas of minority concentration, or where a local development plan includes such housing, and comparable opportunities exist for housing to be occupied by minority families in the income range to be served by the proposed project, outside of areas of minority concentration.

The Project Selection Criteria were developed against the background of a number of civil rights decisions that included the *Shannon* opinion, and illustrate the difficult problems coming from diverse lower court and Supreme Court decisions on various aspects of civil rights relating to site selection. Although carefully considered, the criteria are sufficiently general that discretion remains partly in the local processing office for application in specific cases.

A Federal court of appeals held that these Project Selection Criteria were not retroactive, and sustained the legality of a HUD commitment to insure a section 236 mortgage on a rental housing project for moderate income families in an urban renewal area in Chicago.[18] Although those criteria were based on constitutional principles, their specific requirements were held not to be retroactive for the purpose of determining constitutionality and other validity. The HUD action on mortgage insurance was upheld on the theory that it represented a reasonable balance of the need for housing against the risk of greater racial concentration.

Another direct impact of an equal opportunity decision on HUD was *Gautreaux* v. *Romney*[19] in 1971, in which a Federal court of appeals held the Secretary of HUD in violation of the due process requirement of the Fifth Amendment because of his approval of, and assistance to, public housing projects in Chicago that furthered the concentration of minority housing. The case was remanded to the district court for action with the suggestion that a decree requiring the Secretary to use his "best efforts" to improve the condition might be adequate. Instead, the lower court decreed that the Secretary must withhold $26 million in Model Cities funds from the city until the Chicago Housing Authority complied with an earlier decision of the court on site selection and construction of public housing. That decree, in turn, was reversed by the court of appeals on the grounds that it did not follow the prior decision, and that the Model Cities pro-

[16] *Brown* v. *Board of Education*, 347 U.S. 483 (1954)

[17] *Shannon* v. *United States Department of Housing and Urban Development*, 436 Fed. 2d 809 (1970)

[18] *Southeast Chicago Commission et al.* v. *HUD et al.*, United States Court of Appeals, 7th Circuit, 488 Fed. 2d 1119 (1973)

[19] *Gautreaux* v. *Romney*, 448 Fed. 2d 731 (1971)

gram was only partly related to public housing construction.[20]

As a further result of the above court decisions, HUD has issued affirmative fair housing marketing regulations, applicable to all FHA mortgage insurance programs, which require applicants to agree to carry on an affirmative program to attract buyers or tenants of all minority and majority groups.

Although the regulations affecting equal opportunity in employment are primarily the responsibility of the Department of Labor, HUD's housing and other programs have felt the substantial impact of court decisions on these regulations, through the need to suspend construction and otherwise. In a case involving the so-called Philadelphia Plan, a Federal court of appeals approved the use of goals in hiring minority construction workers where the contractor, under a federally assisted construction contract, was merely required to exercise good faith to attain those goals and required not to discriminate in employment practices (*Contractors Ass'n. of Eastern Pa.* v. *Secretary of Labor* [21]).

Judicial decisions in the housing equal opportunity field affect not only administrative actions by agencies, but their legislative proposals and the enactments of the Congress as well. Their effect on civil rights acts has been mentioned. In recent years there has been a special emphasis on housing for low and moderate income families—throughout the central city, in suburban areas, and in new communities—the underlying thrust of which is to seek a greater proportion of housing for minorities, because minority groups have a much heavier proportion of low income families than does the general population. (See "Evolution of Federal Legislative Policy in Housing: Housing Credits," Semer and Zimmerman, DHUD, 1973.)

In that connection, a Federal court of appeals recently held that HUD and certain other agencies authorized "to sue and be sued" may be liable in damages for their actions in violation of the Civil Rights Act of 1966. In that case (*Baker* v. *F & F Investment Company and FHA*) [22] minority homeowners in Chicago brought action for damages on the alleged grounds that they were compelled to purchase their homes under mortgage financing as a direct result of discriminatory housing practices. They claimed that HUD and other agencies knew of and perpetuated residential racial segregation in Chicago through mortgage insurance and other policies and practices over a period of years.

A Current Conflict of Equal Opportunity Principles: A recent further development in court cases beyond the *Gautreaux* and other related decisions appears to present a most complex problem that will have a broad and major effect on the Government's efforts to bring housing benefits to all on an equal basis. This problem is a logical result of the inherent possibilities of conflict between two concepts of minority rights that have been recognized by the courts: (1) On the one hand, the rights of individual members of minority groups to specific housing accommodations or other benefits through the elimination of discrimination; and (2) on the other, the right of a minority group, as a whole, to the ultimate benefit of integration in housing. These cases involve situations where there may be no discrimination against any individuals of a minority race, but where the continuation of existing priorities or other benefits for them threaten to concentrate members of that race to the point of maintaining or reestablishing racial segregation.

One such case was *Otero* v. *New York City Housing Authority* [23] in 1973, in which a Federal court of appeals reversed a district court grant of summary judgment enjoining the housing authority from renting apartments in a public housing project to others than former occupants of the urban renewal site on which the project was built until all site occupants applying for apartments had been accommodated. The majority of those occupants were minority persons, and the priority given them followed the housing authority's regulations. The court of appeals held that the summary judgment was precluded where genuine issues of material fact existed as to whether nonwhite concentration in the project would have a "tipping" effect that the authority could avoid by suspending its priority regulation. Strict application of the priority would have resulted in the project having an 80 percent nonwhite population, while the alternative proposed by the authority would have reduced that percentage to 40 percent by admitting whites who had not been site occupants.

Thus, the court in that case applied equal opportunity principles to tenant selection that had been applied earlier to project site selec-

[20] *Gautreaux* v. *Romney*, 457 Fed. 2d 124 (1972)

[21] *Contractors Ass'n. of Eastern Pa.* v. *Secretary of Labor*, 442 Fed. 2d 159 (1971)

[22] *Baker et al* v. *F & F Investment Company and FHA et al.*, United States Court of Appeals, 7th Circuit (No. 72-2036) (1973)

[23] *Otero* v. *New York City Housing Authority et al.*, 484 Fed. 2d 1122 (1973)

tion, and, in doing so, cut deeply into existing regulations already put into effect for the purpose of assuring equal opportunity through nondiscrimination in selecting tenants in public housing. The appeals court held that the Fair Housing Act of 1968 (42 U.S.C. secs. 3601 and 3608(d)(5)) imposed a duty on the Secretary of HUD and, through him, on local housing authorities to act affirmatively to achieve fair housing. That was held to include the duty to foster and maintain racial integration. The court said:

> The authority is obligated to take affirmative steps to promote racial integration *even though this may in some instances not operate to the immediate advantage of some non-white persons* . . . we hold that to the extent that [the priority for site occupants] conflicts with the authority's duty to integrate, the latter prevails and that the authority may limit the number of apartments to be made available to persons of white or non-white races . . . where it can show that such action is essential to promote a racially balanced community and to avoid concentrated racial pockets that will result in a segregated community. (Emphasis added.)

In so ruling, the court recognized that the Fair Housing Act of 1968 was designed primarily to prohibit discrimination in the sale, rental, financing, or brokerage of housing, but that a duty was also placed on HUD and local housing authorities to give consideration to the impact of public housing on the racial concentration in the area. Thus, the decision places responsible public officials in the difficult position of having to determine in each case where the line must be drawn legally, giving the proper balance to each conflicting principle. All factors relevant to racial composition of the area and future imbalance of races would be subject to review by the courts.

The recent case of *Jeffrey Hart et al.* v. *The Community School Board of Brooklyn et al.* v. *HUD et al.*[21] involved the same two conflicting principles of equal housing opportunity, and resulted in a decree against HUD having very serious implications for shaping the administration of all public housing projects and possibly other federally assisted housing. The decision of the Federal district court in that case held (January 28, 1974) that the community school board was "liable" to plaintiff students for unlawfully operating a segregated school, and that housing authorities (State, local, and Federal) were "liable" to those students because they helped maintain the segregation in the school through their administration of public housing projects in the area.

[21] *Jeffrey Hart et al.* v. *The Community School Board of Brooklyn et al.* v. *HUD et al.*, (U.S.D.C., Eastern Division of New York, Civil Action 72C.1041) (1974)

The racial balance in the school at issue, the Mark Twain Junior High School of Coney Island, changed drastically from 1962 to 1973; the proportion of white students dropping from 81 percent to 18 percent. The city, State, and Federal governments, individually and together, had sponsored and managed many publicly assisted housing projects and multi-family developments in the school district. Over 3,000 units of public housing had been built in Coney Island, and an additional 4,000 were planned or under construction. Not surprisingly—and except for public housing built for the elderly—the proportion of white population in public housing dropped similarly to that of white students in the Mark Twain school.

The court concluded that a major cause of this racial imbalance was the regulation of the New York City Housing Authority that gave first priority to former site residents of urban renewal areas. (A priority, it should be noted, that is still explicitly recognized in the Federal public housing statute, and which indeed was at one time mandatory in that law.) As displaced white families generally fare better than minorities in finding new housing, a disproportionate number of nonwhites apply for public housing. The occupants of new units of public housing in the early 1970's were therefore overwhelmingly minority families. The court stated that "the sequence tended to discourage middle class families who observed what appeared to be a precipitous policy of tipping." This was held to be particularly true with respect to white families with school-age children who might otherwise have rented or purchased housing in the area serviced by the school. As residential segregation was the result of State action, then the school board's use of a residential criterion, as in this case, was said to be double discrimination.

The court thus found a vicious circle of action—racially segregated schools, contributing to residential segregation, contributing to racially segregated schools. The court held this unconstitutional to the extent of State action by Federal, State, and local housing authorities, as well as by school officials. Great reliance was placed on the decision in the above case of *Otero* v. *New York City Housing Authority* as to the responsibility of housing officials to eliminate segregation in housing. That was held to mean that "the State must act to eliminate *de facto* racial imbalance unless it is clearly unpractical to do so."

In remedying the racial segregation at the school, the court held it had the power and duty to require not only the school board to act, but other agencies of the State as well, including the New York City Housing Authority. The court looked on the obligation of the State as a whole, and its responsibility for the several local public authorities that were involved in producing the unconstitutional results. Similarly, the court decided that Federal housing authorities are under the same compulsion to avoid segregated housing, and that the court had the power to require action by them too to carry out their responsibility in this regard. Nothing effective could be done, said the court, without the active participation of the Federal Government.

Accordingly, the court decreed that, in conjunction with the preparation of a plan by State and local officials for elimination of segregation in the school, housing officials of the city, State, and Federal government shall provide a joint plan (within a prescribed time) to remove the racial imbalance in public housing in Coney Island. The decision said:

> Renting and construction patterns shall be modified to encourage substantial numbers of whites and middle class families with children to move into buildings constructed with the aid of public funds. Plans should include advertising and inducements to encourage persons such as members of unions, policemen, firemen and other civil servants to move into the area with their families to stabilize its population.

The court quoted the holding in the *Otero* decision that the housing authority's obligation to integrate prevailed over any conflict with its regulation giving occupancy preference in public housing to former residents of urban renewal sites.

Although the Government is not appealing this decision in the *Hart* case, Federal administrative officials recognize its potential for affecting actions by other courts to the extent of drastically changing the administration of all existing and new public housing projects assisted by the Federal Government, and possibly other federally assisted housing.

A final significant development bearing on the relationship of court decisions and program administration in connection with the cases just discussed should be noted. In many of them, the courts did not simply hand down decisions and decrees, but retained active jurisdiction over the controversies in order to assure that the courts' orders were carried out both in letter and spirit. Thus, to a degree generally unusual in judicial practice, these courts have undertaken not only to declare and clarify the law, but to assume a considerable degree of supervisory responsibility for its faithful execution.

Protecting Against Local Government Actions That Would Thwart Federal Program Objectives

The current judicial decisions of this type which have impact on Federal programs relate chiefly to equal opportunity issues, and to the rights of the poor who need low income housing, especially rental accommodations.

Racial Bias: The courts generally have held that local governments may not interfere with the production of federally assisted low and moderate income housing by racial discriminatory zoning or similar practices, regardless of whether the actions of local officials were racially motivated. Thus, a district Federal court held unconstitutional an attempt by a city to block a federally assisted low income housing project for Negroes by first zoning the area as a park and later refusing sewer connections—*Kennedy Park Homes Association, Inc.* v. *City of Lackawanna, New York.*[25]

In the case of *Dailey* v. *City of Lawton, Oklahoma*[26] a Federal court of appeals held that a refusal to grant a building permit and a zoning change to permit a low income housing project to proceed violated the Fourteenth Amendment to the Constitution—racial motivation was found in that case. A similar decision was given in *Crow* v. *Brown*,[27] involving a turnkey public housing project near Atlanta, Ga., where a Federal court of appeals held that the only basis on which the county denied building permits was the belief that the housing would be occupied by blacks in a predominantly white area. A similar decision in *Morales* v. *Haines*[28] involved section 235 housing.

In the Supreme Court decision of *Nellie Hunter* v. *Edward Erickson*,[29] an ordinance of the City of Akron, Ohio, was held in violation of the Fourteenth Amendment because it required a special type of referendum as a condition to the "fair housing ordinance" becoming effective. That was said to place a special procedural burden on racial minorities.

Two decisions of a court of appeals dealt with racially segregated housing patterns in Cleveland, Ohio: *Banks* v. *Perk*[30] and *Mahaley* v. *Cuyahoga Metropolitan Housing Authority*.[31] The former held that future public housing sites

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[25] *Kennedy Park Homes Association, Inc.*, v. *City of Lackawanna, New York*, 436 Fed. 2d 108 (1970)
[26] *Dailey* v. *City of Lawton, Oklahoma*, 425 Fed. 2d 1037 (1970)
[27] *Crow* v. *Brown*, 332 Fed. Supp. 382 (1971)
[28] *Morales* v. *Haines*, 349 Fed. Supp. 684 (1972)
[29] *Nellie Hunter* v. *Edward Erickson*, 393 U.S. 385 (1969)
[30] *Banks* v. *Perk*, 341 Fed. Supp. 1175 (1972)
[31] *Mahaley* v. *Cuyahoga Metropolitan Housing Authority*, 355 Fed. Supp. 1257 (1973)

must be located outside the city's area of racial concentration, and that the absence of racial criteria in the local housing authority's site selection procedure violated the Fourteenth Amendment. The need to build low income housing outside of the city confronted the local housing authority with the problem dealt with in the second decision—the refusal of suburban governments to enter into cooperation agreements required by Federal law as a condition to aid for public housing projects. The court held such refusals, if without logical basis, constitute racially discriminatory actions, and ordered the housing authority to prepare a plan for scattered sites in the suburbs.

The effectiveness of such court action depends on more than just the initial decision, as was shown by the experience of the courts and local agencies involved in the several *Gautreaux* decisions in Chicago (some of which are cited above). There the U.S. district court in *Gautreaux* v. *Chicago Housing Authority* [32] held in 1969 that the public housing program of the city was being maintained on a racially discriminatory basis with respect to site selection and tenant assignment. A "preclearance" procedure with the alderman of the ward of the proposed housing project was especially condemned as a method of excluding Negroes from white areas and producing a highly concentrated number of public housing projects. The court prescribed specific requirements for sites of future public housing in the city with fixed percentages of units in relation to minority concentration. That decision was upheld by the court of appeals.[33] Thereafter the district court was in a running battle with city officials and forced to issue specific decrees [34] on the administrative steps the city and the Chicago Housing Authority must take to proceed with public housing. Officials of HUD were involved, as reflected in litigation discussed earlier.

In a more recent action (September 11, 1973), the district court denied a motion by the plaintiff to require the Chicago Housing Authority and HUD to plan and fund low rent public housing projects for the entire metropolitan area, the motion being based upon court decisions involving school integration on a metropolitan basis. However, the court did direct HUD to use "its best efforts," and cooperate with the Chicago Housing Authority, to increase the supply of public housing within the City of Chicago, consistent with applicable laws, regulations, and court decrees.[35] That decision is being appealed by both sides.

Discrimination Against Poor: Where no racial bias exists, the role of the courts in protecting the poor against discriminatory housing actions by local governments is much less extensive and more loosely defined. Some decisions have been recorded, however.

The Pennsylvania Supreme Court held, for example, in the Appeal of Kit-Mar Builders, Inc.[36] that a township's 2-acre or 3-acre single family zoning was unconstitutional. It stated that a township could not arbitrarily decide who would live in its boundaries, while disregarding the interests of the entire area. Similarly, the same court held in the Appeal of Girsh [37] that a township zoning scheme that excluded apartments was unconstitutional. The court stated that such action amounted to zoning out the people who would be able to live in the township if apartments were available.

A court of appeals in *Southern Alameda Spanish Speaking Organization (SASSO)* v. *City of Union City, California* [38] ruled on a city's zoning requirements that allegedly made it impossible to provide adequate housing for low income families. The court refused to hold the ordinance illegal until after a period of experience, but said it may well be that a city is legally obligated to see that its plan accommodates the needs of low income families.

Assistance to the provision of public housing under existing cooperation agreements between a local housing authority and the city was provided by two recent decisions involving Cleveland, Ohio—*Cuyahoga Metropolitan Housing Authority* v. *City of Cleveland* [39] (two separate decisions carrying the same name in 1972 and 1973).

Perhaps the leading case in this area is *James* v. *Valtierra*,[40] in which the Supreme Court of the United States upheld a referendum (a required procedure under the State constitution) deciding against a public housing project in San Jose, Calif. (Referenda are very common procedure in California.) There was no proof of

[32] *Gautreaux* v. *Chicago Housing Authority*, 296 Fed. Supp. 907 (1969)

[33] *Gautreaux* v. *Chicago Housing Authority*, 436 Fed. 2d 306 (1970), *certiorari denied* 402 U.S. 922 (1971)

[34] *Gautreaux* v. *Chicago Housing Authority*, 342 Fed. Supp. 827 (1972); 363 Fed. Sup. 690 (1973)

[35] Ibid.

[36] The Appeal of Kit-Mar Builders, Inc., 268 Atl. 2d 765 (1970)

[37] The Appeal of Girsh, 263 Atl. 2d 395 (1970)

[38] *Southern Alameda Spanish Speaking Organization* v. *City of Union City, California*, 424 Fed. 2d 291 (1970)

[39] *Cuyahoga Metropolitan Housing Authority* v. *City of Cleveland*, 342 Fed. Supp. 250 (1972); 474 Fed. 2d 1102 (1973) (separate cases with same name)

[40] *James* v. *Valtierra*, 402 U.S. 137 (1971)

racial discrimination. The Court held the State had the right to require a referendum on a matter, such as public housing, that involved local public expenditures and actions.

This case is widely cited as authority for the proposition that the equal protection clause of the Fourteenth Amendment does not protect the poor, as such, against housing discrimination, and the case provided support, in part, for the President's July 11, 1971, statement on Federal policies relative to equal opportunity in housing.

Actually the Court was particularly careful in that case to limit its decision to the facts involved, relying heavily upon the referendum procedure (especially because of its great usage in California) as well as the local government involvement in a public housing project. The Court said " . . . a lawmaking procedure that 'disadvantages' a particular group *does not always* deny equal protection" (emphasis added), thus distinguishing the case from those involving "invidious" and "arbitrary" classifications which have traditionally been held in great numbers to violate the Equal Protection clause. It seems reasonable to assume that a classification by social or economic strata in housing could be of such a nature that it would be held to meet the traditional "invidious or arbitrary" tests. If so, there is a basis for much further judicial impact on local agency actions affecting housing.

Determining Validity of Impounding Housing Program Funds

Because of the attention being given to this subject currently, its importance is rather generally recognized. Much of the relevant litigation is still pending.

The validity of executive branch action in suspending housing programs and impounding housing funds was brought directly into issue in the case of *Commonwealth of Pennsylvania et al.* v. *James T. Lynn et al.*[41] in the U.S. District Court for the District of Columbia. Plaintiffs brought a class action, on behalf of all applicants for Federal financial assistance under the section 235, the section 236, and the rent supplement subsidy housing programs, to obtain injunctive relief to compel James T. Lynn, Secretary of Housing and Urban Development, and Roy L. Ash, Director of the Office of Management and Budget, to begin reprocessing pending or new applications for such assistance, which were suspended by the Secretary on January 8, 1973.

On July 23, 1973, Judge Charles Dickey filed his decision in the case, upholding the standing of the plaintiffs to bring the class action, and holding unlawful Secretary Lynn's suspension of the programs on January 8, 1973 and his refusal to accept new applications or process applications pending on that date. The court enjoined the Secretary from refusing to accept new applications or to process existing applications in accord with his own regulations, and ordered him to approve and complete the processing of those projects found by him to be qualified under those regulations. (A motion by Director Roy Ash for dismissal as to himself was granted on the alleged ground that the OMB does not, as a technical matter, "apportion" obligational authority to enter into commitments such as those involved in these programs.)

The court decision in that case was based on a conclusion that the provisions of several enactments amounted to a mandate by the Congress that subsidy housing programs must continue without suspension, and that under the Constitution only the Congress can change that requirement. The court rejected defendant's argument that suspension and impounding are a proper exercise of discretion pending a further reevaluation of the programs that presented difficulties of administration consistent with congressional intent.

For that conclusion, the court relied heavily on language in the Declaration of National Housing Policy in the Housing Act of 1949 calling for "the realization as soon as feasible of the goal of a decent home and a suitable living environment for every American family," and the statement that:

> . . . The Department of Housing and Urban Development . . . shall exercise (its) powers, functions, or duties under this or any other law, consistently with the national housing policy declared by this Act and in such manner as will facilitate sustained progress in obtaining the national housing objectives hereby established.

Subsequent congressional actions, including repeated appropriations, were cited by the court as showing a continuing intent to the same effect. Special emphasis was also given to the national housing goal in the Housing and Urban Development Act of 1968, prescribing a specific goal in terms of units to be produced, especially the goal for housing for low income families, and the declaration that the highest priority be given to that housing. The court specifically held that

[41] *Commonwealth of Pennsylvania et al.* v. *James T. Lynn et al.*, 362 Fed. Supp. 1363 (1973); U.S. Court of Appeals, D.C., No. 73-1835; Supreme Court of the United States, October Term, No. A.230 (1973)

the discretionary powers of the executive branch under Article II of the Constitution do not include authority to terminate or suspend indefinitely a statutory program, such as involved here, for the reason that Congress may see fit to alter it later.

The above case has been appealed by Secretary Lynn to the U.S. court of appeals. A stay of judgment was denied by the district court and by the U.S. Court of Appeals for the District of Columbia, but Chief Justice Burger granted a stay, and by a vote of 8 to 1, the Supreme Court denied a motion to vacate that stay.[42] That meant, of course, that suspension of the programs could continue pending a decision on the merits by the U.S. court of appeals. The appeal has been argued in that court but no decision has been rendered. (Since this section was written, the circuit court handed down a decision reversing the trial court and sustaining the position of the Government.)

During the week following the above decision by Judge Charles Dickey, he also held unlawful the suspension of similar subsidy housing programs of the Farmers Home Administration (section 502 and section 512) on the same grounds as expressed in the above decision *(Willard La Verne Pealo, et al.* v. *Farmers Home Administration, et al.)*.[43] The Government decided not to appeal that decision, and the Farmers Home Administration resumed processing applications under those programs.

In the pending case of *Augusto Guadamuz, et al.* v. *Roy L. Ash, Earl M. Butz, and James T. Lynn*,[44] prospective beneficiaries under the Section 312 Rehabilitation Loan Program of the Department of Housing and Urban Development and the Rural Environmental Assistance Program of the Department of Agriculture seek to compel the defendants to fund the programs at the maximum levels authorized by the Congress. On June 29, 1973, Judge Thomas A. Flannery granted preliminary injunctive relief, ordering that the "court's order shall constitute documentary evidence of an obligation of the United States" of the appropriated funds under the section 312 program of HUD that were impounded by the defendants. Unless obligated by June 30, 1973, those funds would have lapsed by statute. The court indicated that its action would preserve the opportunity for the court to decide the important issue on the merits, and that substantial questions had been raised as to the powers of the defendants to impound the funds. (The Rural Environmental Assistance Program was not included in this action as its funds did not lapse June 30, 1973.)

In 1972, a U.S. district court, in the case of *Housing Authority of the City and County of San Francisco* v. *HUD*,[45] refused to take action to force the release of impounded urban renewal funds which were needed by the housing authority for its development programs for public housing. The court found that no statutory language required by the executive branch to spend the designated amount of funds appropriated, and said the plaintiff was asking the court to determine when the President's conceded discretionary authority becomes an abuse of discretion. The court held that, in the absence of justiciable standards for making that determination, the issue is a political one for resolution by the Congress.

A case that received much public attention *(State Highway Commission of Missouri* v. *John Volpe, etc., and George Schultz)*[46] had only limited relevance to housing programs because of unusual language in the applicable statute relating to State highway funds. (The court held that language in the statute was precatory and not mandatory—meaning, in effect, that it was the sense of the Congress that the funds in question not be impounded or withheld from obligation. However, the court relied primarily on the specific statutory apportionment procedure, by DOT for the States, preceding the appropriation, and the provision that if a State's highway program is approved under that procedure there is "deemed" to be a contract to pay the State's proportionate amount of the appropriated funds.)

A case involving another program is relevant to housing fund impoundment, but also turned on special language in the authorizing statute. *Local 2677, American Federation of Government Employees* v. *Phillips*[47] held illegal the actions by the Acting Director of OEO to discontinue funding community action agencies and to abolish OEO. Such actions were held to be contrary to the specific language of a 1972 amendment prescribing that the community action agencies "shall" continue through June 30, 1975.

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[42] Ibid.

[43] *Willard La Verne Pealo et al.* v. *Farmers Home Administration et al.*, 361 Fed. Supp. 1320 (1973)

[44] *Augusto Guadamuz et al.* v. *Roy L. Ash, Earl M. Butz, and James T. Lynn*, 368 Fed. Supp. 1233 (1973)

[45] *Housing Authority of the City and County of San Francisco* v. *HUD*, 340 Fed. Supp. 654 (1972)

[46] *State Highway Commission of Missouri* v. *John Volpe and George Schultz*, (U.S. Court of Appeals, 8th Circuit, No. 4273), 41 L.W. 2539 (1973)

[47] *Local 2677, American Federation of Government Employees* v. *Phillips*, 358 Fed. Supp. 60 (1973)

That unusual language was held to prevail over budgetary or other executive actions. The court said the Congress could terminate the program either by changing the law or by not appropriating funds for it; Congress has done neither.

Determining Compliance with a Non-Housing Federal Objective—Environmental Protection

The impact of the National Environmental Policy Act of 1969 (42 U.S.C.A. 4332), as interpreted by the courts, is analogous in a sense to many other results of court decisions that have a pervasive effect on housing program operations, such as decisions on due process or other protections of individual rights. But decisions on environmental protection are much more than that. Just as equal opportunity requirements added an additional objective to housing programs, so did environmental protection, but the latter is somewhat different in that its objectives are not quite so related to housing as such.

It also has been said that one initial impact of this act as interpreted by the courts has been an unprecedented disturbance to orderly project operations under HUD and other programs. To the extent that this objection is correct, it may well have been due, at least in considerable part, to inadequate consideration being given in all quarters to the significance of the original legislation when it was being considered and enacted.

One initial impact of the decisions of lower courts in this field is uncertainty—as often occurs when there are conflicting objectives of a controversial nature. This can be illustrated by a few decisions. One is the recent decision in *San Francisco Tomorrow* v. *George Romney*,[48] holding that HUD had not violated the act by entering into two amendments to an urban redevelopment contract without filing an Environmental Impact Statement (which is required by the act in connection with each "major Federal action"). The amendments increased the amount of grants for urban redevelopment and the amount of grants for relocation activities in connection with it, which the court refused to consider as "major" Federal actions inasmuch as they carried out the original loan and grant contract that constituted the major Federal action. The same decision, however, held that HUD violated these provisions of the act by approving a change in another redevelopment project from "an industrial park project to a neighborhood development program."

The decision of *Benjamin Jones* v. *James Lynn*[49] held otherwise, in a case involving the Fenway Park Urban Renewal Project in Boston, Mass. which had been approved in 1967 but was still substantially incomplete. The court of appeals remanded a district court decision that had denied injunctive relief under the act on the basis that amendments to the original urban renewal contract to increase relocation grants and a temporary loan authorization did not constitute "major Federal actions." The court of appeals held that the amendments could be major Federal actions that affect the environment through changes in relocation and otherwise. It continued a temporary stay of construction pending the district court's reexamination and detailed findings on relevant factors. The decision also contained the suggestion to the district court that, if planning indicates the need for further financial assistance, the court should "order HUD" to conduct an environmental study of the entire project to determine what changes can still be made and to inform the community of what the impact will be, what adverse effects cannot be avoided, and what irretrievable commitments of resources are involved when the plan is fulfilled.

The recent decision in *Brotherhood Blocks Association of Sunset Park* v. *Secretary of HUD* [50] involved a proposed auction of 182 properties in Kings County, New York, that had been acquired by the Secretary under the home mortgage insurance programs and had not been sold under previous offers. The properties were once improved, but the buildings had been demolished; they were largely scattered sites, and they were in rundown parts of the area. In accordance with its issuances, HUD had prepared, in connection with the proposed sale, a special environment clearance (or "negative impact statement") which concluded that an environmental impact statement under the National Environmental Policy Act was unnecessary because the sale would simply substitute one owner for another and not affect the environment.

The court held that the clearance document was inadequate because the public, including individual community groups, was not given a voice in framing the decision, and that the public was entitled to advance notice of the sale and an opportunity to submit relevant data. The bulk

[48] *San Francisco Tomorrow* v. *George Romney*, 342 Fed. Supp. 77 (1972); 472 Fed. 2d 1021 (1973)

[49] *Benjamin Jones* v. *James Lynn*, 354 Fed. Supp. 433 (1973); 477 Fed. 2d 885 (1973)

[50] *Brotherhood Blocks Association of Sunset Park et al.* v. *Secretary of HUD* v. *United Block Association, Combined Block Association*, 474 Fed. 2d 1336 (1973)

sale of so many properties—as distinguished from individual sales—was held to constitute a "major Federal action" requiring public participation or the preparation of a special environmental impact statement under the act. It had been alleged that the auction sale would result in purchase by speculators who would hold the land undeveloped and thus contribute to further urban decay in the area. The court stated public participation in the proposed sale might have resulted in an acceptable alternative.

That decision may be compared to another, *Nucleus of Chicago Homeowners Association* v. *James Lynn,*[51] in which the court concluded that a similar "negative impact statement" was adequate in the case of a proposed public housing project. It had been alleged that the environment of the project would be adversely affected by its tenants, because public housing tenants are prone to crime, violence, and other undesirable qualities. The court held that "environmental impact," within the meaning of the act, cannot be reasonably construed to include a class of persons per se, and therefore the social and economic characteristics of the potential occupants of public housing are not decisive in determining whether an environmental impact statement is required under the act. The court also pointed to conflicting evidence given in the case on the subject, and expressed doubt as to whether psychological and sociological effects upon neighbors lend themselves to measurement.

Charting Course Through Conflicting Laws

One of the major contributions of the judiciary to Federal programs such as housing is the resolution of conflicting, or apparently conflicting, statutes applying to program operations. Such conflicting statutes can be of widely different types: different provisions in a single Federal enactment, in separate Federal statutes, in separate State statutes within the same or different States, or in a Federal and a State statute. One of the best examples involves the separate sovereign powers of the State and the Federal Government, as indicated below in two very recent decisions.

The case of *Charles Baker* v. *William Donovan*[52] dealt with the apparently conflicting statutes and regulations of the Federal Government and the State to fix rentals in a local public housing project financed by the Federal Government. Tenants in a public housing project of the City of Newport, R.I., whose rentals were being adjusted upward with their incomes in accordance with usual procedures under contracts pursuant to the U.S. Housing Act of 1937, claimed that such action violated a State rent-freeze statute. It was alleged especially that the rent increase violated a provision of the State statute specifically prohibiting a housing authority from increasing any rental on the basis of an increase in family income for a period of one year after such increase in income. The State law also said that the statute should apply only where not inconsistent with the U.S. Housing Act of 1937 and regulations thereunder. However, the applicable Federal contract provided that income limits and rents fixed by the local housing authority must meet the requirements of local laws. It was also contended that the Federal statute was silent on the specific time when rent increases were to take effect, and therefore the State law, which was specific on the matter, should prevail.

The Supreme Court of Rhode Island held that the rent increases in accordance with Federal law were valid, and that the State rent-freeze provisions did not prevail. It was found that silence in the Federal statute on the specific time of the rent increase was not controlling, as the court would look to the entire statute to determine its intent, and the core of its philosophy was the adjustment of rentals to incomes, both in cases of increases and decreases. It was unreasonable, said the court, to ascribe "to the Federal lawmakers an intention to allow their own work to be rendered inefficacious and nugatory by state law."

The case of *Housing Authority of the City of New Haven* v. *Dorsey*[53] dealt with an alleged conflict of State and Federal law concerning tenants in a public housing project serving on the board of commissioners of a local housing authority. The commissioners constituted the governing body of the housing authority in the case. It had been created by the city pursuant to State law, and owned and managed the public housing project.

The State attorney general had ruled that two public housing tenants serving as commissioners of the housing authority were holding office in violation of a State statute prohibiting such commissioners from "acquiring any inter-

[51] *Nucleus of Chicago Homeowners Association et al.* v. *James Lynn,* (U.S.D.C., Northern District of Illinois, Eastern Division, No. 72-C.1197) (1973)

[52] *Charles Baker et al.* v. *William Donovan,* Supreme Court of Rhode Island (No. 1645-appeal) (1973)

[53] *Housing Authority of the City of New Haven et al.* v. *Donald Dorsey, Commissioner, Department of Community Affairs et al.,* 288 Atl. 2nd 446 (1972), *certiorari denied by* Supreme Court of United States (41 L.W. 3661; Also 42 L.W. 3010 and 3306)

est, direct or indirect, in any housing project." Those commissioners claimed that Federal law and regulation required that public housing tenants be made eligible to serve as commissioners and that under the doctrine of Federal supremacy, the Connecticut law must bow to Federal statutes and contracts, citing a 1970 amendment to the U.S. Housing Act of 1937:

> It is the sense of the Congress that no person should be barred from serving on the board of directors or similar governing body of a local public housing agency because of his tenancy in a low rent housing project.

The Supreme Court of Connecticut upheld the attorney general's position, relying on the State legislature's acquiescence in that position by not amending, at subsequent sessions the statute he interpreted. That court also pointed to the common law conflict of interest inherent in a commissioner acting on matters affecting his personal interest, such as establishing the amount of rentals for units in the project. The court held that the "sense of the Congress" provision did not make it mandatory that States permit tenants to be commissioners, pointing to another declaration in the U.S. Housing Act of 1937 that purports to "vest in the local public housing agencies the maximum amount of responsibility."

The Supreme Court of the United States denied certiorari in that case.[54]

Decisions Affecting Program Operations

This category is the least dramatic and perhaps the most pervasive of all. It is least dramatic because it does not necessarily deal with whether a program can go forward at all, or whether it does so with its broad scope or fairness, but only with the way in which it goes forward. It is the most pervasive category because of the countless constitutional and legal issues that may affect day-to-day operations. Further, while the impact of this category of judicial decisions is not necessarily dramatic, it may in some cases prove to be dramatic—to the extent of greatly delaying major projects, or adding significantly to program cost, or radically altering the direction of a program for better or worse.

Because of the virtually unlimited numbers of cases that affect program operations, the discussion under this category will be limited to a few examples relating to due process in evictions and rent increases, grievance procedures, relocation rights, freedom of information, and administrative actions.

[54] Ibid.

Tenant Due Process Rights: In the 1930's managers of low rent public housing projects were generally told by local public housing agency lawyers that evictions of tenants could be legally governed by the same procedures as those customarily governing evictions from private housing. That is to say, when a tenant was evicted for nonpayment of rent, or disturbing the peace of other tenants, or for other apparently good reasons, there was no need for formal notices, hearings, findings of fact, or other formal procedural safeguards associated with governmental action. The local public housing agency was considered to be acting in a "proprietary" rather than governmental capacity. Regardless of whether this advice was sound when given, it was followed for many years and seldom challenged. When procedural safeguards were applied to eviction proceedings, it was done as a matter of discretion rather than in recognition of tenants' rights.

More recently, judicial decisions have held that the tenants of public housing are entitled to governmental due process in eviction proceedings. In one case arising in New York,[55] the tenant was held to be entitled to a written statement of the charges against him, a copy of applicable rules and regulations, access to all information contained in a folder which might be relied on by the board hearing his case, the right to confront and cross examine those who supplied the information against him, an impartial hearing examiner, and a decision with findings of facts and reasons.

In other cases, the courts have extended some of the due process requirements applicable to public housing to governmentally subsidized private housing. Thus, a Federal district court in Massachusetts[56] extended to a tenant of a privately owned housing project assisted by a low-interest-rate loan under the National Housing Act (section 221 (d)(3)), and by partial local real estate tax abatement, the right to notice as to the grounds of his eviction, even though his lease had expired. The court also held that a landlord could not evict a tenant in retaliation for "organizing" other tenants, because that was a violation of the tenant's First Amendment rights. (However, a contrary decision[57] was reached very recently by a Federal district court in Idaho which held that a tenant in a section 236 project (with additional Federal rent supple-

[55] *Escalera* v. *New York City Housing Authority,* 425 Fed. 2d 853 (1970)

[56] See *McQueen* v. *Druker,* 317 Fed. Supp. 1122 (1970)

[57] *Nettie Potter et al.* v. *Payette Manor Apartments, HUD, et al.,* (U.S.D.C., District of Idaho, No. 73-105) (1974)

ment assistance) had no right to notice and an administrative hearing prior to a refusal to renew or a decision to terminate his lease.)

Decisions such as these assert values relating to fairness and other constitutional rights that can well be viewed both as desirable in themselves and as contributing to the betterment of the Federal housing programs. But it is also true that these values are served at some cost in money, time, and convenience to other tenants. It takes manpower, time, and money to comply with the added procedural safeguards, and doing so does change the way in which the programs work. In the two eviction cases cited, the record shows that there were grounds for urging more speedy eviction than is generally possible in a formal proceeding. There were charges against the several tenants in these cases—or against members of their families—that included narcotics law violations, statutory rape, frequent damage to leased property, and a pattern of repeated delinquency in paying rent. The very seriousness of such charges provides reasons both for speedy evictions, if the charges can quickly be proven, and for procedural safeguards, even though time-consuming, commensurate with the importance to the tenants of the assurance that they not be wrongly found to be at fault. It is understandable, then, that the courts are more likely to rule in favor of relatively formal hearings in these eviction cases and against formal hearings in the "rent increase" cases next discussed.

Due Process in Rent Increases: From the inception of the FHA rental housing program, FHA reserved power of control over rents as an incident of the exercise of its administrative discretion. Its concern was with the program as a whole—that is, how to obtain maximum production of good housing at fair and moderate rentals in the program as a whole. It was felt both by the Congress and the FHA during the 1930's that an attempt to impose rent controls through formal trial-type hearings, with full participation of tenants, would result in drastically lowered production of moderately priced housing aided by the FHA. Consistent with this view, rents were set initially on the basis of overall market conditions and estimated project costs, with consideration being given to keeping rents low while assuring a fair profit to the owners and a margin of income that would be useful in safeguarding the FHA insurance fund. Landlords were permitted to adjust rentals—as among individual units within a project—provided that the total rent roll was within an agreed-upon limit, instead of being told what the rent should be for each apartment. Also, rent increases were approved from time to time based on rising operating costs and taxes in the locality as a whole.

More detailed reviews of rentals for individual units were made when the FHA acted as agent for Federal rent control agencies during World War II, but these reviews were based on rent control laws rather than on the National Housing Act.

Some inroads have been made very recently, however, in the exemption of FHA rental housing from due process requirements for tenants objecting to rent increases. In the case of *Marshall* v. *Lynn,*[58] the Court of Appeals for the District of Columbia held that tenants in a section 221(d)(3) rental project (with the below-market interest rate subsidy) have rights to notice of a proposed increase in rentals and an opportunity to object in writing before the rents are increased. Although less than a formal hearing, that procedure puts private rental housing with subsidy assistance more on a par with public housing in the case of rent increases, as was done with respect to private subsidized housing in the case of eviction, as mentioned above.

In another case (*Tenants' Council of Tiber Island* v. *Lynn* [59]), the same court denied such due process rights to tenants in an FHA section 220 rental project, where no overt Government subsidy is given. The court made the distinction between section 221(d)(3), where "reasonable rentals" are required for the benefit of tenants, and the section 220 program, where rentals are not regulated for the benefit of tenants and the program is designed to provide housing to assist in eliminating slum conditions from urban renewal areas. Plaintiffs in this case have filed a petition for certiorari to the Court of Appeals for the District of Columbia. A Federal district court has held recently that even in a section 221 (d)(3) project, the tenants do not have a constitutional right to notice and hearing on rental increases *(Al Harlib* v. *Romney)*.[60]

Traditionally, the courts have held that the tenant does not have the same claim under the Constitution to participate in a hearing where the issue is rental levels in FHA housing as in one where the issue is eviction for good cause. Typi-

[58] *Elizabeh Marshall et al.* v. *James Lynn et al.*, United States Court of Appeals for the District of Columbia (No. 71-1786) (1973)

[59] *Tenants Council of Tiber Island et al.* v. *James Lynn et al.*, United States Court of Appeals for the District of Columbia (No. 71-1931) (1973)

[60] *Al Harlib et al.* v. *George Romney et al.*, (U.S.D.C. Northern District of Illinois, Eastern Division, No. 72C2550) (1973)

cal of the case law on this point is a recent decision by the U.S. Court of Appeals for the Second Circuit.[61] The court there stated:

> Congress has made clear not only in the statutory language §221(a) . . ., but in a relevant committee report that the purpose of the §221(d)(3) program was to promote "the construction of housing by private enterprise" . . . . By leaving rent control in such projects to a regulatory agreement between the Secretary and the mortgagor . . ., Congress indicated its belief that a mandatory provision for subjecting all rent increases in such projects to what would amount to a full-fledged public utility rate proceeding with the expense and delay necessarily incident thereto might well kill the goose "in solicitude for the eggs."

Turning to judicial review, the court also stated:

> It would be most unusual for Congress to subject to judicial review discretionary action by an agency in administering a contract which Congress authorized it to make. Other factors tending in the direction of nonreviewability are the managerial nature of the responsibilities confided to the FHA, . . . the need for expedition to achieve the Congressional objective, . . . and the quantity of appeals that would result if FHA authorizations to increase rents were held reviewable.

If the court is correct in its reference to "killing the goose," the judicial restraint exhibited in this decision and another decision [62] there cited, could make the difference between the survival of FHA rental housing programs during the mid-1970's and their gradual withering away.

Different considerations apply to rent increases in low rent public housing. Courts have held that "due process" requires public housing tenants to be given advance notice and an opportunity to file written objections prior to an across-the-board service charge or rent increase. While a full hearing is considered unduly burdensome, notice and an opportunity to be heard have been held necessary because the increases are "State actions" [63] under the Fourteenth Amendment.[64] The FHA cases have referred expressly to the fact that the FHA does not itself initiate proposed rent increases in privately owned housing that it aids. That is, the rent increases do not constitute State action, and the review by FHA involves the application of discretion to accomplish a number of purposes—including the encouragement of housing production—that are not limited to the achievement of low rents.

HUD Grievance Procedures: Because of the increasing constitutional rights of public housing tenants being recognized by the courts, HUD began to formalize those new rights in agency issuances in order to obtain uniformity on a national basis and assure equitable treatment. One of those issuances, which became involved immediately in litigation (*Joyce Thorpe* v. *Housing Authority of the City of Durham,* 1969 [65], said, in effect, that no tenant should be given notice to vacate without being told by the local housing authority the reasons for the eviction and given an opportunity to make such reply or explanation as he may wish. In that case, the Supreme Court upheld the validity of the issuance and found it to be mandatory on local housing authorities.

The basis of that Supreme Court decision is extremely important in terms of HUD's legal authority over the management of all public housing projects assisted under the U.S. Housing Act of 1937. The Court decided that the rulemaking power under section 8 of the act is an independent authority for HUD to regulate the management of public housing projects (whether existing or new) if the regulation is related to the purposes of the enabling legislation. Against the argument that this impairs the obligations of contracts already entered into between HUD and the local housing authorities, the Court held that the regulatory authority is supplementary and valid as applied in the case. That decision was reached notwithstanding language in the act that:

> It is the policy of the United States to vest in the local public housing agencies the maximum amount of responsiblity in the administration of the low-rent housing program . . . with due consideration to accomplishing the objectives of this Act while effecting economies.

As a result of the increasing rights that the courts afford tenants in public housing, and the resulting pressure from tenants' organizations, HUD developed comprehensive circulars on the subject which were issued in 1971 after much discussion and clearance with organizations of local housing authorities. Those circulars, known as Grievance Procedures, required that a tenant's lease recognize certain minimum rights and obligations, and established safeguards for the settling of a tenant's grievances, including the right to an administrative hearing before an impartial board or official on any alleged violation

[61] *Langevin* v. *Chenango Court, Inc.*, 447 Fed. 2d 296 (1971)

[62] *Hahn* v. *Gottlieb*, 430 Fed. 2d 1243 (1970)

[63] See *Burr* v. *New Rochelle Municipal Housing Authority*, 347 Fed. Supp. 1202 (1972); 479 Fed. 2d 1165 (1973)

[64] *Thompson et al.* v. *Washington, Lynn, National Capital Housing Authority, et al.*, United States Court of Appeals for the District of Columbia (No. 71-2049) (1973)

[65] *Joyce Thorpe* v. *Housing Authority of the City of Durham*, 393 U.S. 268 (1969)

of rules by him. The decision of the board was to be final unless changed by court action.

Notwithstanding the *Thorpe* decision, the circulars were soon subjected to strong attack in the Congress and in the courts by a relatively small group of local housing authorities. They claimed that the circulars were unconstitutional, and were unauthorized because of the statutory language quoted above.

In *Housing Authority of the City of Omaha, Nebraska* v. *United States Housing Authority,*[66] a U.S. district court enjoined the application of the above procedures on the petition of several local housing authorities. The Court of Appeals of the Eighth Circuit reversed the district court, and the Supreme Court of the United States denied certiorari. The court of appeals decision relied on the *Thorpe* decision, emphasizing HUD's rulemaking powers and its duty to supervise local housing authorities and police its contracts with them to assure compliance with the authorizing statute.

Relocation Rights and Payments: With regard to the requirement in the urban renewal law that there be, or that there is being provided, adequate replacement housing for families displaced by urban renewal activities, there was a tendency for many years on the part of Federal urban renewal officials and the courts to take at face value assurances by local urban renewal agencies that this requirement was being met. Unfortunately, many local renewal officials tended to rely on the availability to urban renewal displacees of housing that was also being relied on to serve the needs of many others being displaced by other public or private actions.

Understandably, dissatisfaction with this state of affairs led to widespread litigation and a line of cases (a leading case being *Western Addition Community Organization* v. *Weaver*[67]) holding that persons displaced or about to be displaced from an urban renewal project have legal standing to challenge the viability and adequacy of the local relocation plan. The immediate effect of these decisions was, of course, to provide benefits and avoid hardships in accordance with the intent of the law as enacted.

More important, however, was the strong reinforcement that these decisions gave to a change already taking place in the general direction of the program as a whole. That is, large clearance projects involving widespread dislocation of residents were far less likely than before to even be considered or planned, let alone undertaken.

Until a few years ago, it had been the policy of the HHFA and HUD to recommend, and the Congress to enact, provisions that required 100 percent of the cost of relocation payments to be paid by the Federal Government to families displaced under HUD development programs, instead of a percentage representing the Federal share, as in the case of grants, for the development project. This was done solely because of State court decisions which raised serious questions as to whether State agencies could pay any portion of the cost of relocation payments in view of the State constitutional restrictions in almost all States prohibiting the lending of public funds or credit of the State or its political subdivisions to, or in aid of, individuals or corporations. The above policy has changed in view of more recent court decisions, and accepted practices of State payments to individuals, which promote general welfare.

Freedom of Information: Courts have clarified somewhat the very troublesome area of "Freedom of Information" which is now largely (but not entirely) controlled by the Freedom of Information Act (5 U.S.C. Sec. 552). In *Charles River Park "A" Inc.* v. *HUD*[68] the court held the act neither required nor precluded disclosure of a confidential financial statement filed with HUD by a builder under an insured mortgage. The court held the applicable law rather to be 18 U.S.C., section 1905, which makes it unlawful for a United States employee to disclose confidential data—that is, information the disclosure of which could injure the person submitting it by affecting his competition with others. There had been some uncertainty on this point among those in the executive branch principally responsible for administering the act.

In another recent case, *Stokes* v. *Brennan,*[69] the court held that a manual of the Department of Labor for instructing compliance officers was not an "interagency" memorandum exempt from the Freedom of Information Act requirements and had to be released as the act prescribed.

Administrative Actions: Two principal factors act as at least partial barriers against judicial interference with administrative actions in

[66] *Housing Authority of the City of Omaha, Nebraska* v. *United States Housing Authority, etc.*, 468 Fed. 2d 1 (1972); *certiorari denied* 35 Law Edition 2nd 558 (February 20, 1973)

[67] *Western Addition Community Organization* v. *Weaver*, 294 Fed. Supp. 443 (1968)

[68] *Charles River Park "A" Inc.* v. *HUD*. 360 Fed. Supp. 212 (1973)

[69] *Stokes* v. *Brennan*, 41 L.W. 2580. United States Court of Appeals, April 3, 1973.

housing programs: (1) The broad discretion generally conferred upon the program administrators by the terms of the authorizing statute; and (2) the cardinal rule of judicial restraint applied in decisions on administrative actions generally, and repeated in hundreds of decisions, that a court will not substitute its policy judgment for that of an executive official carrying out a statutory function in the absence of fraud or clearly arbitrary or capricious conduct. Notwithstanding that latitude, administrative action in a housing program can depart from congressional intent to the point where a court will hold the action illegal, even though the authorizing statutory language may seem sufficiently broad and no consitituional problem exists. Such a court decision can have a major impact on an entire program, as did the recent case of *Fletcher* v. *Housing Authority of Louisville.*[70]

In that case, a Federal court of appeals held invalid a local housing authority's rent range formula which was based upon a HUD general circular. The formula established a fixed percentage of the local authority's public housing units to be rented at each of four ranges of dollar rentals, regardless of the status of the waiting list of applicants. Those percentages were supposed to correspond to the percentage of persons in each rental group in the city eligible to apply for the housing. The whole purpose of the formula was to increase project revenue and reduce the need for operating subsidies from HUD, in accordance with the HUD circular.

The court held the formula to constitute an abuse of discretion because it was contrary, in two ways, to the basic intent and purpose of the U.S. Housing Act of 1937. First, the formula was geared to the wrong group—those eligible to apply for occupancy—while the relevant pools to be compared among the four rental ranges were those who expressed an interest in the housing —i.e., those who actually applied for it. Granting automatic priority to higher income applicants who might or might not apply in the future was held discriminatory. Second, the court said the formula imposed a significant penalty on the eligible applicants who had been on the waiting list for public housing for many months. From their positions in line, they had been abruptly moved behind others with no greater housing need and with a later application date simply because the latter could afford to pay more rent. The court found that the formula was, in effect, mandated by the HUD circular and was adopted for no other apparent reason.

In holding the formula contrary to the intent of the 1937 act, the court cited its provisions on admission policy which required that each local public housing agency give full consideration to, among other things, the applicant's "urgency of housing need." The court also relied on several amendments of the act designed to assist in bringing public housing to lower income families, including the Brooke Amendments to restrict certain individual rental amounts and to provide operating subsidies for projects where needed. The formula not only ignored the housing needs of applicants, said the court, but actually discriminated against those in greatest need. The court recognized the validity of adjusting rentals to income for reasons of equity and to increase revenue, but concluded that "tenant admission policies which discriminate against applicants because of their poverty are no longer justified."

The impact of court decisions relating to individual administrative actions by an agency can range from minor to monumental. The most extensive litigation on such actions by a housing agency in a single situation has been that involving the efforts of the Federal Home Loan Bank Board to correct alleged abuses by the Long Beach Federal Savings and Loan Association. (See *John Fahey* v. *Paul Mallonee; Federal Home Loan Bank Board* v. *Paul Mallonne;* and *Federal Home Loan Bank Board* v. *Long Beach Federal Savings and Loan Association*[71].) The Board initiated an administrative hearing that was challenged in the courts, and in an action several years later took over the assets and operation of the association. This engaged the courts, the Board, and even congressional committees in extended and bitter controversy. About a score of independent judicial actions were brought over a period of about 15 years, involving numerous parties and interveners and a litigation expense which apparently was shocking to the courts. The Supreme Court, in the case of *John Fahey* v. *Paul Mallonee,* supra, upheld the constitutionality of the provision in the Home Owners Loan Act (sec. 5(d)) authorizing the Board to regulate savings and loan associations and appoint a conservator to take charge of an association and hold a hearing thereafter as attempted in the case. However, because of their sheer volume and complexity, the multitude of

[70] *Mary Fletcher et al.* v. *Housing Authority of Louisville, HUD, et al.*, United States Court of Appeals, 6th Circuit (No. 73-1466) (1974)

[71] *John Fahey* v. *Paul Mallonee,* 332 U.S. 245 (1946); *Federal Home Loan Bank Board* v. *Long Beach Federal Savings and Loan Association,* 295 Fed. 2d 403 (1961); *Federal Home Loan Bank Board* v. *Paul Mallonee,* 196 Fed. 2d 336 (1952)

related actions and issues in the litigation through the years cannot be reviewed here.

Impact of Administrative Actions or Policy Decisions

The basic policies that shape and guide Federal programs, including those in housing and urban development, are largely determined by enabling legislation, as interpreted in the light of its legislative history and modified from time to time by budgetary and other limitations imposed by the Congress during the consideration of appropriation and other funding legislation. Nevertheless, the history of the programs is replete with examples of major policy decisions traceable to the exercise of administrative discretion, rather than to statutory mandates or even influences.

A major occasion for the conscious exercise of administrative discretion presents itself when regulations, rules, and procedures are first drawn in order to implement new enabling legislation. Many other occasions for adopting new policies or modifying old ones by conscious decision occur later, as experience is gained in administering programs, or as surrounding circumstances change. These occasions may generate amendments to regulations, rules, and procedures, or the issuance of supplementary circulars, notices, or interpretations to field and other operating officials. Still other changes in policy or prescribed practice (sometimes of great importance) are made—whether consciously or unconsciously—as a result of the cumulative effect of day-to-day decisions in individual cases. Over time, such decisions may well give formal effect to major changes in program direction or emphasis, and also may well lead to yet other major changes thereafter.

The regulations, manuals of procedure,. circulars, and other guidelines embodying the administrative rules to govern Federal housing programs are enormously voluminous, and much of the material is complex or highly technical. Any sort of general critique or analysis of such an extensive subject matter would be a project far beyond the boundaries of reasonable time, length, or cost.

It is possible, however, to illustrate with a limited number of examples the fact that policy decisions made in the exercise of administrative discretion may have effects as far-reaching, as basic, and sometimes even more unexpected than legislative enactments. Indeed, they share with basic court decisions both their unpredictable nature in the first instance, and the fact that their effects may extend far beyond what was readily perceived at the time they were made.

A number of examples have been chosen for this purpose. These decisions were utterly different in kind, scope, and effect, but they may be thought to have several things in common:

- Their consequences continued long after their original intended effects;
- They affected in important ways not only the particular circumstances they were intended to clarify or resolve, but also had much broader effects, often extending to the whole of the housing industry and the public as well;
- They played roles in the nation's evolving efforts to deal with its housing and urban development problems analogous to, and perhaps as significant as, major departures undertaken contemporaneously by the legislature and by the courts—and indeed had their own impacts on these.

Organizing the Government's Housing Agencies

The first organization of the Government's housing agencies was accomplished through administrative rather than legislative action. On February 24, 1942, President Roosevelt mildly surprised the country in general, but astounded the numerous housing agencies throughout the Government, by combining them into a new National Housing Agency, headed by an Administrator. This was accomplished by the issuance of Executive Order 9070 of that date.

The President's action came as a total surprise to the housing industry, and to those who were carrying out Federal housing programs in many departments and agencies of the Federal Government. The move was made under his emergency war powers, which did not require any expression of findings and reasons in a special message (as was the case with later actions under the Reorganization Act), and none were offered. It was simply said that the new Agency was being set up to help coordinate and expedite the production of housing, which was urgently needed to support the defense effort.

The new Agency fufilled this basic function very effectively, not only carrying out a number of programs for the direct production of defense housing, and for the use of existing federally owned or aided housing for defense-related purposes, but serving as the mechansim under the Government's priorities system for determining the housing that could be constructed and could receive scarce materials such as lumber, copper, and the like. However, it did something else: It brought quite a new institutional identification to the role of the Federal Government in regard to housing and problems related to housing.

Establishment of a Permanent Agency: In 1946, with the war over and the prospect that the war emergency would end in the near future, it was obvious that some action had to be taken, since the legal authority for the very existence of the National Housing Agency would end whenever the formal termination of the state of emergency might legally occur. A Presidential Reorganization Plan was proposed under the Reorganization Act which would have made the National Housing Agency a permanent agency of the Government. The Congress, however, rejected this plan by preventing it from taking effect. The rejection was effected on not altogether substantive grounds, though certain elements of the plan were found objectionable. (The late Senator Taft, undoubtedly the most influential single member of the Congress on this issue, made it clear that his opposition was mainly due to the fact that certain assurances he believed had been given him as to what would be proposed had not been faithfully adhered to in the plan as presented, and that he had not been consulted about these matters.)

In the following year, the President again submitted a Reorganization Plan—No. 3 of 1947—which provided for the establishment of a permanent agency in similar form, but under a new name—the Housing and Home Finance Agency. For obvious reasons, the plan was drawn with some care to meet the objections that had been made to the unsuccessful plan of the previous year. This time the Congress permitted the plan to become effective, and the Federal Government's first permanent housing agency as such came into existence.

It is worth pausing here to note that, in spite of the spirited debate that accompanied the consideration of the Reorganization Plan, there was not a great deal of choice actually open to the Congress. The basic facts were that the National Housing Agency did, in fact, exist; that some mechanism for carrying out the Government's housing programs had to be provided for; and that the legal basis for NHA might soon expire. In other words, the real choices presented to the Congress were three:

First, to approve—which assured at least continuity;

Second, to disapprove—which meant chaos, since the constituent elements of NHA would have suddenly flown apart and reverted to their status 5 years earlier, although, in the meantime, programs, personalities, organization, and relationships within and between Government and the housing industry had greatly changed.

Third, to reject the plan and substitute for it a legislative solution, which would have meant a protracted period of conceptualization and proposal, hearings, drafting and enactment—quite possibly without a result all that materially differet from the plan before them.

Faced with these available courses, Congress took the first, though not without some protest and complaint.

The Veterans Housing Program: It may be worth digressing here for a moment to record the early history of the placement of the veterans housing program under the GI bill in the Veterans Administration, rather than in the Government's housing agency—at that time, the NHA.

It was obvious to the Administration and to the Congress well before the war ended that the release of millions of veterans into civilian life would create a major housing problem as they married and sought places to live and raise families. It thus seemed natural to propose that the Federal Government should set up a special program to extend housing assistance to these veterans, to be carried out by NHA.

The then-Administrator of NHA, however, strongly objected to this approach—not so much in terms of the program itself, as its placement in NHA. He foresaw (quite correctly) that the problems of returning veterans would not be confined to housing, but would extend to many other areas—lost educational opportunities, problems of disability, special medical care, and many others. He therefore argued that it would be better to center all these matters in a single agency focused on veterans, rather than for NHA to take on singlehanded the housing element of the total problem. In the end, his view prevailed, and ever since, the Veterans Administration has been engaged in major housing programs involving grants, loans, insurance, and guaranties, as well as property acquisition, management, and disposal on a scale comparable to those of NHA, HHFA, and later HUD.

Whether this was a right or a wrong judgment is not our concern here. The point of this digression is that in the first instance it would almost undoubtedly have been entirely feasible to place the special Federal housing program for veterans in the Government's housing agency. Later, although such a change was often proposed and discussed as a theoretical matter, housing benefits had become so identified—psychologically and politically—with the whole fabric of veterans benefits generally, that it was no longer possible for it to be seriously entertained.

Growth of HHFA Functions and Responsibilities: The mere existence of a single agency in the executive branch responsible for the principal housing programs of the Federal Government exerted an influence in itself on both the Executive and the Congress. Thus, in the years after its establishment, its responsibilities were repeatedly extended—to slum clearance and urban redevelopment in 1949; to a greatly expanded public housing program in the same year; to certain community facilities and to operations in the secondary market for housing mortgages in 1950; to urban renewal in 1954; and to many other housing and urban problems in these and other years. It is idle to speculate what might have happened if such an agency had not existed; to suppose that the same things would have happened seems improbable in the extreme.

It does not seem a forced reading of the history to say that HHFA advanced legislative proposals at least in part because it existed as an agency that worked with the problems, and was in a position to propose approaches for dealing with them. Conversely, Congress accepted such proposals—or modified them, or originated approaches of its own—partly because there existed an agency that could be given responsibility for carrying them out.

Establishment of the Department: Prior to the establishment of NHA, references in the literature to the possibility of a Cabinet Department for housing and urban affairs did occur, but only rarely and mainly in a conjectural or theoretical vein. After the establishment of HHFA, however, this idea began to emerge with repeated and growing attention. The history of the idea and its realization in the Department of Housing and Urban Development Act of 1965 is worthy of study in and for itself. For the purposes of this account, it is sufficient to note that it came less than 20 years after the establishment of HHFA as a permanent part of the executive branch—an action that had itself been rendered virtually inevitable by the reorganization of 1942.

That measure, of course, did not end this story. The Congress has now had before it a proposal from the President for a still broader Department of Community Development (to include housing) to take the place of HUD. The fate of that proposal still remains to be seen. But whatever it may be, it seems clearly to be true that in the area of housing and urban problems the grand design that has unfolded, and is still unfolding, has been molded and shaped in critical degree by that original administrative decision in 1942 to establish a National Housing Agency for a purpose that was not only limited but temporary in nature—i.e., to help focus housing programs in support of the war effort, which at that time was at the heart of the country's attention.

Equal Opportunity in Housing

The assertion and protection of basic constitutional rights are not necessarily the exclusive domain of the legislative and judicial authorities. They can be both the substance and the result of a purely administrative action. In the field of housing, this could hardly be better illustrated than by the issuance of Executive Order 11063 on equal opportunity in housing by President Kennedy on November 20, 1962.

That order was the major administrative action of the Federal Government with respect to preventing discrimination in the sale, rental, or use of housing. It was also one of the milestones in the progress of civil rights during the last two decades, and one of the first and most significant steps taken administratively in the entire field of civil rights. It had long range as well as immediate effects.

The new order was entirely the product of administrative, rather than legislative, developments. No housing legislation had directed or contemplated such action. On the contrary, during consideration of some housing legislation in earlier Congresses, there had been occasional attempts to obtain antidiscrimination amendments—all of which had been unsuccessful.

Clearly, however, the order had major public and political support that reflected a growing interest and demand for some such action in this area. These coincided with a changing climate on all civil rights matters after the United States Supreme Court decision in *Brown* v. *Board of Education* and subsequent judicial actions, discussed earlier.

During his election campaign in 1960, President Kennedy had promised an Executive order against housing discrimination if he were elected. Civil rights organizations and the U.S. Commission on Civil Rights had pressed hard for either Federal executive or legislative measures that would prevent discrimination in all housing and related activities. However, specific steps—or even policy statements—on the subject by the executive branch had been rare prior to Executive Order 11063. The only effective executive action had been the significant (but very narrow) Executive order of President Truman directing the elimination of discrimination in the armed services, including discrimination in military housing.

As a candidate, Senator Kennedy had spoken confidently—almost casually—of abolishing discrimination with "a stroke of the pen." Undoubtedly, many people understood this to mean that he would take such action almost as soon as he took his seat in the Oval Office. The phrase itself was to haunt him, as those who were pursuing minority rights asked the question: What was inhibiting the Presidential pen?

As President, Kennedy quickly learned that he had not only many other and more pressing obligations, but that the matter of ending discrimination was far more complex than he had made it sound. Thus, it was 2 years after his election, and more than 1½ years after he took office that he finally put pen to Executive Order 11063.

Although the order constituted administrative rather than legislative action, careful attention was given by the Federal officials involved in developing and drafting it to the constitutional and general statutory authorities considered relevant. That was necessary because those authorities, as the drafting officials then saw them, were not sufficient to permit the order to cover as much of the country's housing as many people desired. Accordingly, the specific provisions of the order were carefully tailored to cover as much housing as possible without entering areas where it might fail for lack of underlying authority. Its provisions reflected extensive legal research and meetings on the subject by representatives of involved Federal agencies, as well as ultimate concurrence by the President.

The basic portion of the order (as thus developed and issued) directed all Federal departments and agencies to take appropriate action to prevent discrimination in the sale, rental, or use of residential property and related facilities (including land to be developed for residential use) if:

1. Owned or operated by the Federal Government;

2. thereafter provided through grants, loans, or contributions by the Federal Government;

3. provided by loans thereafter insured, guaranteed, or otherwise secured by the credit of the Federal Government; or

4. located in federally assisted urban renewal areas, where the loan and grant contract was executed after the effective date of the order.

The order covered lending practices of lending institutions with respect to residential property and related facilities insofar as such practices related to loans thereafter insured or guaranteed by the Federal Government. (Another portion of the order established the President's Committee on Equal Opportunity in Housing, which had no regulatory authority, but recommended general policies and procedures to implement the order and to promote coordination of agency activities under it. The Committee consisted of the Secretaries of Treasury, Defense, and Agriculture, the Attorney General, the Housing and Home Finance Administrator, the Administrator of Veterans Affairs, the Chairman of the Federal Home Loan Bank Board, a member of the staff of the Executive Office of the President who acted as chairman, and members selected by the President from the general public.)

These basic provisions of the order rested primarily on two legal bases: (1) The constitutional authority of the President to direct the exercise of discretionary authority of departments and agencies of the Federal Government; and (2) the broad statutory powers, which each of the affected agencies had, to issue regulations to further the purposes of the programs it administered. (The possible application of the Civil Rights Act of 1866 to antidiscrimination measures relating to housing was not then a factor. The pioneering decision of *Jones* v. *Mayer Co.* (392 U.S. 409), so applying that act, was not rendered until June 17, 1968.)

To bolster the application of that broad, general regulatory authority to the Executive order, its preamble stated that:

> . . . the granting of Federal assistance for the provision, rehabilitation, or operation of housing and related fa-

cilities from which Americans are excluded because of their race, color, creed, or national origin is unfair, unjust, and inconsistent with public policy of the United States as manifested in its Constitution and laws; . . .

and

. . . the executive branch of the Government, in faithfully executing the laws of the United States which authorize Federal financial assistance, directly or indirectly, for the provision, rehabilitation, and operation of housing and related facilities, is charged with an obligation and duty to assure that those laws are fairly administered and that benefits thereunder are made available to all Americans without regard to their race, color, creed, or national origin.

Notwithstanding the importance and historical significance of Executive Order 11063, it was at that time and in those circumstances limited in terms of the volume of housing it covered. The scope and meaning of the order (as well as its limitations) can be understood best by viewing the categories of housing and related activities excluded from it, and the reasons therefor.

Conventionally Financed Housing: The most important category of housing excluded from the order was conventionally financed housing—that is, housing being built or sold without FHA or VA mortgage insurance or guaranty, or other comparable direct Federal financial aid. Consequently, the bulk of the Nation's housing was actually not covered. That fact not only greatly limited the effectiveness of the order, but made it applicable to housing developers in an unequal manner. Those using FHA insurance or other Government financial assistance contended that the burden of compliance would cause many to shift to conventional financing—which would deprive consumers of the protections afforded them in connection with Government insurance or other aid.

Consideration of whether to exclude conventionally financed housing from the order raised what was probably the most difficult single legal question in connection with the drafting of the order.

Almost all housing built in the country could have been covered if the order could have been extended to all housing assisted by loans from private institutions that received financial aid or supervision, in any form, from the Federal Government. Thus, the Federal Deposit Insurance Corporation insured the deposits in all but an inconsequential number of commercial banks, and the Federal Savings and Loan Insurance Corporation insured the share accounts in all Federal savings and loan associations and many State chartered associations. These Federal associations were also chartered by the Federal Home Loan Bank Board. National banks were supervised by the Comptroller of the Currency.

It was contended by some that all of those Federal agencies and officials could and should be required to issue regulations prohibiting assisted private lenders from: (a) Discriminatory practices in making housing loans; and (b) from making housing loans without requiring the borrowers to comply with antidiscrimination requirements concerning the sale, rental, and use of the housing assisted. It was argued that legal authority existed for such action, especially in the cases of the FDIC and FHLBB, because they were created with a principal purpose of facilitating community credit, of which housing credit was a major aspect.

The order as finally written, however, did not invoke this regulatory authority because of substantial doubt as to its legality for the purposes of preventing racial discrimination. That doubt was expressed by the Department of Justice, on the basis that the statutory provisions conferring regulatory authority on the FDIC and the FHLBB were intended to apply only to the financial solvency of the private lenders and to related credit objectives. That limited scope was contrasted with the regulatory authorities of Federal housing agencies, which were intended to be used to carry out any of the objectives of their housing programs. Fairness in the sale, rental, and use of housing was determined to be one of those objectives.

As matters developed, and because of the overall importance of the order in the context of other equal opportunity developments in housing, the exclusion of conventionally financed housing did not greatly detract from its positive value or long term effect. Indeed, it was never shown conclusively that the exclusion resulted in any substantial shift by housing developers from FHA insurance to conventional housing, despite the gloomy predictions of its detractors.

Existing Housing: Even within the category of Government-assisted housing, there was a further limitation. The order was made inapplicable to that housing that had received the Government assistance prior to the order (as indicated above with respect to the specific categories of housing covered). That action also was taken because of serious doubts concerning the Government's legal authority to apply the new requirements more broadly. The basic authority for the order derived from the nature of the regulatory authorities of the agencies involved—which, it was determined, could not constitutionally be made retroactive to housing already subject to those regulations in effect at some prior time, when the mortgage insurance or other Government aid was provided. (Arguments were also advanced that FHA general regulatory controls, such as its holding of controlling stock in many of the sponsor corporations, were adequate for the purpose, but after much study their language or context was considered to preclude that interpretation.)

With respect to such existing housing and related facilities, the order simply required each agency to use its "good offices," and to take other appropriate action permitted by law to prevent discriminatory practices in connection with residential property and related facilities. That amounted to little more than a direction to seek voluntary compliance by builders and sellers of housing through persuasion or incentives.

The exclusion of housing with prior Government assistance was very significant as it affected the low rent public housing program (which at the time had about 500,000 dwelling units) and the FHA multifamily mortgage insurance programs.

One- and Two-Family Owner-Occupied Homes: This major category of Government assisted housing was not excluded by the terms of the order itself, but by FHA and VA, pursuant to authority given them by the order to exempt housing (not explicitly covered) where determined to be necessary or appropriate in the issuance of their implementing regulations. Such housing was not excluded for essential legal reasons, as the controls could have been applied to owner-occupied housing receiving mortgage insurance or other aid after the issuance of the order. The exclusion was made rather because of a strong political preference at the time not to burden individual homeowners with the requirements of the order. That policy was reflected, in ever decreasing degrees, in later equal opportunity actions affecting housing.

Executive Order 11063 initiated the substantial Federal actions on equal opportunity in housing, the later ones being essentially legislative or judicial rather than administrative. The latter soon overshadowed the order in scope and effectiveness, but may reasonably be viewed as extensions of it, which underlined its importance.

The Civil Rights Act of 1964 made the benefits of all Federal financial assistance programs available without regard to race, color, or national origin, and provided special enforcement machinery. The Government mortgage insurance and guarantee programs were excluded in recognition of the application to them of Executive Order 11063, but housing programs of grants or other subsidies for community facilities and other projects benefitting housing were covered by the act.

The enactment of title VIII of the Civil Rights Act of 1968 extended, in scheduled stages, the protection of civil rights to housing, so that by 1970 all dwellings were covered except a one-family owner-occupied house being sold or rented without a broker and without any discriminatory advertising. That act also broadly prohibited related discriminatory practices in lending, advertising, and other activities. It provided specific enforcement machinery through both judicial and executive means. (Action against violators under Executive Order 11063 is limited primarily to debarment from further program benefits, but that proved to be quite effective.)

Finally, on June 17, 1968, in the case of *Jones* v. *Mayer Co.* (392 U.S. 409), the United States Supreme Court held that the Civil Rights Act of 1866 prohibited (and still prohibits) racial discrimination in the sale or rental of any housing, holding also that the 1866 act and title VIII of the Civil Rights Act of 1968 stand independently and do not limit or impinge on each other.

Launching the Low Rent Housing Program

When new legislation is first implemented, it is not unusual for practical problems to arise that may not have been fully foreseen during the legislative process. These may result from defects in drafting, or simply from failure to visualize the difficulties that will be encountered in actual practice under the new law. In these circumstances, the administrators may be put to a choice between exercising a high degree of legal and administrative ingenuity, or taking the uncertain and time-consuming route of seeking amendatory or perfecting legislation.

Such was the situation when the low rent public housing program was launched under the U.S. Housing Act of 1937.

First, there was a critical problem arising from one of the principal limitations in that act—one that reflected a major issue during debate on the legislation. That was the provision limiting Federal loans to 90 percent of the cost of a low rent housing project. (At the time the 1937 act was under consideration, it was assumed by all concerned that the development of local public housing projects would be financed by direct Federal loans from the new USHA.)

During consideration of the act by the Congress, there was considerable discussion in both the Senate and the House over the percentage of capital cost of an assisted housing project that could be borne by a Federal loan. As first introduced, the Senate version of the legislation had no limitation on Federal lending. At one point an attempt was made to amend the pending legislation to require specifically that a local governing body obtaining Federal funds must contribute in cash or land to the capital cost of the project. The House version limited a loan to 85 percent of development cost.

In conference, a compromise was effected and the 90-percent limitation that resulted read as follows:

> Sec. 9. The Authority [United States Housing Authority] may make loans to public housing agencies to assist the development, acquisition, or administration of low-rent housing or slum-clearance projects by such agencies. Where capital grants are made pursuant to section 11 the total amount of such loans outstanding on any one project and in which the Authority participates shall not exceed the development or acquisition cost of such project less all such capital grants, but in no event shall said loans exceed 90 per centum of such cost. In the case of annual contributions in assistance of low rentals as provided in section 10 the total of such loans outstanding on any one project and in which the Authority participates shall not exceed 90 per centum of the development or acquisition cost of such project.

At that time, many if not most local communities lacked the resources to make cash or land donations equal to 10 percent of development cost. Others might have given up the idea of undertaking a housing project if a local capital contribution were required for Federal assistance. Thus, the requirement for local contributions of 10 percent virtually could have stopped the low rent public housing program at the outset.

Rather than reopening so sensitive a legislative issue, a financing arrangement that avoided the roadblock was developed administratively. First, it was determined that the 90-percent limitation applied to the Federal loan and did not prevent the remaining 10 percent from being borrowed from non-Federal sources. The Federal loan (or loan commitment) was in fact limited to 90 percent of project cost. Generally, short term notes backed by the Federal loan commitment were issued to private purchasers by the local housing authority to permit commencement of construction. On completion of construction and full accounting to establish project cost, the local housing authority sold, on the private market, long term bonds supported by the Government's binding commitment to make annual contributions. The bonds issued equaled 100 percent of project cost; accordingly, the 90-percent limitation was no longer a problem, since Federal loans were not involved. (This 90-percent limitation is no longer in the act, having been repealed in 1969 because of another financing problem that developed shortly before that time.)

Secondly, another provision of the act posed a serious problem in the launching of the low rent public housing program—the "equivalent elimination" requirement. The act provided, in effect, that, for every new dwelling unit constructed thereunder, the project must include the removal from use of one unsafe or unsanitary dwelling (except that certain deferral of removal was permitted). This statutory provision read:

> . . . no annual contributions shall be made, and the Authority shall enter into no contract guaranteeing any annual contribution in connection with the development of any low-rent housing or slum-clearance project involving the construction of new dwellings, unless the project includes the elimination by demolition, condemnation, and effective closing, or the compulsory repair or improvement of unsafe or insanitary dwellings situated in the locality or metropolitan area, substantially equal in number to the number of newly constructed dwellings provided by the project; except that such elimination may, in the discretion of the Authority, be deferred in any locality or metropolitan area where the shortage of decent, safe, or sanitary housing available to families of low income is so acute as to force dangerous overcrowding of such families.

This provision would have constituted a major obstacle to a large portion of the program if each assisted housing project had to include the removal from use of an unsafe or unsanitary dwelling as part of the physical housing development—or even if it had to include such removal by the local housing authority itself through any other direct means. Most low rent public housing projects were feasible only if constructed on vacant land, or land containing few such dwellings. Even in slum and blighted areas, the existing buildings on sites were more often commercial or industrial than residential. It would not have been feasible for the local authority to buy unsafe or unsanitary properties elsewhere solely to meet the equivalent elimination requirement, since it would have added so substantially to the cost of the project as to make it infeasible, and would have made the authority an offsite landlord if the dwellings were not demolished or sold.

This whole problem was solved administratively in a manner that avoided any project being actually thwarted by the equivalent elimination requirement. Under a liberal interpretation of the act, it was determined that the required removal of unsafe or unsanitary dwellings, in order to be "included" in the project, need not necessarily be accomplished within the project's physical boundaries, or as part of the physical development of the housing project, and need not even be accomplished by the local housing authority, if it obtained assurance that the removal would be accomplished within a reasonable time by some other local body that had adequate legal authority to do so. Typically, this other local body was the city, which had broad "police power" under which it could demolish, condemn, close, or force the repair or improvement of unsafe or unsanitary dwellings in the locality.

This administrative determination was first reflected in a portion of U.S. Housing Authority Bulletin No. 3 on policy and procedure, which provided:

> (b) Off Site Elimination. When the new dwellings are constructed on vacant sites or on sites occupied by relatively few unsafe or insanitary dwellings, arrangements must be made for the accomplishment of all or some of the necessary equivalent elimination elsewhere in the same locality or metropolitan area. Since the expense makes it impractical to buy the buildings to be so eliminated, the cooperation of others must be secured.

The assurance that others would furnish the necessary cooperation in eliminating unsafe and insanitary dwellings took the form of "Cooperation Agreements" between local public housing authorities and local governments. Under such an agreement, the local government undertook that, without cost to the local housing authority and generally through the use of the local government's police powers, it would cause the elimination of a number of unsafe and insanitary dwelling units substantially equal in number to the number of new units to be constructed in the public housing project.

Normally, the "equivalent elimination" language was included in a cooperation agreement which also provided for tax exemption, vacating of streets, zoning, and the furnishing of municipal services, but at times it was a separate agreement. The use of this device made necessary the enactment of State "Housing Cooperation Laws" (or the inclusion of provisions in State "Housing Authority Laws") giving cities power to enter into such agreements. These in turn led to court tests in which the power of the municipalities so to contract was upheld.

Initiating the use of the cooperation agreement to obtain equivalent elimination also had effects that extended beyond the requirements of the U.S. Housing Act of 1937. At that time, even though municipalities were empowered to force the demolition, closing, or repair of unsafe or insanitary dwellings constituting a threat to health and safety, the power had not been generally used. Many municipalities were actually unaware of their power to effectuate slum clearance through the use of the police powers, or lacked the incentive to enforce existing laws and municipal ordinances relating to such buildings. The hearings and debates in city councils during consideration of cooperation agreements brought these powers into greater focus and public attention, and made the municipalities more conscious both of their powers and the need to exercise them, and had the positive effect of encouraging the use of those powers far beyond, and quite independent of, the public housing program.

Launching the Slum Clearance and Urban Redevelopment Program

Legal interpretations and administrative policy decisions in the early days of a new program largely determine the general forms and approaches to its execution that will govern operations, often for years to come. An interesting case in point arose in the course of initial operations under the Slum Clearance and Community Development and Redevelopment Program—the initial designation of the slum clearance program authorized by title I of the Housing Act of 1949 (Public Law 81–171).

As always happens in the beginning with a complex new statute, a great many legal problems arose as the then Housing and Home Finance Agency began to prepare the new program for operation. One such question that came up quite early was a determination as to what would be required of a "local public agency" to qualify for planning advances, which were authorized in the act (along with loans and capital grants). The relevant language of the statute read:

> The [Housing and Home Finance] Administrator may make *advances of funds to local public agencies for surveys and plans in preparation of projects* which may be assisted under this title . . . etc. (Public Law 81–171, sec. 102(d)) (Emphasis added.)

HHFA attorneys ruled that this language, particularly taken in conjunction with the provision that such planning advances could be required to be repaid from funds later becoming available for "undertaking" projects, meant that there must be a project or projects in being before a planning advance could be made, together with some showing that such projects qualified for assistance under title I.

Since most of the local public agencies in the early period of the program's life were hardly older than the act itself, if as old, the practical effect of this ruling was that those that needed and sought planning advances—which, to all intents and purposes, meant all of them—were required to, in effect, pretend that they had "projects" in being, and that they knew enough about these putative projects to demonstrate their eligibility for title I assistance.

The fact was, of course, that both the program and the local agencies were so new that it was quite impossible (except in unusual local situations) for them to have such "projects," and this approach to initiating the planning process therefore resulted not only in lost time and in a great deal of agonizing and largely pro forma documentation at the local level, but had the more serious and lasting effect of encouraging decisions on project areas and concepts in excessive haste and with inadequate information, and even virtually freezing them in place because of the investment of time and effort—thus tending to build into the program in its very early stages mistakes of judgment that might have been avoided had the initial planning stage taken a more orderly course.

This was, of course, essentially a legal interpretation, but it was also an administrative decision. As has been noted repeatedly in these pages, lawyers who know precisely what policies and objectives are in the minds of the program administrators tend to view statutory grant of authority in a light favorable to their realization, when they can reasonably do so without doing violence to the statutory language or to clear congressional intent. There is little reason to think, therefore, that a determined program administrator, who clearly visualized the consequences of the alternative route, could not have prevailed upon the attorneys to take the view that the practical and necessary purpose of these advances was to make "surveys and plans" for the purpose of preparing projects—not then in existence or even identified—which would, on the basis of such planning and preparation, qualify for loan and grant assistance. This would have entailed a certain risk of loss where funds were used for planning and no project ever eventuated, but that would not have been an unreasonable risk to take. (As a matter of fact, this happened anyway, even under the stricter interpretation, and the Agency was finally authorized to use capital grant appropriations to write off uncollectable planning advances.) Had such an interpretation been made initially, the early years of the slum clearance and urban redevelopment program might have taken a different and, conceivably, a more useful course.

There is another consequence of this and similar decisions, however, that is worthy of note. Once the local public agencies were put on notice that they would have to meet some rather difficult and technical tests to even qualify for planning advances, they understandably began to besiege the Agency for information and guidance as to how they were expected to proceed. Unfortunately, however, the program administrators were as new and inexperienced as the local public agencies themselves, so that they had no choice but to improvise the best answers that they could as they went along.

Thus, there fairly quickly developed a somewhat incoherent system—if it can properly be called that—of program guidance to the local agencies through meetings, telephone calls, letters, circulars, visits, and so on. In the end, this generated enough confusion as to what the applicable standards and policies actually were that gradually a formal system of procedural directives was put together to serve as a channel of communication with the field offices and local agencies.

But by that time, a pattern had set in under which the Federal officials prescribed detailed forms, requirements, and submissions from local public agencies as a matter of course—notwithstanding that the theory of title I was that it should provide Federal assistance to programs essentially local in character, embodying local planning, priorities, and decisions. This pattern of administration was to endure for many years, and ultimately was to become one of the principal sources of local discontent with what was considered to be "bureaucratic interference" and "dictation" from Washington.

It would be an exaggeration, of course, to attribute this development entirely, or perhaps even mainly, to the initial Agency posture with respect to planning requirements. Many other problems and circumstances played a part in shaping the lines of communication in the direction they developed. Nevertheless, it is clear that if the Agency had initially taken a different and more step-by-step view of the planning process, it would have been far easier to satisfy the local agencies with very general directives, calling their attention to the provisions of the statute and emphasizing that project submissions, when ultimately ready, would basically be held to standards of reasonableness, feasibility, and faithfulness to the statutory objectives.

Thus, for example, a system might have evolved that would have relied much more heavily on local decisions, findings, and certifications, and subjected more to postaudit and less to prior review—an administrative approach to which the Agency (by then the Department) was compelled almost 20 years later by the sheer cumulative force of local and congressional exasperation.

Improving Techniques of Financing to Meet Changing Program Needs

At least twice in the history of the rural housing programs of the Farmers Home Administration (FmHA) administrative ingenuity and flexibility have been brought to bear to develop new financing techniques that enable FmHA to adjust to changing programs and rapidly rising workloads with a minimum loss of momentum and service to rural areas. In each case, the new systems were ultimately endorsed (and even modified and improved) by the Congress in amendatory legislation. However, major delays and program tieups were avoided by working out feasible solutions within then existing law.

Sale of Insured Loans at Market Prices: The first such case occurred in 1966 with the decision to sell insured rural housing loans at market value.

The Rural Housing Insurance Fund (RHIF) was established in 1965 by Public Law 89–117, and capitalized with an appropriation of $100 million. FmHA, through its 1,730 local offices, makes housing loans primarily with funds advanced from the RHIF. These loans in turn are sold to private investors, and insured at the time of sale. Proceeds from such sales are deposited in the Fund and are available for new loans, among other purposes.

Two events soon combined to make the $100 million capital of the RHIF inadequate. One was the increase in market interest rates above the level paid by borrowers, and the other was the rapid increase in the authorized levels of rural housing programs.

Until July 1, 1968, the interest rate to borrowers on insured housing loans was 5 percent. When market rates exceeded rates paid by borrowers, the insured housing loan program was stymied, because the Fund was unable to market the loans it held rapidly enough to provide the funds needed for new loans. Increased authorized program levels added to the problem. The FmHA, in order to avoid a situation in which the program might grind to a halt, decided to offer insured notes to investors at rates above the borrowers' note rates. The initial offering in March, 1966 was at 5.4 percent—a premium of .4 percent.

The practice of selling at above or below market interest rates was favorably received by Congress as a practical solution to a practical problem, and has been followed since 1966. The Fund is reimbursed for interest losses by annual appropriations.

The Block Sale Method: The second administrative innovation to meet the expanding financial requirements of the rural housing programs came a few years later, in 1970.

As the rural housing program increased in volume to $800 million in fiscal 1970 and to $1.4 billion in 1971, the old method of selling and transferring the individual notes to the investors became too cumbersome. Investors preferred holding one piece of paper, rather than a portfolio of individual notes. To improve the marketability of insured notes, the FmHA started the block sale method in February 1970.

Under the block sale method, investors were able to buy Insurance Contracts through underwriting firms in the capital markets in New York. These Insurance Contracts, which were issued in denominations ranging from $100,000 to $1,000,000, were evidence of ownership of specified insured notes held in custody by a bank acting as agent for the FmHA.

This method of sale, to supplement the direct sale of insured notes, enabled the FmHA to maintain the RHIF in a sufficiently liquid position to meet the needs of a $2 billion housing program.

The block sale method was further simplified and made more attractive to investors by language included in section 817 of P. L. 93–86. This new language provided that:

> No provision of law shall prohibit issuance by the Secretary of certificates evidencing beneficial ownership in a block of notes insured or guaranteed under this Act of Title V of the Housing Act of 1949; any sale by the Secretary of such certificates shall be treated as a sale of assets for the purposes of the Budget and Accounting Act of 1921. Any security representing beneficial ownership in a block of notes guaranteed or insured under this Act of Title V of the Housing Act of 1949 issued by a private entity shall be exempt from laws administered by the Securities and Exchange Commission, except sections 17, 22, and 24 of the Securities Act of 1933, as amended; however, the Secretary shall require (i) that the issuer place such notes in the

custody of an institution chartered by a Federal or State agency to act as trustee and (ii) that the issuer provide such periodic reports of sales as the Secretary deems necessary.

This authorization permitted further major improvements in the "block sale" method, to better adapt insured notes to the investment market and also reduce paperwork involved in the transactions.

Thus, these two administrative decisions to go ahead by making the best use of the tools at hand not only protected the rural housing program from what might have been protracted delays and serious breakdowns in program operations, but led in the end to legislation that endorsed and even strengthened the financing methods that had been devised and successfully tested in the market.

Establishment of FHA Minimum Property Standards

The original National Housing Act did not contain a single provision that expressly or implicitly required the FHA to establish detailed minimum property standards for housing financed with the aid of mortgage insurance. The act was entitled "An Act to encourage the improvement in housing standards and conditions, to provide a system of mutual mortgage insurance and for other purposes."

The reference to encouraging "improvement in housing standards and conditions" gives ample support to the idea that the imposition of detailed standards is consistent with the congressional intent, but it gives no valid support to a contention that such minimum property standards were required or specifically contemplated.

A reading of the act as a whole makes it clear that the improvement in housing standards and conditions referred to might just as well have been contemplated through the encouragement of an increased volume of repair and improvement of the existing housing stock. Indeed, it could have been argued that the imposition of detailed minimum property standards for each and every unit of new construction aided by mortgage insurance would not speed up but slow down the implementation of the program—so that resulting gains in the quality of individual units newly built would be offset by a reduction in the number of new units started, thus perhaps adversely affecting the quality of the housing supply as a whole.

Such a hypothetical argument against the imposition of detailed minimum property standards could have found some support in the legislative history. For example, the lead Administration witness on behalf of the legislation was Harry L. Hopkins, the Federal Emergency Relief Administrator. His testimony listed the major purposes of the legislation as follows:

1. To create employment in the building trades at a time when more than one-third of all the American families on the relief rolls were identified with the building trade.

2. To increase employment in industries that provided materials and equipment for the construction industry.

3. To increase repair work on the existing housing supply which had deteriorated greatly during the 4 years of depression.

4. To unloose private credit rather than public funds in both new construction and housing repair.

It seems reasonable to assume that a more immediate impact on unemployment in the building trades and in the manufacturing of materials and equipment used in housing would result if FHA mortgage insurance were made available to new housing that was acceptable to the market without the delays involved in devising, promulgating, and administering detailed property standards applicable to each unit of new construction. This is particularly true because the minimum property standards that were adopted applied not only to the size and general design of the structure, and the availability of water supply and sewage disposal facilities, but also to the quality of the numerous individual items of materials and equipment going into the housing.

Turning from the act's title and its legislative history to the body of the act, it is interesting to note that it contains many detailed requirements that run to the mortgage terms, while hardly any mention is made of the mortgaged property. Thus, the insured mortgage is governed as to its dollar amount, ratio of loan to value, maturity, amortization, and foreclosure rights. In the case of rental projects, there are specific provisions governing rents, charges, capital structure, and rate of return, but here again the law is silent as to physical construction standards. Thus there was no obligation either in law or legislative history to impose detailed minimum property standards.

On the other hand, the imposition of such standards was certainly within the discretionary authority of the Federal Housing Administrator. The authority to insure mortgages was granted "upon such terms as the Administrator may prescribe" and there was a requirement that each assisted project be "economically sound." An argument could readily be made that the economic soundness requirement in itself justified the imposition of detailed minimum property standards. And it is likely that concern with the economic soundness of each project (and more basic concern with the overall financial soundness of the mortgage insurance system) contributed heavily to the decsion to impose minimum property standards. These considerations were likely uppermost in the minds of the decisionmakers at the time.

There is no basis in the literature of the early 1930's for projecting back into that period the current degree of interest in Federal laws and regulations specifically designed to protect consumers against substandard products. This is not to say that consumer protection may not have been among the motives for adopting the detailed minimum property standards, but it was probably a secondary motive.

The imposition of detailed minimum property standards had several effects that were both contemplated and immediately visible. The occupant of an FHA-financed house received a product that was, or was purported to be, in many respects better than it otherwise would have been—i.e., settlement cracks and roof leaks would be fewer; insulation would be effective; mechanical equipment would last longer; and so forth. And accordingly, the security behind the mortgage was better, as well as more uniform in quality. But for present purposes, the indirect effects of the administrative decision to impose the property standards are of even greater interest. Thus, before long, it became apparent that FHA's minimum property standards were beginning to be applied to conventionally financed construction, so that the benefits reached many additional people.

There were several reasons for this spillover effect. Many builders produced homes or multifamily buildings for both the FHA and the conventional market, and it was more efficient to utilize similar materials and construction practices. In other cases, consistency resulted from habit or because of consumer demand.

Perhaps an even more important reason was related to the impact of FHA requirements on manufacturers and suppliers of materials and equipment. Thus, when the FHA established a minimum standard for an item of lumber or plumbing, the suppliers of that item tended to meet the minimum standard with respect to their entire production lines, so that conventionally financed housing received the benefit of this improved quality willy-nilly. In time, a finding of FHA acceptability became practically indispensable to the successful marketing of new materials and components.

Quite apart from the benefits of improved quality in both FHA-aided and conventional construction, there was a further benefit relating to efficiency within the home building industry and the industries that supplied construction materials and equipment. This benefit was traceable to the greater degree of uniformity and interchangeability in production and construction that resulted from the existence of Federal standards.

Still another indirect benefit was the impetus given to greater uniformity in local building codes, many of which incorporated FHA minimum standards for their own purposes.

It should be noted that these benefits were not limited to standards respecting individual structure. The FHA's activities in this area were eventually extended to the approval of entire systems of prefabricated housing construction. Minimum property standards also extended to such matters as the design of streets and curbs, utilities, and entire subdivisions.

Thus, the successive waves of secondary effects—few of which could have been fully anticipated at the time—were both wide and lasting. This is the more remarkable since the original decision had been made to achieve a rather specific and limited "economic soundness" objective that might quite reasonably have been sought without any recourse to detailed property standards.

Subdivision Requirements of Farmers Home Administration

Just as important administrative innovations often must be developed and applied as new programs are implemented, similar innovations may follow legislative expansion of a program into new or broader fields of activity. An example of this was the recent administrative development and issuance of comprehensive requirements for planned or existing subdivisions to be assisted under the rural housing program of the Farmers Home Administration. Those requirements filled a void in most areas where the program operates, and the FmHA, as a Federal lender in the home mortgage field, thus took the initiative in assuring adequate standards to protect the interests of the assisted homeowners, as well as those of the Government to the benefit of the general public.

The rural housing program of the FmHA, as initially authorized by title V of the Housing Act of 1949, had as its primary mission providing Federal financial assistance for farmhomes and service buildings, so that subdivision development requirements were not relevant. In accordance with the authority in title V, the FmHA at that time issued guidelines prescribing standards only with respect to housing and other buildings. These naturally dealt primarily with structural aspects of building planning and design, although there were references to related factors, such as water and waste disposal systems. Those guidelines were adequate as long as houses being built or improved were on farms or on scattered sites, and where the work was done under contract on a one-house-at-a-time basis.

The need for more comprehensive standards in the form of subdivision regulations became evident, however, when distinctly new types of activities and problems occurred under the program as it was gradually expanded beyond the original concept through a series of legislative amendments over a period of years.

In 1961, an amendment (P. L. 87–70) expanded the program to authorize loans to owners of nonfarm tracts in the open country and in rural towns with populations of not more than 2,500. This population limit was raised to 5,500 in 1965 (P. L. 89–117) and to 10,000 in 1970 (P. L. 91–609). Loan volume was quite small during the early years of the program, but had increased to $1.4 billion by fiscal year 1971 and to $2 billion in fiscal year 1973. The rapid increase in program levels, the authorization to issue conditional commitments to builders and developers of projects, and the introduction of an application packaging method by the agency attracted larger scale builders and developers, which made subdivision controls a necessary and important part of the program.

There was a special need for requiring compliance with subdivision regulations prescribed by the FmHA as a condition to financial assistance under the program, because most of the areas where it operates had no prior local subdivision standards whatsoever. Some rural communities had taken an active interest in zoning and land use regulations, and others had become concerned about building and sanitation codes. Except for a few scattered localities, however, little had been done to adopt and enforce subdivision requirements that met acceptable standards for water supply, waste disposal systems and utilities, street design and layout, lot size and arrangement, drainage, parking, and use of open space. Most rural towns had not been concerned about subdivision standards because large scale subdivisions had not been a part of their experience.

In 1970, the FmHA issued preliminary guidelines for building sites, and in 1973 released more comprehensive and specific controls applicable to both planned and existing subdivisions. By now, these requirements have gained general acceptance. However, resistance characterized the initial reaction of some builders and developers—especially those who had been developing low budget subdivisions with features such as individual wells and septic tanks, open ditch drainage, or minimal streets. Also, some local communities objected to the new standards because they often made it necessary to spend local funds for additional public facilities.

The impact of this administrative action by FmHA ultimately reached far beyond the scope of the program itself, and far beyond the specific administrative needs that led to it. For example, the FmHA subdivision standards:

1. Resulted in some communities installing, extending, or upgrading their water and waste disposal systems to accommodate not only the new subdivisions but the community as a whole.

2. Made many local leaders aware of the need to provide facilities and services essential to a good living environment if they expected their communities to grow and to attract the capital needed to do so.

3. Caused some planning and regulatory bodies to give more attention to subdivision development in rural areas.

4. Set the pattern for good, well designed subdivisions for builders, developers, and private lenders in rural areas.

Refusing Mortgage Insurance to Certain Neighborhoods (Red Lining)

Many administrative decisions—like that to establish FHA minimum property standards for the mortgage insurance system—are made at a definite time and on a specific point—a decision to do something or not to do it; or a decision to do something in a particular way or to do it in some other way. Others arise over time, or crystallize out of precedent and practice. An example of the latter is what came to be known as "red lining" in the FHA program.

The figure of speech arises from the image —in some offices perhaps quite literally true—of a map of a particular city in which certain neighborhoods or areas are encircled in red, with the understanding that no mortgage is to be insured on a property lying within the proscribed area. Such general area disqualifications did in fact occur, and they were, by and large, areas of slum and blight, largely occupied by low income people.

It is possible to suggest at least three reasons why this approach to underwriting—whether or not it involved actually drawing lines on a map—may have come into general use.

First, FHA may well have been influenced—and understandably—by the customs and practice of conventional mortgage lenders. This was due in part to the "economic soundness" policy in the statute itself, and a desire to show that FHA was gaging the quality of its insurance risks so as to carry out the congressional intent in this respect. In part, it was no doubt due to a feeling that it was important for FHA to establish itself in the minds of the business community and the public as a prudent and businesslike operation. Both considerations gave weight to the fact that conventional mortgage lenders had reached virtually unanimous, even if tacit, agreement that it was unwise to invest mortgage funds in these areas.

Second, the practice yielded a considerable administrative convenience and some economy. If it is known in advance that an application is almost certainly going to be rejected, there is little point in spending the time and effort necessary to process it in full. Automatic rejection of applications from undesirable areas, therefore, not only saved time and trouble, but in the end produced a further convenience: When it became known that such areas were out of bounds, mortgagees stopped even preparing applications in the first place, so that FHA was spared the workload of receiving and rejecting them.

Third, the FHA's own appraisal methods tended to produce this underwriting result. In the case of existing properties, the measure of choice in this type of appraisal was that of comparable recent sales of similar properties in the same or an essentially similar neighborhood. But a large proportion of this type of housing was in low income rental use and in most such so-called comparables were not available. In that situation, the appraisers turned to another method—capitalizing the income-producing power of the property. Since most slum housing is operated at relatively high rents and low expense for maintenance and repairs, it throws off a substantial return to the owner. Hence, the income capitalization method tends to produce an unreasonably high value, considered in the light of the actual physical condition of the structures, their amenities, and their surroundings. In other words, taking into account the incomes of prospective buyers (for ownership, as distinguished from investment), mortgage loans on such properties at those values would in fact very likely not have been economically sound in most cases.

Although the policy or practice of red lining put the FHA in a good light from the standpoint of its economic soundness test and its financial position, it had just the opposite effect in terms of the public and congressional perception of FHA's responsiveness to its status as a public agency. It was widely criticized as being interested only in the upper middle class, especially in the suburbs. As a matter of fact, it seems most unlikely that FHA actually had any reluctance to deal with any particular class or income stratum. The practical fact was the wealthy did not need FHA, and the poor were, in the main, ineligible to use it.

With the advent of the equal opportunity decisions of the courts (discussed earlier) and new legislation in this area, these criticisms grew progressively louder and more widespread. Then came the introduction of housing subsidies provided through the FHA machinery, under the rent supplement program and later under sections 235 and 236. Finally matters reached the point where large sections of the public were convinced that FHA was deliberately dragging its feet in carrying out these programs, and was discriminating against the poor in general and the minority poor in particular. As always, these public attitudes were quickly reflected in the Congress.

In the late 1960's, HUD and the FHA moved strongly to try to turn this situation around. Redlining as such was prohibited, and field offices were directed to give priority attention to the needs of low and moderate income people, including those in the central cities.

This administrative action was followed by congressional sanction in the Housing and Urban Development Act of 1968 which authorized: (1) The waiver or relaxation of FHA property standards to permit mortgage insurance for blighted areas in central cities; (2) the acceptance of certain mortgagors as eligible for insurance although their credit ratings are below usual FHA standards; and (3) the creation of a Special Risk Insurance Fund, for those and other insurance operations, with an authorization for appropriations to cover expected losses incurred by the Fund. (See sections 223(e), 237, and 238 of the National Housing Act.)

But the concept that this was to be accomplished with care and all reasonable prudence appears not to have gotten through to those involved in day-to-day operations as fully as the urgency of getting FHA off the hook of foot-dragging. Many field offices seem to have thought, perhaps with some reason, that their efficiency and performance were to be judged in large part by the volume of loans insured in once-forbidden areas. In any event, such loans began to be insured in considerable volume, not only under the subsidized programs but under the unsubsidized programs that offered favorable terms for low and moderate income people. The result was a host of new problems, equally serious although of an entirely different nature.

Foreclosures and property acquisitions on defaulted loans began to come in and rapidly swelled in volume. In great numbers of cases, poor homeowners faced with some unexpected financial problem or disillusioned with the actual quality of their homes after a few months of occupancy, simply abandoned them and disappeared. In some areas, such as Detroit (where FHA acquired more than 15,000 units in about 2 years' time) the situation reached such proportions as to be commonly termed a "scandal." For the first time in its history, FHA was forced to draw upon the Treasury for very large amounts to meet insurance claims.

That there was collusion and fraud in many of these cases is beyond doubt. A considerable number of indictments have already been handed down, and many more investigations are still in progress. It seems likely, however, that the more common causes were of a simpler nature—that the property was assigned an unreasonably high value (and therefore mortgage amount), and that the purchaser was not fully and objectively evaluated from the standpoint of his reasonable debt-carrying capacity, or both. Thus, what the experience really demonstrated was that substituting one form of bad judgment for another is likely to change matters, but unlikely to improve them.

It also raises a question whether, in any program to revitalize FHA and enhance its effectiveness as a housing agency, it may not be useful to reconsider the whole approach to methods, techniques, and even policies of appraisal, and more broadly of underwriting, and to examine such questions as, for example, whether there are not inherent differences between the assumptions and techniques for these purposes that are adequate for a commercial agency and those that are suitable for an agency of Government charged both with a public purpose and with the burden of proceeding with due diligence, prudence, and care.

Turnkey in Public Housing Programs

The invention of the technique of producing low rent public housing through what is called the Turnkey method is an instance of a somewhat unusual use of administrative discretion and ingenuity—the development of what is, to all intents and purposes, virtually a new program, or a new form of a program, not on the basis that the authorizing statute specifically provides for it, but rather on the basis that there is nothing in the statute that specifically prevents it.

It is clear from even a general reading of the legislative history that the Congress never imagined that it was authorizing the turnkey approach to public housing. That is not to say that they would have refused to authorize it had it been suggested. It simply never occurred to them—or, indeed, to anyone else—at the time. Whatever their reaction might have been had the subject come up, the statute they wrote was susceptible to being executed through the turnkey approach, rather than through the method that everyone assumed would be followed, and which indeed was followed exclusively until about 1966.

Under the original and conventional approach, the local housing authority would select and acquire a site, hire architects and engineers to prepare plans and specifications, and then proceed through the laborious and often onerous procedures applicable to public construction projects with respect to competitive bidding, award, and supervision of construction.

Under the Turnkey approach, by contrast, the local housing authority enters into an agreement with a private developer who has access to a site to purchase a low rent housing project after it is built by him. The local authority, of course, retains the right to approve such basic elements as design, amenities, and costs.

The Turnkey concept may be considered a rather adventurous departure in view of the natural tendency to adhere to traditional methods in the absence of specific congressional sanction for program innovations. Nevertheless, it is based upon legal authority, at first deemed tenuous but now recognized as valid. This is the statutory power to acquire, as well as to develop and build, low rent housing. While the term "acquisition" appears in both the Federal law and the complementary State legislation, it had always been conceived as the authority for the acquisition of land, or land and buildings for demolition or rehabilitation necssary for construction by the housing authority. The idea of local public housing authorities using Federal assistance under the U.S. Housing Act of 1937 to undertake a program involving the acquisition of new, completed housing projects had not been contemplated previously.

The only significant challenges to legal authority for Turnkey operations were limited to State law questions in a few States. Efforts, all unsuccessful, were made in some States to interpret existing State laws (or enact new ones) to extend to Turnkey construction by a private owner the public bidding or labor standards already applicable to public works construction by a city or other public agency.

There was some critical reaction to the Turnkey system. For example, the American Institute of Architects feared that quality might suffer; that the local housing authority-architect-client relationship might be jeopardized; and that architectural fees would be an issue. However, the merits of the system were thought to outweigh any such risks—primarily cost savings, and more rapid project development. Obviously, administrative costs of the local housing authority in connection with the construction are substantially reduced by Turnkey. Cost savings to the builder, which can be passed on to the housing authority, result from the avoidance of lengthy and expensive public bidding procedures, as well as labor standards or other requirements applicable to public construction projects.

Another important cost saving results from the flexibility of a private owner in altering his construction procedures or physical items going into a building without adversely affecting the end product prescribed by the local housing authority. This avoids the delays inherent in housing authority procedures on such matters that require formal meetings and decisions by public officials. The use of a site already owned by the builder has advantages both to him and the local housing authority, as compared to site acquisition by the authority itself for a regular public housing project.

Another virtue of the Turnkey concept claimed for it by its advocates is its effect in making possible more extensive use of private enterprise in the public housing program through the use of private architects and private developers in site acquisition and development.

As of December 1972, 775 local housing authorities had made use of the original Turnkey concept in developing 1,433 projects comprising 181,480 dwelling units.

Further logical extensions of this principle of greater involvement grew out of the original experiment, and have been used to a more limited extent. One is called Turnkey II which involves simply contracting out project management to selected private management firms. The method can be employed before or during construction, to assist in the selection of occupants and in their training and orientation, or limited to pure management after construction. Emphasis has been given to selecting management that is responsive to social and human requirements, as well as physical and financial matters. A Turnkey III and an experimental Turnkey IV involved eventual home ownership by tenants in public housing projects.

Housing for Low Income Families on Indian Reservations

For many years the low rent public housing program of the Federal Government, under the U.S. Housing Act of 1937, was not generally applicable to Indian reservations, notwithstanding the deplorable housing conditions of thousands of low income families living on those reservations. The framers of that act had not specifically contemplated its application to Indian reservations or made special provisions for them—having primarily in mind urban housing in blighted areas where the city or other locally authorized agency would construct and own the housing to be occupied by the low income families. Accordingly, because of unusual factual circumstances with respect to Indian reservations, they had been, in effect, excluded from the benefits of the act.

It was not until 1961 that the executive branch (through the joint efforts of the Bureau of Indian Affairs and the Housing and Home Finance Agency) developed a program to bring the benefits of the low rent public housing program to low income families on Indian reservations. In doing so, the following two principal matters were dealt with.

Eligibility of Indian Tribes: Under the act, financial assistance can be furnished only to public housing agencies defined as "State, county, municipality or other governmental entity or public body" authorized to undertake low rent housing and slum clearance projects. Generally these eligible bodies have been local public housing authorities created under or by State law expressly enacted for that purpose. Indian tribes are not generally subject to State law except as Congress may so decree, nor have they express statutory authority regarding public housing. The issue of the eligibility of Indian tribes to receive grants, loans, and annual contributions under the above legislative definition, therefore, posed special problems.

The HHFA resolved that issue by making a legal determination that Indian tribes are "governmental entities" or "public bodies," and that incorporated tribes, at least, could establish public housing authorities and engage in providing low rent housing under the broad charter powers given them by the Federal Government. That made them eligible for public housing assistance. From that determination flowed other decisions under the act, such as those relating to tax exemption and ability to convey title to housing property on default.

Mutual Self Help: A solution to the legal barrier, however, did not suffice to make the program feasible on a substantial scale. Many Indians on reservations have very low incomes, even in relation to those of families in public housing generally, but they have construction skills or the ability and willingness to learn and use them. Accordingly, a "mutual self help" or "sweat equity" technique was developed for the first time in the low rent public housing program and used in the construction of housing for Indians. In essence, this concept treated the contribution of labor toward project development by prospective occupants as a means of reducing construction costs. In addition, the value of labor contributed by an occupant was credited toward his eventual ownership of the dwelling.

Under this technique, the amount of funds that the local housing authority has to borrow for project development is reduced by the amount of the "sweat equity." However, the amount of the Federal annual contribution for the project is computed on the basis of the total development cost including "sweat equity." This amount of Federal contribution in relation to the reduced private borrowing makes it possible to pay off the indebtedness sooner—that permits the housing authority to accelerate the transfer of each individual dwelling to the Indian occupant, as that can occur only after the indebtedness is paid.

About 135 public housing authorities have been established on Indian reservations. Some of these have built public housing under conventional methods, as well as through the "mutual self help" technique.

Thus, a combination of legal and administrative ingenuity and flexibility in effect "discovered" a whole new class of beneficiaries of the low rent public housing program—a class who were obviously deserving and in urgent need of the assistance provided, and who up to then had been omitted from the scope of the program not by intent but, in effect, by oversight.

2 Major Rationales for Federal Housing Policies

The Rationales for Government Intervention in Housing: An Overview

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Introduction

Many reasons and justifications for a government role in housing have been offered. Few have been substantiated by disciplined research as being the best way to deliver, or even to deliver at all, the benefits envisioned by the proponents of the particular government action.

Early planners and reformers believed strongly in the socially reforming qualities of improved housing; in the words of LeCorbusier, the noted architect, "re-form the conditions of habitation and you can eventually improve man's behavior." [1] Such a strong belief in the benefits of good housing has been subject to heavy criticism,[2] although it has been invoked in support of government housing programs.[3]

[1] Brian, Brace Taylor: *LeCorbusier at Pessac, The Search for Systems and Standards In the Design of Low Cost Housing,* Harvard University Press, October 1972:

a "This concept of the house as an active, formative . . . entity . . . appears in LeCorbusier's concept of planning: reform the conditions of habitation and you can eventually improve man's moral behavior." Part 1, p. 1.

b ". . . The communical room should be the basis of low-cost housing . . . the basis, moral as well as physical, for creations of the dwellings of the willing man . . . ." Part 1, p. 2.

c "Reformers such as (Alfred de) Foville, Charles Luckas, Emile Cheysson and others, saw a kitchen-garden annexed to an individual dwelling as a means for stabilizing the working-class population near factories . . . ." Part 1, p. 4.

[2] John P. Dean, "The Myths of Housing Reform," American Sociological Review, April 1949.

[3] For an example of this, see the statement by Dillon S. Myer, then Commissioner of the Federal Public Housing Authority, quoted in Hugh O. Nourse, "A Rationale for Government Intervention in Housing: The External Benefits of Good Housing, Particularly with Respect to Neighborhood Property Values," paper submitted to the National Housing Policy Study.
All succeeding references in this paper are to papers commissioned for the National Housing Policy Study. The papers, written by noted scholars, summarize the evidence on the various rationales, and provide analytical insight into the implications of the evidence. The bibliographies of these papers contain references to many original studies, which provide the ultimate basis for the analysis of this section. The papers are published in this volume.

Both advocacy and criticism have been based on inconclusive evidence. While there has been a large volume of research on many topics in housing, much of that research is subject to serious methodological shortcomings. Also, on some important topics, there has been very little research.

Further, separating and controlling for the many variables at work in "before" and "after" housing situations is not a simple research problem. It requires prolonged observation of very large samples of people who do not view themselves as guinea pigs. The funds, the willingness, and the capability to undertake such research have not often come together.

Nevertheless, progress in the social sciences has produced a reasonable amount of empirical evidence on which to judge many of the rationales for government action in housing. Relatively few are yet firmly supported by existing evidence.

Background

The basic reason for government intervention in the housing market—the reason for any government housing policy—is that, without such a policy, there would not be a sufficient stock of adequate housing in the United States. Since there are few remaining backwoodsmen or cave-dwelling hermits, and nearly everyone does in fact live in a housing unit of some sort, it is necessary to define "sufficient" in terms of housing quality, rather than merely in terms of the number of housing units.

The question of whether the housing stock is sufficient, in terms of quality, should be answered on the basis of several different criteria. These criteria fit into four broad categories.

One category is equity. Is there a fair distribution of adequate housing for everyone within the United States? Particular concern here is given to the poor, who may be unable to afford housing of quality as high as the majority of the public believes they should occupy. The criterion against which the existing stock is to be measured is the level of housing quality that public opinion finds to be the minimum adequate for everyone in our society.

A second category is efficiency. Is everyone freely able to buy as much housing as he is willing to pay for? In our society there is a presumption that provision of goods and services should be left to private, free markets in which buyer and seller come together, each seeking to make himself as well off as possible. The markets for many goods and services fail to work perfectly, however; if they fail, it is possible that government intervention may be needed to improve the market mechanism.

A third category, combining the first two to some extent, is concerned with special housing problems. The housing market may work well in general, without government intervention, but does it work well for minorities? Does it work in rural areas as well as in urban ones? Different groups within society may be unable to buy housing on equal terms. There are questions of both equity and efficiency in this situation, which again may be improved by government intervention.

The final category concerns national economic conditions. Do policies designed to achieve broad national economic objectives create special problems for housing that cannot be solved without additional government action? Particular attention is often focused on the effects of monetary policy on the housing market.

There is a literature dealing with these questions, analyzing them from a logical standpoint and attempting to determine their practical importance. In the succeeding section of this paper, the current state of knowledge is discussed. Precise answers are not available on every point, but in most instances useful inferences for policy can be drawn from the existing evidence.

Equity

Income Redistribution

Public opinion as to what is equitable, or fair, provides one fundamental reason for government concern with housing. American citizens as a whole appear to believe that the poorest people among us should live in better housing than they are able to afford, and that they should be assisted to do so. This is a political judgment which has been made and reaffirmed many times by Congress and the President, under administrations of both parties.[4] It has provided the basis for housing subsidy programs. As a political decision, it is a sufficient justification for government concern and action. Individual citizens may disagree and may attempt to persuade others to change their opinions, but there is no empirical means to "prove" that such a judgment is factually "wrong."

It is important to note that the political judgment concerns more than housing; it is part of a more general opinion that the poor have too little income, too low a standard of living. The distribution of income that arises from the economic activities of individuals, as producers and consumers, is too unequal; some people are too poor. They cannot afford enough of any goods and services, not just housing.

Dissatisfaction with income distribution does not justify a housing program; it justifies a welfare program.[5] Poor families are unable to buy adequate food, clothing, transportation, medical care, or adequate housing. However, the first three are left to the poor to choose among for themselves. For example, there is no national automobile policy to provide automobiles to everyone, even though some people are unable to afford an automobile. Nor is there a program to insure that everyone gets some minimum daily requirement of protein, vitamins, and minerals, even though there is general recognition that these are very important to health and well-being. Instead the poor are usually given cash and left to make their own decisions on how to spend it.

In fact, it can be shown that a housing program is inferior to a welfare program, from the standpoint of improving the well-being of the poor. The welfare program provides money; the housing program provides only housing. Under the welfare program, the poor have more options.

If the recipients of welfare want to spend their entire subsidy on housing, they are free to do so. In this case, the two programs are equivalent, and leave the recipient equally well off. But this is unlikely. Usually, the recipients will want to spend part of their increased income on housing, part on food, etc., in which case the welfare payment is more valuable to them than a program providing housing worth an amount equal to the welfare payment.

As an example, under the public housing program, a poor family may be given an apartment which is worth $175 per month, but for which it pays only $45 per month from its own income. If the poor family were given $130 per month cash instead, it could rent the same apartment if it wanted to; or it could buy other goods and services of its own choice. It would be no worse off, and almost certainly it would be more satisfied, under the welfare program. And it

[4] Robert Agus, "Legislative Commitment to Housing," paper submitted to the National Housing Policy Study.

[5] Harold M. Hochman, "Housing Subsidies as Redistributive Instrument," paper submitted to the National Housing Policy Study.

would have been able to decide for itself what to do. Thus the income redistribution argument provides little basis for a housing program.[6]

"Merit Good"

Another kind of political judgment has sometimes been advanced for government housing programs. This is the notion that housing is a "merit good" that people should be encouraged or required to consume, in particular, over and above the amount that they would choose to consume.[7]

It is easy to confuse this argument with others to be discussed later; therefore, it is necessary to spell out precisely what it says. The basic point about a "merit good" is that people consume less of it than they ought to, for their own benefit. The qualification is important. The "merit good" argument does not depend on any presumed benefits to society as a whole from its consumption. It states that if the poor consume more housing and other "merit goods," and less of other goods and services, they will be better off; the rest of society need be neither better nor worse off.

In this form, the argument is difficult to sustain in a democratic society. It is directly counter to our basic belief that individuals should have the freedom to pursue their own path to happiness. Nor is it clear how the majority will be able to discover that the poor are not as well off as they could be, when the poor have been unable to find this out about themselves.

It can be argued that American citizens have decided that housing, and perhaps a few other goods, are "essential needs" for all people and should be provided even to those who would prefer other goods. In other words, our basic belief in individual liberty is to be modified by a requirement that certain standards of consumption should be met by everyone. The argument is at best uncomfortable, and at worst patronizing and paternalistic.

Optimal Redistribution

In recent years a new line of argument has been developed that combines the "merit good" concept with a broader view of income redistribution. Briefly stated, this concept of "optimal redistribution" is based on the belief that the satisfaction of the giver as well as the receiver should be taken into account in evaluating redistribution programs.

The poor may prefer to be given money. They might prefer to spend it on, say, liquor and gambling (to choose invidious extremes), rather than a new apartment. The rest of society—the taxpayers—may prefer to have the poor occupying the new apartment, rather than spending money for other purposes. In this situation, a welfare program is not clearly or necessarily superior to a housing program, because some people are happier with one, and some with the other.

The appropriate program is one which makes both the poor and the taxpayers at least somewhat better off. A housing program might still fit this description: The poor would have a higher standard of living than they would have with no redistribution program, though they might have other preferences, given a choice. The taxpayers have lower incomes, counterbalanced by the satisfaction of knowing that the poor have better housing. The welfare program would give choices to the poor and leave them more satisfied than they would be with a housing program, but the taxpayers would not be better off, since they would have the dissatisfaction of lower income and unwanted uses of public funds.[8]

This is a rather new idea in the analysis of government programs. There is virtually no evidence as to what subjective value taxpayers may actually place on housing consumption by the poor vis-a-vis other forms of consumption. There are only guesses.

Efficiency in Housing Markets

External Benefits

The concept of "optimal redistribution" implies that individuals derive satisfaction from the consumption patterns of other individuals, as well as from their own. This idea has been, and continues to be, an important part of the justification for government intervention in housing markets, in a somewhat different context. It has long been argued that improved housing conditions in a neighborhood benefit other residents of the neighborhood, besides benefiting those

[6] Richard F. Muth, "The Rationale for Government Intervention in Housing," paper submitted to the National Housing Policy Study.

[7] Joseph S. DeSalvo, "A Rationale for Government Intervention in Housing: Housing as a 'Merit Good,' " paper submitted to the National Housing Policy Study.

[8] Richard A. Musgrave, "Policies of Housing Support: Rationale and Instruments," paper submitted to the National Housing Policy Study.

whose housing is improved directly. Stated the other way around, substandard housing inflicts costs on others besides its occupants. These benefits or costs may be both monetary and nonmonetary: Higher property values for other property in a neighborhood when the substandard housing is upgraded or replaced; lower crime, delinquency, disease, and death rates when housing is improved.

If these external benefits are generated by poor housing, then a case can be made for government intervention in the housing market.

Individuals acting in their own self-interest will not take account of the benefits that they create for others when they occupy good housing. They will consume housing only up to the point where the last dollar spent on housing creates a dollar's worth of satisfaction for themselves alone. They will ignore the additional benefits it may create for their neighbors because most individuals have no incentive to take this into account. They will consume "too little" housing, from a social standpoint. Under these circumstances, government intervention to increase the consumption of housing is desirable, in order to insure that the benefits to all of society are fully purchased.

The existence of either monetary or nonmonetary benefits would be sufficient justification for government intervention. Whether or not they exist is a question of fact, rather than theory, which must be answered by detailed studies of housing markets.

There is evidence that good housing creates monetary benefits for other nearby housing. The upgrading of whole neighborhoods in many American cities exemplifies this. As individual houses are improved, prices rise for nearby property which has not yet been renovated. The benefits spill over onto nearby property. There are several qualifications to this result, however. First, it does not apply in rural areas, where there are wide distances between houses. Second, even in urban areas the range of the benefits is probably very small, perhaps extending only to adjacent property, perhaps extending as far as all other property on the block, almost surely extending no further. Third, and most important from a policy standpoint, there is virtually no evidence that any Federal Government housing programs have been able to generate these externalities for surrounding properties.[9]

The most careful studies to date find that nearby property is unaffected by urban renewal, public housing, or Section 235 and Section 236 housing. Thus, though such externalities probably occur in some situations, they are not created by government subsidy programs. The rationale for government intervention is valid, but the form of government intervention has not been effective.

The extent to which improved housing reduces crime, disease, and other social ills has been long debated and analyzed. From the standpoint of housing policy, it is useful to separate the possible benefits into those which accrue to the occupants of the improved housing, and those which accrue to other people.

For example, it is obvious that lead-base paint poisoning of small children ceases when they are moved to housing with no lead-base paint, though symptoms of the earlier poisoning remain.[10] The change is highly desirable for them and for their families, but it does not create benefits for other residents of the neighborhood. By contrast, if improved housing generated lower rates of contagious disease, it would bestow benefits on many people besides its occupants.

Of the social ills that may be attributed to substandard housing, several affect, almost exclusively, the occupants of the housing: These include poor school performance, property destruction due to fire, and some health problems. On the other hand, crime and delinquency and contagious diseases affect other people to a substantial extent. The former category does not justify a government housing program, even if it is shown that benefits exist; it justifies either an income redistribution program to enable the poor to move out of substandard housing and reap the benefits of good housing, or an educational program to demonstrate to nonpoor residents of substandard housing that they could avoid social ills by moving.

Moreover, the evidence that improved housing alone reduces these problems is, at best, mixed. The clearest effect is that fire losses are reduced, but there is no evidence that school performance, insofar as it can be measured by standardized test scores, is affected by housing conditions. There is some evidence that individuals may have fewer psychological problems, but the effects of housing are slight, and the evidence is not entirely conclusive.

In the category of social ills that clearly create external costs for others, health may be im-

[9] Nourse, op. cit.

[10] Stanislav V. Kasl, "Effects of Housing on Mental and Physical Health," paper submitted to the National Housing Policy Study.

proved for some groups, while crime and delinquency apparently are not affected by housing. There is evidence that children in good housing are less prone to infectious diseases such as measles and chicken pox, and to dysentery and other digestive diseases; for older persons, no benefits have been established to date.[11] There is some evidence that crime can be reduced by good architectural design, but not by housing conditions per se.

These conclusions may be surprising; many people appear to believe that housing does affect health, crime, etc., and that argument often has been advanced as a justification for housing programs. In order to justify the housing program, however, it is necessary to show conclusively that housing quality has an effect on crime or disease, apart from the characteristics of the people living in the housing. It is easy to show that rich people living in high quality housing are less likely to commit crimes or contract tuberculosis than are poor people living in substandard housing. It is hard to show that housing is the causal factor.[12]

The studies that have been most careful to isolate housing from other factors have demonstrated very little evidence that housing has any significant effect on social ills. The most that can be said is that housing is one of a complex of factors which interact to produce the problem.[13] From the evidence to date, it is reasonable to conclude that expenditures for housing subsidies cannot yet be justified on the expectation of a reduction in social ills.[14]

A final point about the effect of externalities on the efficiency of the housing market is especially important from the standpoint of Federal housing policy. The benefits of good housing—to the extent that they exist—and the costs of substandard housing are primarily if not exclusively local.

This is particularly true of the monetary benefits. Property values are raised, if at all, in a very small area. Fire damages are reduced only within a block or two at most. That is also true, to a slightly lesser extent, for social benefits. The disease rate, for example, may be reduced for people living in the immediate area, but less so for people living in the rest of the city or metropolitan area. Benefits to residents of other cities and States are likely to be very small, occurring only because of population mobility. The same would be true of crime and school performance if connections between housing and these phenomena could be shown to exist.

The national importance of more efficient housing markets is thus small, relative to its local importance. Unless local governments are hopelessly inefficient, these externalities should be left primarily to local officials. Failure of Federal programs to generate the externalities may suggest that local programs already may have produced what effects there are.[15]

One final word is necessary on the extent and quality of the research to date. Some of the potential effects of house and neighborhood may be beyond the measurement of current investigative efforts and skills. These effects may occur during succeeding generations. The long term effect of substandard housing on a mother, and her effect on her children, and the family's effect in turn on others in the neighborhood, is an example. The effects may be too subtle for the size of present samples or the term of observation. Changes in death rates from thrombosis, in quantities of a few per hundred thousand, have been isolated and are a concern in the study of the contraceptive pill, for example. But these findings required very large sample populations and very long periods of observation. Studies of this magnitude have not yet been undertaken in the housing area.

Thus, although current investigations give little support to many long-lived housing beliefs, it must be cautioned that the final word may not be in.

Other Federal Programs

Policies of the Federal Government may inadvertently impede the functioning of the housing market. Such policies include urban renewal, which until recently has been responsible for reducing the stock of housing in each project area by causing more demolitions than new construction; the Federal highway program, which destroys housing in urban areas; and a variety of programs—such as timber industry regulations—which impinge on housing.

The case for Federal programs to ameliorate these effects, where they are significant, is probably more compelling than for any of the factors previously discussed in this section. Where hous-

[11] Jerome Rothenberg, "A Rationale for Government Intervention in Housing: The Externalities Generated by Good Housing," paper submitted to the National Housing Policy Study.
[12] Kasl, op. cit.
[13] Rothenberg, op. cit.
[14] Muth, op. cit.

[15] Richard E. Wagner, "The Division of Responsibility for Housing Policy in a Federal System of Government," paper submitted to the National Housing Policy Study.

ing is destroyed in the national interest, there is a moral obligation to provide some assistance to those affected.[16]

This can be done by payment of just compensation for the value of the property taken and for the costs of relocation. However, many of the costs of relocation are psychological rather than pecuniary.

It is not clear that the additional housing should be provided by the Federal Government. The private market will provide housing for those who can pay for it; an individual who has paid for his home should be able to buy its equivalent elsewhere. Since most projects have operated with very long time lags between planning and construction, private suppliers should have little difficulty in preparing for the need.

Local Government Policies

In addition to the foregoing government policies, it is sometimes argued that local governments themselves interfere with the functioning of housing markets, creating hardships for many people. It is further argued that Federal intervention is the only, or best, means to redress such problems. There are three ways in which local governments may interfere: zoning restrictions, building code requirements, and poorly planned local renewal and development programs.

The arguments for Federal intervention in the latter are similar though much less compelling than for the Federal Government's own program impact.

The zoning argument is usually applied to suburban jurisdictions which zone to keep out the poor. To the extent that minorities are poor, the zoning serves also to separate the races, with whites in the suburbs and others in the center city. This is accomplished by requiring larger lot sizes than would be utilized in the absence of zoning.

A problem with this argument is that it appears to imply owners are acquiescing to the lowering of property values. If smaller lot sizes appear in the absence of zoning, then property could have increased in value, without zoning. This is because people are willing, for example, to pay more for two half-acre building sites than for a single 1-acre building site. If the zoning board requires 1-acre lots, then landowners—and voters—effectively incur capital losses; their property is worth less than it could be.[17] Countering this, the satisfaction of the majority of homeowners having little or no subdividable property, and content with present use, offsets the few who would benefit from the subdivision or who desire more intense use of land within the community.

A more important problem with the zoning argument is that the empirical evidence fails to support it. Careful studies of housing densities fail to show any evidence that suburban densities are lower than they would be if the independent suburbs fell within the political boundaries of the central city. Densities decline with distance from central business districts of central cities, but the decline is gradual. There is no sharp break regularly found at the political boundary between city and suburb.[18] There are, of course, conspicuous exceptions, where communities have deliberately up-zoned, but these seem to be few.

The most that can be asserted is the obverse of the argument: Those seeking isolation from the poor and from minorities, having consciously or unconsciously observed the regular decrease in density and of accompanying increases in price, select an area of sufficient distance to achieve their desired isolation.

Subdivision requirements governing land improvement may be similar in effect. Increased requirements for streets, sidewalks, storm drains, etc., raise the cost of building lots. Developers build correspondingly higher priced houses in order not to unbalance values. The poor are effectively excluded. Evidence of widespread and systematic use of this device for exclusion also does not exist.

Building code requirements may impede the workings of the housing market by setting unnecessarily restrictive standards, limiting the use of newer, more economical products and techniques. A problem may also be created because codes differ significantly between adjacent jurisdictions, making it difficult for builders to realize economies of scale by producing large numbers of similar units at the same time.

This question has been much debated, and the evidence is not entirely conclusive. The best current evidence, however, suggests that building codes may raise housing costs by perhaps 8 percent.[19] This is a substantial figure. The build-

[16] Wallace F. Smith, "A Rationale for Government Intervention in Housing," paper submitted to the National Housing Policy Study.

[17] Wagner, op. cit.

[18] William H. Oakland, "A Rationale for Federal Government Intervention in Housing: Distortions Arising from Present Fiscal Arrangements at the Local Government Level," paper submitted to the National Housing Policy Study.

[19] George Sternlieb and David Listokin, "Building Codes: State of the Art, Strategies for the Future," paper submitted to the National Housing Policy Study.

ing code, however, like the zoning ordinance, is a product of local government. If codes are unduly restrictive on the local level, it has not been shown that they could be made less so if they were promulgated and enforced at a higher level.

A State or Federal code for example, could eliminate different practices between adjacent jurisdictions which have hindered large-volume builders and factory production of housing and components, but at the possible cost of reducing or eliminating quick response to problems at the local level. It is also argued that a more centralized code administration might be more difficult to persuade to adapt to technological advances, while multiple code administrations might provide opportunities for new technologies to prove themselves in at least one or a few jurisdictions, in natural experiments.

Risk

There is special concern over the possibility of imperfections in credit markets, as well as the housing market itself. Two major areas can be identified. One is the risk inherent in the market. Housing is built and bought over time. There is always a risk that either builder or buyer will be unable to pay for the house, due to unexpected circumstances. The risk is especially great for the buyer. The existance of risk may generate inefficiencies in the housing market, under certain circumstances. Government intervention could be useful in reducing the cost of the risk by spreading it among many buyers.[20]

That has been the rationale for government mortgage insurance and loan guarantees, such as those of the FHA and VA. By contrast to pre-FHA conditions, home mortgage interest rates have declined, and repayment periods have increased, bringing down the monthly cost of homeownership and permitting a great many more people to own their own homes. It is possible that some of these effects would have occurred without FHA and VA programs, but the best evidence indicates that the programs are responsible for a substantial net increase in the housing stock, perhaps as much as 30 percent in the 1948–1956 period, for example. The percentage of homeownership has nearly doubled from the 1930's to the present, probably in large part because of the actions of these programs, plus rising general affluence.

[20] Dwight Jaffee, "Credit for Financing Housing Investment: Risk Factors and Capital Markets," paper submitted to the National Housing Policy Study.

Several points should be considered in reviewing whether these programs have been necessary. First, the presence of risk does not necessarily cause a market to work inefficiently. Private firms are able to provide insurance against fire, theft, and similar problems. Sometimes risk does impede the market, however. Insurers may be unwilling to take particular risks, for example. The costs or difficulty of determining the risk may be too high. The Federal Mortgage Insurance programs may well have provided an answer in a case in which private firms were unable to determine the risks of long term, low interest mortgages, and hence were unwilling to make the loans.

The FHA premium has more than covered its losses on defaults and has permitted the buildup of substantial reserves. Economic feasibility has been demonstrated. As a result, private mortgage insurance has begun to appear, and could eventually take over many or all of the Government's functions.

Thus, a theoretical argument for Government intervention has been supported by the evidence, to the point at which the intervention may be nearing successful conclusion.

Supply of Credit

A second area of concern in housing finance lies in the supply of credit to housing. It often is argued that market imperfections inhibit the flow of funds into housing, so that the supply of credit is less than it would be if financial markets were more efficient. (This argument applies to the overall level of credit in housing, rather than to the problem of cyclical fluctuations in the supply of credit. The latter question is discussed later in this paper.)

When the supply of funds to the mortgage market is examined, it is obvious that different types of financial institutions participate in the market to very different degrees. Savings and loan associations, for example, held about 45 percent of all outstanding mortgage debts on homes and small apartment buildings in 1970, and mutual savings banks held another 15 percent. The portfolios of these institutions are concentrated in residential mortgages, in contrast to commercial banks, insurance companies, and pension funds.

Some students of the mortgage market have advocated measures to increase the participation of the latter institutions as a means of expanding the supply of credit to housing.

Others have argued that differences between institutions do not inhibit the flow of funds into housing. Funds can be transferred between institutions as rates of return on mortgages change, relative to bonds or other investments. In fact, there have often been pronounced cyclical shifts of this kind. We experienced one in the summer of 1973.

The argument, in fact, often is reversed; it may be that existing institutions, including Federal programs, supply more credit to housing than would have been provided by an unimpeded free market. The argument that more credit should be supplied to housing appears to be primarily a restatement of the argument that housing deserves special treatment, either as a "merit good" or because of external benefits or other market imperfections.

Housing Market Adjustments

Another kind of possible market imperfection may arise in the process by which the housing market adjusts to changes in demand. It takes time to build houses; when the demand for housing increases, the supply cannot be increased immediately, and until it can be increased the price of housing may increase inordinately.

The dynamics of housing market adjustment have received relatively little attention. The best evidence suggests that about half of an increase in demand is supplied within 2 years, and over 90 percent within 6 years.[21] Whether this is "fast" or "slow" is a matter for comparison. It does not appear to be very different from the adjustment of capital investment to increased demand, but other consumer goods respond much faster.

It takes time for demand to adjust, as well as supply. Leases must expire; houses must be sold. Available evidence indicates that the adjustment does not cause a sharp increase in prices. Rather, it involves a gradual increase in prices as demand increases and new housing is supplied, followed by a gradual decline. In this, it is not very different from other products having an increase in demand and sellers ready to increase supply.

Thus, there does not seem to be a serious problem of sharp price fluctuations generated by shifts in demand; indeed, if there were, it is hard to see which Federal policy would be appropriate to counteract rapid, local shifts in demand.

Housing Problems of Special Groups

The previous section was concerned with general reasons why the housing market may not work efficiently. In this section, possible market imperfections pertaining to specific groups or regions are considered, to see whether they exist and whether they provide a reason for Federal housing programs.

Discrimination

Discrimination against minorities is the greatest concern in this category.[22] There is a widespread observance that blacks in particular, and other minorities as well, are unable to buy housing on the same terms as whites. Discrimination has raised the price that blacks must pay for housing.

Within the last 15 years there have been numerous studies to estimate the extent of discrimination. Some studies have not found any differences in the prices paid by blacks and whites for identical houses; others have found differences in prices paid by black homeowners but not by black renters (and vice versa); still others have found price differences for both categories. It is difficult to establish a precise result because nearly all of the studies have had shortcomings. The central tendency of the work done to date indicates that blacks pay 5 percent to 10 percent more than whites for identical housing.

Price discrimination of this sort is clearly a matter of national concern. It is important, however, to note that discrimination is mixed with poverty as well; housing discrimination against blacks is compounded by low incomes. To the extent that the problem is a poverty problem, then, the rationale for a government program is the same as that discussed in the section on equity.

The separate problem of discrimination must be met by vigorous enforcement of open-occupancy laws, which will tend to keep prices paid by all groups the same. Existing programs do little to reduce prices to minorities, except as they are kept free of discrimination.

Job Dispersal

Others with a housing-related problem are the poor residents of central cities. The problem

[21] Edgar O. Olsen, "A Possible Rationale for Government Intervention in Housing: The Slow Adjustment of the Housing Market to Its Long-Run Equilibrium Position," paper submitted to the National Housing Policy Study.

[22] John F. Kain, "Background Paper on Housing Market Discrimination and its Implications for Government Housing Policy," paper submitted to the National Housing Policy Study.

arises because much employment has moved from central city to suburb. It is thus more difficult and expensive for these poor to hold jobs, since transportation and commuting expenses for them are raised. As a solution, programs to aid the poor in obtaining better housing in the suburbs are frequently advocated.

Despite widespread belief that this is a serious problem, available evidence appears to indicate that it is not.[23] While jobs have steadily increased in the suburbs, there are disproportionately more jobs for the poor in the central cities than in the suburbs. There is no greater imbalance between poor residents and available jobs in the cities than elsewhere.

There is job discrimination, and there is locational discrimination, but these are not housing-caused, nor best solved by housing answers.

A program to move the poor to the suburbs would put most of them farther from their jobs than they are now, and would not, of itself, increase job opportunities for them.

Growth Policy

It is frequently argued that the distribution of population has become too concentrated in the larger metropolitan areas, and that housing programs should be developed to encourage a redistribution towards the more sparsely settled areas.

This argument has two parts, neither of which has been proven. First, it is not clear that population is "too concentrated" in any meaningful sense. While the largest cities have severe problems of congestion and pollution, for example, they also produce the highest paying jobs. Higher pay may be an offshoot, but more likely it results from size itself. It takes certain levels of concentration to generate the necessary levels of business opportunities which can then in turn sustain the higher pay.[24]

To the extent that cities have pollution and congestion problems, the appropriate policy is to reduce pollution and to arrange the city more favorably to diminish its nodes of congestion. When this is done, the costs of living or working in the city may go up for many people, but the cities will also be more pleasant places in which to live, and this may further attract new residents.

Attacking pollution in big cities by building housing in small towns is a terribly circuitous approach to the problem. Population grows where jobs are. A housing program is not likely to redistribute population. People will not move to areas where they cannot find work merely because there is better housing.

Rural Areas

Rural areas contain a disproportionate share of the poorest housing in the nation. Housing markets in these areas may be a contributing factor; the markets may be less efficient than in urban areas. There are, however, many other contributing factors as well. Rural areas are typically poorer than urban areas; they tend to have obsolete building codes (or none at all); poor land-use controls may hamper housing. To the extent that these factors operate, rural areas do not have a unique problem; rather, they are places where many problems, previously discussed, occur simultaneously.

Moreover, some of the special problems of rural areas arise out of poverty. For example, it is argued that sources of credit in many rural areas are scanty. There are few lending institutions, with small resources. The level of assets and liabilities of financial institutions reflect the wealth of the areas they serve; scanty resources for local banks are largely a result of low incomes for local residents.

The particular housing market problems of rural areas result from size.[25] Rural housing markets are small. There are few buyers and sellers. It is not feasible to produce houses on a scale large enough to realize the economies of large-scale production. Thus, housing costs tend to be higher in rural areas. Similarly, lenders in rural areas may incur higher service costs, or greater risk, because of the small size of the market.

A second source of problems is that rural areas are, by definition, less dense. It is more expensive, on a per household basis, to supply supporting public facilities; in turn it becomes more expensive for the rural family to occupy housing of a quality equivalent to that of urban homes.

The market is simply responding to its natural supply/demand relationships. That does not make it inefficient. Government intervention in rural housing markets would probably not pro-

[23] Lawrence H. Thompson, "The Suburbanization of Employment," paper submitted to the National Housing Policy Study.

[24] Edwin S. Mills, "Housing Policy as a Means to Achieve National Growth Policy," paper submitted to the National Housing Policy Study.

[25] Chester M. Wells, Jr., et al, "Rationale for Government Intervention in the Housing Sector of Rural America," paper submitted to the National Housing Policy Study.

mote greater efficiency; rather, it would involve subsidizing the residents of rural areas, because they are poor, or because of a political judgment that rural areas should be assisted.

National Economic Policies

It is often argued that economic policies designed to achieve stability and high levels of economic activity for the Nation as a whole, may have particularly severe consequences for housing, and that these consequences should be mitigated by special programs to insulate housing from them. Concern is focused chiefly on monetary policy, which is believed to have especially strong effects upon housing; fiscal policy is usually regarded as less important.

Monetary Policy

The attempts by the Federal Reserve System and other Federal agencies to reduce fluctuations in national economic activity by controlling the supply of money and/or the level of interest rates are believed to have substantial impact on the housing construction industry.

This occurs because housing is a particularly durable, long-lived asset. It is possible for potential buyers to plan purchases of housing, and to defer purchase in periods of high costs. A major component of cost is the interest for mortgages. Interest rates have been, typically, high during business expansion and low during recessions; buyers are aware, or become aware, of this well-established pattern, and tend to abstain from purchasing when interest rates are high.[26]

The demand for housing, over the business cycle, thus increases in periods of recession, rather than being spread evenly over the cycle. The action of buyers can be likened to the behavior of the housewife who concentrates her purchases of linen during the January "white sales."

Recessions are periods of low incomes as well as low interest rates, which might offset some demand for housing. It seems clear from the available evidence, however, that housing demand is not very sensitive to changes in income which are expected to be temporary. The purchase of a house is paid out of the income of many years into the future. The decision to buy, and the price that the buyer is willing to pay, depend more on his estimate of future income than on present income, especially if that income is temporarily low. Lower incomes in the mild recessions of the postwar period have not, in fact, offset the effects of lower interest rates.

As a result, housing construction has been basically a countercyclical industry. The quantity of new housing produced tends to be highest when the rest of the economy is relatively slack, and lowest when the rest of the economy is operating at or close to full capacity.

These facts suggest that attempts to even out the fluctuations in the housing industry are misguided, from a national standpoint. The housing industry's countercyclical pattern provides a stabilizing force for the economy as a whole. When resources are not demanded in other industries, they are demanded in housing and are readily available; when resources are demanded elsewhere, demand for them in housing is relatively light. Policies to stabilize the cyclical demand for housing would act to destabilize the economy as a whole. They would tend to worsen business cycles, driving prices and output up in booms and making recessions more severe. From the national standpoint, this is not a desirable result.

Cyclical Instability and Housing Costs

It is sometimes argued that the cyclical instability of the housing construction industry leads to higher costs of new housing (and thus to higher costs of all housing).[27] The evidence on this point is not conclusive, but it does not generally support the argument. Higher costs are more likely when entry into the industry is difficult, and if the industry uses specialized equipment, labor, or resources. Neither appears to be true, however. Entry is relatively easy; the industry is characterized by low startup costs. Fixed costs are low. Most resources can readily be used in other industries.

Fiscal Policy

There has been relatively less concern over the effects of fiscal policy on housing construction and prices, in contrast to monetary policy. There is even some evidence that fiscal policy instruments reduce the countercyclical tendencies of housing construction. For example, the investment tax credit appears to have shifted

[26] David I. Meiselman, "The Impact of Counter-Cyclical Monetary and Fiscal Policies on Housing," paper submitted to the National Housing Policy Study.

[27] Bernard Saffran, "Appropriate Role of Government in Housing," paper submitted to the National Housing Policy Study.

fixed investment from housing to capital equipment purchases.[28] Its repeal appears to have reversed the shift. Since the purpose of the tax credit is to expand production during recessions, to the extent that it is successful, it tends at the same time to reduce housing construction. This fiscal policy instrument thus tends to smooth the construction cycle, as critics of monetary policy desire.

Conclusion

The strongest case for public concern with housing is as an aspect of public concern over the distribution of income. A large number of poor people have housing conditions which the majority of the citizens believe to be inadequate.

This political concern with the well-being of the poor, however, does not in itself justify special emphasis on housing. Rather, it justifies a program of income transfer to the poor. Such a program would be clearly superior, as far as the poor themselves are concerned, to a housing subsidy program. With an income transfer, the poor can have greater freedom of choice, and can achieve a greater level of satisfaction than if they are given only housing of equal value.

Special concern with housing can perhaps be justified if the attitudes of taxpayers also are taken into consideration. If taxpayers get satisfaction from increased housing consumption by the poor, and do not get similar satisfaction from increased food, clothing, medical care, etc., for the poor, then a housing program may be a politically desirable way of redistributing income. This argument is plausible, but there is little evidence on which to evaluate it.

Current housing policies appear to give relatively little attention to the poor. The best evidence is that the tax subsidies provided to middle and upper income families—particularly the subsidies to homeownership in the form of tax deductions—far outweigh the benefits of expenditure programs for the poor. Some method of extending these tax advantages to the poor, such as a tax credit for renters, is probably appropriate if existing provisions are to be retained in the tax laws.[29]

[28] David D. Ramsey and George Vredeveld, "A Rationale for Government Intervention In Housing: Impact of Government Non-Housing Policies on the Housing and Mortgage Markets," paper submitted to the National Housing Policy Study.

[29] Mills, op. cit.

Apart from considerations of equity, there is little evidence that housing markets suffer from imperfections which make government intervention desirable. Research into the social benefits supposedly generated by good housing has found few instances of such benefits, particularly from government housing programs. Improved health, to a small extent, is probably the only established benefit. Good housing may improve neighborhood property values also, but only in a very small geographical range. Local rather than Federal intervention may be appropriate on the basis of these external benefits, but little inefficiency is likely to result if they were ignored altogether.

There is some justification for government support in mortgage markets in order to reduce default risks in situations where private insurance of mortgages would be less efficient. Otherwise, there is little justification for government intervention to improve the functioning of the housing market.

Although inherent market inefficiencies appear to be a minor problem, there are some imperfections generated by local government activity. The most important of these appears to be local building codes, which increase housing costs by placing restrictions on the use of new materials and technologies. Code differences between adjacent jurisdictions may add to costs as well.

Discrimination against minorities, especially blacks, is another market imperfection because it raises their housing costs, although the available evidence for this is not entirely conclusive.

There are, thus, some market inefficiencies and imperfections. With the exception of the risk problem, however, all are local in scope. The benefits of better health and enhanced property values, the costs of restrictive building codes and discrimination—all are local phenomena. Eliminating substandard housing in New York does not enhance property values in California, for example.

Some Federal role may be justified on the grounds that the benefits of good housing are gradually diffused throughout the country as people move; but the benefits remain largely if not entirely local, and the Federal role appears to be subsidiary to the local government's role.

The Rationale for Government Intervention in Housing

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Summary

The direct benefits of housing subsidies to their recipients are always smaller than the value to them of an income subsidy of the same cost to the government. The larger the subsidy per family, the smaller its benefit relative to that of an income subsidy. Two conclusions follow from these considerations. First, the rationale for housing subsidies, as opposed to income subsidies, must be found either in indirect benefits of housing subsidies to other than the subsidy recipient or from an inability of the private market to supply better housing to lower income families who are given the means to pay for it. The considerations discussed in the second section of this paper suggest, however, that the indirect benefits of housing subsidy programs are minimal. In addition, postwar experience has dramatically demonstrated the private market's ability to improve housing as incomes have risen.

The second conclusion following from an examination of direct benefits of housing programs is that their total is maximized when the additional housing provided is divided among the whole of the lower income population. Providing relatively large increases in housing consumption for relatively few families is probably the greatest shortcoming of existing Federal programs. In the third section it is argued, for example, that the direct benefits of the public housing program are only about three-fifths as large as they might be if the housing produced by the program were divided among all eligible families. Most Federal programs are deficient in that the capital costs of housing only are subsidized by them. Consequently, Federal expenditures on them, and their costs to the economy as a whole, are greater than they need to be to produce the quantity of housing obtained from them.

The easiest way to overcome the shortcomings of existing programs is through a system of housing allowances. Under such a program, recipients of Federal assistance would use funds provided them to purchase housing of their choice on the private market. Housing allowances of any aggregate size could readily be divided among the whole of the lower income population and would avoid the excessive cost of subsidies to capital expenditures only. They would provide for a greater degree of competition among suppliers of housing to lower income families and provide incentives for private rehabilitation of slums. They would not of necessity concentrate large numbers of lower income families in projects. Housing allowances would provide people with the means to do for themselves what previous governmental programs have been able to do only at excessive cost and great administrative effort.

Introduction

The current suspension of Federal housing subsidy programs provides an unusual opportunity to reappraise these programs. Although the Federal Government has provided housing assistance to lower income families since the 1930's and the number of dwellings made available annually has increased substantially in recent years, few if any persons are satisfied with the results. There are a variety of possible reasons for this. Most important, perhaps, for the average person is the realization, probably implicit, that better housing does not magically transform the lives of slum dwellers. Another is the high average cost of dwellings constructed under Federal programs. Even, in the 1950's, the average public housing dwelling cost $13,500. Other reasons include the concentration of large numbers of lower income families in the vicinity of slums and the fact that, despite intensive efforts, Federal housing programs have displaced many and assisted relatively few of the lower income population. Thus, a reexamination of the rationale for Federal housing programs seems clearly called for.

Indeed, the first question one ought to ask is, "Why have a housing program at all? Why not use the funds for general income subsidies instead?" The second section of this paper addresses these questions. First, the direct benefit to subsidy recipients, or the value they place on the additional housing provided them, is examined. Next, indirect benefits to others than the subsidy recipient are considered. The second section concludes with an evaluation of the common argument that the private market is unable to provide sufficient quantities of decent housing for lower income families.

The third section presents an appraisal of the principal economic effects and shortcomings of current housing programs. Primary attention is paid to the public housing program, which, until recently, had provided far more dwellings to lower income families than any other. Estimates of the value of public housing to its tenants and to the lower income population generally are presented first. Then two important factors leading to the excessive cost of public housing—the form of the Federal subsidy and building upon cleared slum land—are discussed and their effects evaluated. Attention is then directed to other Federal programs. Because of its similarity with housing allowances, special attention is paid to the rent supplement program in the discussion of recent developments in Federal housing programs.

Housing allowances, under which recipients of Federal assistance would purchase housing of their own choice on private markets, are discussed in the fourth section. The first part of this section discusses advantages and limitations of housing allowances. Particular attention is paid here to the fact that, under such a program, its benefits could be divided among the whole of the lower income population. The single most important objection to housing allowances—that they would merely enrich landlords—is also reexamined. The second part of the fourth section makes a series of specific recommendations for implementing a housing allowance. Many practical details are omitted of necessity because of this paper's size. Attention is directed, rather, to the more important conceptual questions regarding housing allowances.

Benefits of Housing Programs

Federal housing subsidies produce benefits to the recipient of the subsidy. In the case of public housing, for example, its tenants live in better housing than they otherwise would. Public housing and other Federal programs may also benefit the taxpayer generally by reducing the size of the slum areas of various cities or by reducing municipal expenditures. Finally, Federal programs may overcome faulty workings of the private housing market. Each of these sources of possible benefit will be analyzed in this section.

Direct Benefits

Housing, or any other subsidies for specific items of consumption, is always inferior to general income subsidies from the recipient's point of view. Instead of enabling a family to inhabit a dwelling whose monthly rental value is, say, $100 greater per month than the unit the family would otherwise occupy, the family could be given $100 monthly to spend as it chooses. If the family wished to do so, it could spend the whole of the monthly payment on housing, as it is in effect forced to do by housing subsidy programs. One suspects, however, that at most a small proportion of families would so so. Though most, no doubt, would move to a somewhat better dwelling and pay a higher monthly rental, they would also spend part of the $100 on better food, clothing, and other items of consumption. Though lower income families value better housing, they also value a better standard of living generally. One would presume that the pattern of expenditure the family selects for itself yields it a greater total satisfaction.

Giving a family $100 per month, then, but requiring it to spend the whole of the sum on housing, is less beneficial to the family than allowing it to spend the sum as it wishes. Alternatively, a housing subsidy of $100 per month is worth less than $100 per month to the family receiving it. How much less depends upon the size of the subsidy relative to the recipient's income and upon how readily the family can substitute expenditure on housing for other items of consumption. Given the latter, the greater the increase in housing consumption relative to the consumption of other commodities, the lower the value a family places on an additional dollar's worth of housing (valued at market prices). In concrete terms, a fourth bedroom would be worth very little to a family if it did not have the funds to furnish it. Similarly, a larger refrigerator would mean little to a family whose food budget could not fill a smaller one. Because the direct benefits of a subsidy to some specific item of consumption rise less than proportionally with the size of the subsidy, smaller subsidies to a larger number of families produce greater total benefits to the lower income population as a whole.

I have estimated that, as of the mid-1960's, the public housing program allowed its tenants, in effect, to increase their expenditure on housing from $47 to $177 per month.[1] By my calcula-

[1] Richard F. Muth, *Public Housing: An Economic Evaluation* (Washington: American Enterprise Institute, 1973), p. 25.

tions, however, the increase in housing consumption of $130 per month would be worth approximately $71 per month. The latter figure, together with the implicit housing price reduction to the tenant of public housing, would just induce the average public housing tenant to purchase a comparable dwelling voluntarily. The increase in income and reduction in housing price to which the opportunity to live in public housing is equivalent were calculated from the best available evidence on the responses of consumer spending on housing to changes in income and housing prices. Since the typical lower income family spent the same amount on all other items whether living in public or in private housing, a substantial part—roughly half—of the subsidy was dissipated by reducing the value public housing tenants place on additional housing relative to additional expenditure on other consumer goods.

Indirect Benefits

In most discussions, Federal housing programs receive support not only for the better housing that lower income tenants are enabled to inhabit, but also for the benefits produced for the general public. Prominent among these is the reduction in the size of the slum area of cities where housing is made available to lower income families by Federal programs. By reducing the number of lower income families seeking private accommodation, Federal housing programs do reduce the number of low-quality private dwellings. In most U.S. cities, however, privately supplied low-quality housing is not scattered uniformly throughout the city. Rather, it tends to be concentrated spatially in certain neighborhoods. The depressing effects these low-quality dwellings have on other property values are felt principally along the boundaries separating poorer from better neighborhoods. Although Federal programs will indeed reduce the aggregate size of poorer neighborhoods, they will not in general eliminate the boundary effects. Unless Federal programs reduce the circumference of the boundary separating slum areas from areas of better housing, the aggregate of boundary effects on property values would be unchanged. Only the locations of these effects will differ with the size of the Federal program.

Slum dwellings may also effect the level of expenditure a city must make to provide its residents a given level of protection against fire, crime, and health hazards. It is probably the case that slum dwellings are especially susceptible to fire and increase the danger of fire to surrounding dwellings. I find most arguments which seek to establish a causal connection between poor housing, on the one hand, and crime and poor health, on the other, to be tenuous at best. There can be little doubt that crimes and health problems occur more frequently in areas of poor housing quality. This association probably arises principally because all are associated with the lower incomes of the residents of poor housing.

The best empirical evidence of which I am aware suggests, indeed, that little reduction in the cost of local government or improvement in health and personal adjustment results from better housing as such. Weicher[2] analyzed a variety of economic and other influences upon expenditures by local government. He found fairly strong tendencies for expenditures on fire protection to vary directly with housing quality, but for other items of expenditure of local governments, the association with housing quality was weak or nonexistent. Weicher also calculated the effects of housing quality improvement brought about by the Hyde Park (Chicago) Urban Renewal Program on expenditures. Even under the favorable assumption that there were no offsetting housing quality reductions elsewhere in the city, Weicher concluded that the reduction in municipal expenditures associated with renewal was only about 8 percent of the annual cost of the project.

Another study, by Wilner,[3] suggests that, apart from the better housing provided, public housing has little effect upon its tenants. Their study compared lower income families living in public housing in Baltimore with other families who had the same economic and demographic characteristics but who were privately housed. Insofar as matters relating to housing consumption were concerned, public housing tenants clearly scored better. In matters relating to health and personal adjustment, however, differences were small and did not systematically favor public housing tenants. Indeed, one suspects that current disenchantment with Federal housing programs reflects partly, at least, the realization that better housing does not magically transform the lives of slum dwellers. By concentrating large numbers of problem families, as some public housing projects have done, these problems may even have been exacerbated.

[2] John Weicher, "Municipal Services and Urban Renewal," (unpublished Ph.D. dissertation, Department of Economics, University of Chicago, 1968).

[3] Daniel N. Wilner, et. al., *The Housing Environment and Family Life* (Baltimore: Johns Hopkins Press, 1962).

Private Market Failure?

So far in this section, it has been argued that the benefits of housing subsidies to their recipients are worth less than the benefits of an equivalent income subsidy. In addition, there is little reason to suppose that benefits to persons other than the subsidy recipient are very substantial. One frequently hears the assertion, however, that the private market is simply not able to provide lower income families with decent housing. By far the most important reason why it has not done so is the small expenditure that lower income families make for housing. Many argue, however, that even if the amounts they spend for housing were augmented, lower income families would be failed by private producers of housing. Hence, it is argued, government programs are necessary to make better housing available to lower income families.

One reason for this assertion is the belief that too little private capital flows into housing for lower income families. Private lenders are frequently said to refuse to lend, or to do so only at very high interest rates. If some were to do so in hopes of profiting from higher rates on loans to lower income families or for inner city property, however, other lenders would find it profitable to undercut them. The fact that private lenders as a group do little lending for lower income property is probably due to the fact that it would be unprofitable to them at rates comparable to those charged other borrowers. Indeed, usury laws and other legal or institutional restraints on private lending may prevent private lenders from charging high enough rates on loans to compensate them for the added cost and riskiness of loans on lower income property. Whether the interest and amortization on loans for acquiring property or its improvement are paid directly by lower income homeowners or indirectly by renters, the small amounts spent for housing by lower income families limit the size of the loan that these payments can support. In addition, sporadic enforcement of building and occupancy codes, a high degree of residential mobility on the part of lower income families, and the possibility of neighborhood deterioration may all make it more expensive to lend on properties occupied by lower income families.

It is also said quite frequently that the supply of housing available to lower income families is very unresponsive to changes in housing expenditures by these families. At a rather crude level, it is sometimes merely asserted that an increase in such expenditures will cause landlords to raise the rental payments they demand for the properties they own without improving these properties. Any single landlord might wish to do so, of course, but again the argument neglects the fact of competition among private landlords. If any one landlord were to attempt to do so, the tenant could move out into a better available unit elsewhere.

On a somewhat more sophisticated level, it is argued that the attempt by large numbers of lower income families to improve their housing simultaneously would merely bid up rentals generally on the private market. The one really careful analysis of this question I know of, a study by Farb,[4] suggests, however, that this is not the case. Rather, the private housing supply appears to be highly responsive to the expenditures lower income families make. Farb examined statistically the effects of greater incomes on the relative numbers and rentals of substandard v. standard housing in different U.S. cities. He determined that the improvement in housing quality produced by income increases was about 10 times as great as the increase in rentals for housing of given quality. Even if this were not the case, however, governmental subsidies would not necessarily be indicated, because such programs, like increases in private spending, merely increase housing demand and do little or nothing to make supply more responsive.

Postwar experience in the United States, moreover, provides dramatic testimony of the private market's ability to provide better housing. Comparing data from the 1950 Census of Housing and the 1956 National Housing Inventory, Duncan and Hauser [5] concluded that the number of substandard dwellings declined by about one-third in the 6-year period in five out of the six cities studied. (The sixth was New York City, where rent controls still existed.) About 90 percent of the change came from improvement of given dwelling units. Over the decade of the 1950's, the Douglas Commission [6] showed that there was a net upgrading of slightly over 2 million dwellings from substandard to standard quality. During the 1950's, the fraction of substandard dwellings in major central cities fell by about one-half. In my own work [7] I have found

[4] Warren E. Farb, "An Estimate of the Relative Supply and Demand of Substandard Rental Housing In Major U.S. Cities," (unpublished Ph.D. dissertation, Department of Economics, Washington University, 1970).

[5] Beverly Duncan and Philip M. Hauser, *Housing a Metropolis—Chicago* (Glencoe, Ill.: The Free Press, 1960).

[6] National Commission on Urban Problems, *Building the American City* (Washington: Government Printing Office, 1969), Table 1, p. 70.

[7] Richard F. Muth, *Cities and Housing* (Chicago: University of Chicago Press, 1969), Ch. 10.

dwelling condition to be highly responsive to increases in income. Whether one makes comparisons among census tracts of a given city or among various central cities, a 10-percent increase in income produces a decline of about one-third in the fraction of dwellings which are substandard.

Current Federal Housing Programs

Although a variety of Federal housing programs exist, until the late 1960's the public housing program had provided far more dwelling units to lower income families than any other. In addition, although important differences exist among the various programs, they share many features in common. In this section, then, I will first consider some of the major economic features of the public housing program. Following this, I comment briefly on other Federal programs.

Public Housing

Although the public housing program has been subjected to criticism on many grounds, waiting lists for admission are about as long as the number of occupied units. This substantial excess demand for accommodation in public housing clearly suggests that lower income families on the whole consider public housing to be superior to the housing they can purchase on the private market. The waiting lists for admission also testify to one of public housing's greatest faults. While if a family gains admission it substantially improves its housing, relatively few families—perhaps one in 10 who are eligible—have been able to do so. Stated a little differently, the public housing program is like a lottery offering a small chance of a big improvement in housing and a large chance of no improvement to eligible lower income families.

In the second section, in discussing the value of housing subsidies to the recipient, it was argued that such a subsidy is worth less to the recipient than the market value of the additional housing provided. Part of the worth of the subsidy to the recipient is dissipated by reducing the value the recipient places upon additional housing relative to other kinds of consumption. In general, the greater the size of the housing subsidy the less it improves the well-being of the recipient and the more it tends to reduce the value placed upon additional housing. For this reason, the larger the subsidy per family, given the total size of the program, the smaller the value of the subsidy to the average eligible family.

That benefits per family increase less than proportionally with the size of a housing subsidy is well illustrated by the public housing program. In the second section, I stated that the opportunity to live in public housing was equivalent to an income increase of about $71 per month in the middle 1960's. By this is meant that if a family were to receive an additional $71 per month of real income, and the price of housing relative to the prices other consumption items were reduced by the amount implicit to tenants of public housing, the average public housing tenant would voluntarily purchase the amount of housing provided him by the program. These calculations were based upon the best available evidence on the responsiveness of consumer housing purchases to changes in real income and relative prices of housing.[8] Since about 7 percent of the population eligible for public housing was enabled to gain admission, the subsidy was worth about $5 per month per eligible family.

Precisely the same computation may be performed to determine the benefit per eligible family if the additional housing provided to lower income families had been equally divided among the whole of the lower income population. If the latter had been done, each eligible family would have been enabled to consume about $9.10 more housing each month, or to have increased its housing consumption by about one-fifth. Under equal sharing of the total amount of housing provided, the implicit price of housing to benefit recipients would fall far less than under the actual public housing lottery. Consequently, the benefits of equal sharing would have been worth about $8.30 per month to each eligible family, or about two-thirds more than under the actual program.[9] By providing relatively large increases in housing to relatively few families, the public housing program has produced only about three-fifths of the direct benefits it might have.

Not only have the benefits of the public housing program been considerably fewer than they might have been, but considerably less housing has been produced by it than could have been had resources been more efficiently used. There are two major reasons for this. First, during the 1950's, about three-eighths of the dwelling units were built on cleared slum land.

[8] The details of the calculations are described in Muth, *Public Housing*, op. cit., pp. 55–57.
[9] Ibid., p. 27.

Such land cost an average of $1.12 per square foot, as compared with only 9 cents for other land used for public housing.[10] Building on higher cost land has led not only to greater expenditures for land per dwelling built, but also to greater expenditures on construction. The latter occurred because, in seeking to economize on more costly land, builders build taller buildings at greater expense. I have estimated that because of building upon cleared slum land, public housing built during the 1950's cost about 20 percent more than it would had all units been built upon other than cleared slum land.[11]

Not only have demolitions of slum housing to provide public housing sites substantially increased the cost of the program, but they have also partly negated the increase in the low income housing stock the public housing program has provided. As of 1968, about two-thirds of a million public housing units had been built. Yet according to the Douglas Commission,[12] almost half as many private units had been demolished by the program.

The other factor which unnecessarily increases the cost of the public housing program is the form of the Federal subsidy. Under the public housing program, the Federal Government has paid 90 percent of the interest and amortization on bonds issued by Local Housing Authorities (LHA's) to finance acquisition of the structures they manage. The interest on these bonds, like most other debt obligations of local government, are exempt from Federal personal income taxation and carry interest rates that are perhaps half the rates on taxable bonds of the same riskiness. Further, LHA's pay no local property taxes. For all these reasons, as I have argued earlier, expenditure on real estate that would cost a private developer a dollar a year costs the LHA only 5 cents a year.[13]

The latter, then, in designing structures containing public house dwellings, has a strong incentive to use more capital than a private developer would. In part this is done by building high-rise structures, in part by substituting more expensive materials in construction which require less maintenance, and in part by offering tenants larger and better-equipped units in lieu of later maintenance and operating expenditure. According to my estimates, the quantity of real estate used by public housing is about 37 percent greater because of the form of the Federal subsidy.[14] The nature of the subsidy also has meant that the costs per unit of public housing have been about 21 percnt greater than they would have been in the absence of the subsidy. Together, the building of public housing on cleared slum land and the capital cost subsidy have increased capital expenditures on public housing by about 63 percent. In the absence of these features, about 56,000 units could have been built annually during the 1950's for the same Federal expenditure as the 35,000 actually built required.

Other Federal Programs

In recent years there have been many changes in the public housing program, and several new housing programs have been introduced. By and large, however, these programs have retained the principal shortcomings of the public housing program. With the exception of the rent supplement program, for example, in all programs the principal subsidy payment is a subsidy to capital costs. For this reason, part of the excessive resource cost of the public housing program is carried over into more recent programs. And in all, a relatively small part of the low income population has been provided a relatively great increase in their housing consumption. Most of the low income population, however, has received no direct benefit from any of the programs. Consequently, the average benefit per lower income family is smaller than it might have been.

The failure of recent developments in Federal housing programs to correct the major faults of public housing is well-illustrated by two recent modifications to it. Under the turnkey process, a private developer builds a development on his own site to his own plans and specifications and sells it to the LHA. By permitting competition in the development of public housing projects, the capital costs of such projects are reduced. Because its capital expenditure is subsidized, however, the LHA has the same incentive to buy developments that use more capital relative to current expenditure as in the projects it would have developed itself. Under the leased housing program permitted by Section 23 of the 1965 Housing Act, the LHA leases units on the private market and subleases them to lower in-

[10] U.S. Housing and Home Finance Agency, *Fourteenth Annual Report, 1960* (Washington: Government Printing Office, 1961).
[11] Muth, *Public Housing*, op. cit., p. 13.
[12] National Commission on Urban Problems, *Building the American City*, op. cit., Table 6, p. 8.
[13] Muth, *Public Housing*, op. cit., pp. 17–18.

[14] Ibid., pp. 19–20. The capital cost subsidy need not affect the density of projects since the costs of land and structures erected on it are reduced in the same proportion.

come tenants. Leasing offers some of the benefits of housing allowances discussed in Section 4 and may avoid the substitution of initially heavy capital expenditures for later maintenance. Tenants, however, must still bear the costs of household operation out of their own resources. Both under turnkey and leased housing, moreover, relatively few families receive relatively large increases in their housing consumption. The direct benefits of the program are thus much lower than they might be as in conventional public housing.

The fact that capital costs alone are subsidized has probably been responsible for the widespread defaults under the Section 235 homeownership program for lower income families. Under the program, lower income families have been able to purchase housing with as little as a 1 percent downpayment. Especially in the early years of their ownership, these families have little equity in their homes. In older housing of any price range, unanticipated major repairs are sometimes needed; a furnace, plumbing, or wiring may need replacement sooner than anticipated. The program made no provision, however, for assisting homeowners with repair, maintenance, and other operating expenditures. With little equity in the homes they owned, it was cheaper for many families to give up their homes and default on their mortgages than to incur the unexpectedly heavy repair bills.

Of all the recent modifications in Federal housing programs in recent years, the rent supplement program is perhaps the most promising. Because the tenant's rental payment, rather than the dwelling's capital costs only, is subsidized, builders of rent supplement projects have no financial incentive to increase the expenditures they make for real estate at the expense of later maintenance and operating expenditures. In addition, by allowing rent supplement payments to be made to any nonprofit or limited dividend corporation, a greater degree of competition among suppliers of federally assisted housing is permitted. A greater degree of competition would permit cheaper housing than in the public housing program, where, until recently, the LHA was the single developer permitted.

Although the rent supplement program allows for a wider degree of developer participation than the public housing program, it does not go far enough. Developers are permitted to earn no more than 6 percent on their equity investment. Most individuals can earn considerably more in common stocks—9 to 13 percent, if the historical record is any guide. Hence, fewer developers are likely to be attracted to the provision of rent supplement housing than if any profitmaking developer were permitted to participate. Also, those developers who are attracted to the program are likely to be less experienced in the construction and management of housing than are profitmaking developers. In addition, like other Federal housing programs, a rent supplement project must have the approval of the local government having jurisdiction over its proposed location. The governmental units thus have the same ability to limit rent supplement projects to certain areas of the city or to keep them out entirely as in the case of public housing.

As in the case of the public housing program, recipients of rent supplements are expected to spend a fixed fraction of their incomes for rent. The amount they spend on housing does not depend upon the size unit they inhabit. Potential tenants, then—though probably preferring even a smaller unit than they are able to obtain through private housing—have every incentive to find as large a dwelling as they can and are limited only by the availability of units. Because far fewer units would be available under the program than potential tenants, the latter limitation is a severe one for any individual family, of course. In developing rent supplement projects, however, developers have no incentive to limit the size of, and hence expenditures on, any individual units either, since they in effect operate under cost-plus contracts. It thus falls upon the Federal Government to impose elaborate review procedures to limit expenditures per dwelling under the program. These procedures, of course, increase the costs of the program, both to the Federal Government and to developers of rent supplement projects.

Housing Allowances

Under housing allowances, recipients of Federal assistance would be permitted to purchase housing of their choice which is available on the private market. The subsidy received, together with a part of the recipient's income, would be used in making the rental payment for the dwelling inhabited. Such programs have never been instituted on a wide scale in this country. A small experimental program was recently completed in Kansas City, however, and more comprehensive experiments are currently being undertaken by the Department of Housing and Urban Development. In my judgment, such a program has great promise. In this section, I want first to outline the advantages I see in a housing allowance program and to consider some objections to it. I will then discuss certain specific features that I believe would be desirable ones for an actual Federal housing allowance program.

Advantages and Limitations

Earlier in this paper I argued that one of the greatest shortcomings of Federal housing programs has been that they have provided housing assistance to a relatively small fraction of the lower income population. This is inevitable under programs anywhere near the size of current ones so long as assistance is provided through newly constructed housing, as has been primarily the case under the public housing program and others. By so limiting the number of recipients and providing each with a substantial increase in his housing consumption, the benefits of the housing assistance are smaller than they could be if more equally distributed among the lower income population.

Under a housing allowance program, however, it is generally contemplated that Federal assistance could be used in acquiring any unit available on the private market, not just a newly constructed one, as in the case of the rent supplement program. The assistance would be provided either by a certificate redeemable in cash by the recipient's landlord, or directly in cash to the recipient himself upon presentation of a rent receipt for the previous month. Consequently, there is no lower limit to the feasible amount of assistance to any one recipient nor any barrier to widespread distribution of Federal assistance among the lower income population.

Another advantage of housing allowances is that the subsidy would be one to the tenant's rental payment, not to the capital costs incurred by the project developer. For this reason, the wastes inherent in subsidizing capital costs—but not current expenditure—would be avoided. If it were cheaper for private producers of housing to provide better dwellings to subsidy recipients by making minor improvements to already existing units, they could do so. The dislocations associated with the demolitions of poor quality housing would be avoided. Rather, the owners of poor quality dwellings on the private market would be given the financial means and incentive through the enhanced rental expenditures of their tenants to rehabilitate these dwellings.

Not the least of the advantages of housing allowances is that they would provide for a greater degree of competition among suppliers of federally assisted housing, thus reducing its costs. Under most past Federal programs, the suppliers of federally assisted housing have been greatly limited. In the public housing program, for example, the LHA is the only supplier in a city, while in the rent supplement program only nonprofit and limited dividend corporations may take part. By allowing a greater degree of competition among suppliers, inefficient producers would be driven out by more efficient producers and costs lowered.

In similar fashion, housing allowances would allow a wider range of choices by subsidy recipients. Under most Federal housing programs, a lower income family is fortunate, indeed, to obtain assistance at all, let alone to have a choice among federally assisted units. Under a housing allowance, however, the subsidy recipient would receive cash or its equivalent to spend on housing wherever it might be available. By this means, recipients of Federal assistance would not of necessity be concentrated in certain parts of the city, as they have been historically under other Federal programs. Such a plan would almost surely promote freedom of residence of lower income families to a far greater degree than by any other conceivable means. For it would be exceptionally difficult for anyone to prevent tenants and landlords to enter into rental agreements which they thought mutually beneficial. For a variety of reasons, however, it is likely that housing allowance recipients would still tend to cluster in older, central city housing.

Probably the most common objection to housing allowances is that they would merely "line the pockets of landlords" without leading to any improvement in the housing of the poor. I have already commented on this belief in the second section, where the alleged unresponsiveness of the private housing market was discussed. I have little to add here except to repeat my belief that this view is mistaken. It is mistaken in part because it neglects the fact of competition among private landlords. It is also mistaken, in part, because it neglects the evidence of the postwar period and the great improvement in average housing quality that has taken place. Indeed, it is most mistaken of all, perhaps, in that objectors rightly believe that little new housing would be built under a housing allowance program. Yet new housing or massive rehabilitation is not the only means of housing improvement, nor indeed has it been the major avenue of improvement for the central city dweller in the postwar period.

Another, although related, objection to housing allowances is that they would not be large enough to permit recipients of Federal assistance to acquire standard, "decent," or "safe and sanitary" housing. Whether or not they would do so depends upon the total amount of Federal assistance provided and the number of families to whom assistance is supplied. Earlier, I noted my estimate that the public housing program in the mid-1960's provided an average increase in housing consumption of about $130 per month to perhaps two-thirds of a million families. If the same number of families were given $130 per month to spend on privately produced housing, I predict that they could improve their housing by at least as much as in public housing. If, however, the same total assistance were equally divided among all lower income families, each would receive somewhat less than $10 per month. Although this would permit about a 20 percent increase in housing consumption per family per month, no single family would be able to improve its housing as much as the tenant of public housing can. As I have argued several times earlier, however, the aggregate benefit to the lower income population would be greater under an equal division of the Federal assistance.

Some Specific Recommendations

On the basis of the previous considerations in this section, I believe a housing allowance program would be a significant improvement in Federal assistance to housing for lower income families. Many decisions would have to be made about any actual Federal program, far too many even to list, let alone to discuss, in a paper of this size. In the remainder of the paper, then, I wish to consider briefly what I feel to be the most important decisions that would have to be made in designing such a program.

First, in order to maximize the benefit to the lower income population, I would recommend that the benefits of the program be made available to the whole of this population. The average share would be small, of course; an average subsidy of only $25 per month paid to 10 million families would require expenditures of $3 billion per year. All lower income families, however, would be enabled to improve their housing as a result. Further, with relatively small payments per family, a large number of poorer housing units would be upgraded. To repeat, however, the principal reason for this recommendation would be to maximize the program's benefits. Doing so would avoid, insofar as possible, the dilution of benefits associated with the reduction in the value of additional housing that larger subsidies to fewer families would bring.

Second, I would recommend that the payment made to any family be a fixed dollar amount. Under some current programs, including public housing and rent supplement, tenants are expected to pay a fixed percentage, frequently 25 percent, of their income as rent. The Federal subsidy pays the balance. Under these conditions, only the availability of subsidized units limits the size dwelling a tenant would try to obtain. If, however, the subsidy is paid as a fixed dollar amount of the probable average size just noted, each tenant would spend some of his own funds in addition and thus bear the full cost of the last room, or 100 square feet of floor space, rented. The tenant would thus have the same incentive to weigh the worth of his expenditure on housing as he does any other private expenditure. Indeed, the housing allowance recommended here would be essentially equivalent to an income subsidy.

Third, it would seem reasonable to pay higher allowances to larger families, as is done in effect under current programs by providing larger units to larger families. Under current programs, however, the effective subsidy per family declines as the family's income increases. What is, in effect, a tax on additional income earned is thus imposed. Although one would prefer not to impose such a tax, the only alternatives are either to pay the housing allowance to the whole population or abruptly to cut it off once a certain upper limit on income is reached. This last is one of the more adverse features of the public housing program, where a tenant must move out once his income exceeds certain limits. Under the housing allowance, of course, the tenant could remain in his dwelling once his subsidy ceased by paying its rental out of his own funds. Especially because any tax on additional income would be small under the proposed housing allowance program compared to those imposed by Aid to Families with Dependent Children and the Social Security Payroll Tax, I would prefer a gradual reduction in the size of the subsidy as income increases, rather than abruptly cutting it off.[15]

[15] The subject of the effect of transfer payments on labor supply, whether or not they are made in-kind as in housing programs, is far too complex to discuss adequately in a paper such as this. In my judgment, the principal labor supply reduction effect of transfer payments results from the guaranteed minimum income they provide rather than from the marginal tax on earnings they impose.

Fourth, under a housing allowance program, no attempt should be made to require that the dwelling inhabited meet certain administrative standards as to its quality. Given the probable total amount spent on any Federal program, to do so would almost certainly mean that subsidy payments would be made only to a fraction of the lower income population. Further, so restricting the dwelling choice of subsidy recipients would greatly increase the administrative cost of the program. Not only would dwellings have to be checked for eligibility, but, with a larger subsidy payment per family, controls would have to be instituted to insure that the whole of the subsidy payment was spent for housing. Admittedly, not requiring that housing inhabited by subsidy recipients meet certain minimum standards raises the serious question of political feasibility. I do not pretend to be at all expert on this latter question. It should be understood, however, that giving in too readily to considerations of political feasibility would greatly reduce the potential economic benefits of a housing allowance program to lower income families.

Finally, let me repeat that the potential benefits of allowing the subsidy to be spent on existing housing owned by profitmaking landlords are great. Not only would housing be made available at a smaller cost to lower income families, but the scope of their residential location choices would be enhanced. Subsidy recipients, however, should be allowed to rent housing provided by limited-dividend corporations and public authorities as well. Doing so would provide a check on the rentals that profitmaking landlords could charge. However, public or quasi-public bodies should be required to raise the whole of their revenues from the rentals of their tenants. In particular, no capital cost subsidies, tax credits, or exemption from local property taxes should be permitted these organizations, as is now done in the public housing program.

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Housing Policy as a Means to Achieve National Growth Policy

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This paper is in two parts. Part 1 is concerned with the rationale for a national policy to influence sizes of urban areas and with housing as an instrument of such policy. Part 2 is concerned with narrower grounds for a national housing policy. Part of a national growth policy ought to be the attempt to improve the functioning of housing markets, even if it is not intended thereby to affect sizes of urban areas.

In this paper the term "urban areas" is used generically to refer to a contiguous area where population density is much higher than in surrounding areas. The term is used without regard to boundaries of local government jurisdictions. Other terms, such as standard metropolitan statistical area (SMSA) and central city, will be used with Census Bureau meanings.

Part 1 of the paper is concerned exclusively with policies directed at sizes of urban areas. It is not concerned at all with the internal structure of urban areas. Specifically, it is not concerned with the serious problems of the relationships between central cities and suburbs.

The Pros and Cons of a National Policy to Influence Urban Sizes

The Sizes of Urban Areas

On a worldwide and historical basis, the size distribution of urban populations is as well documented as any social phenomenon. National censuses in almost all countries collect data on numbers of urban areas in various population size classes. In the United States, usable data on size classes of urban populations go all the way back to the first census in 1790. For many decades, scholars in many countries have performed statistical analysis of urban size distributions. Although interest seems to have tapered off somewhat in recent years, it appeared for a while that analyzing urban size distributions might become a demographic subspecialty. A good survey and analysis of earlier work is by Berry and Garrison [4]. An elaborate analysis of U.S. data is by Madden [11].

A universal conclusion of urban size distribution studies is that urban sizes vary enormously within a country or large region at every point in history. Every country has large numbers of urban areas clustered near the minimum size that is recorded, usually between 2,000 and 10,000. And every country has at least a few urban areas that are 10 or 100 times that size. In the 20th century, most large countries have at least a few urban areas that have populations in excess of a million. In the United States, there are, of course, more than 30 SMSA's with more than a million population.

A second universal conclusion of urban size distribution studies is that urban size distributions are highly skewed, with large numbers of small urban areas and a few very large ones. A statistical distribution which embodies this skewness notion is the rank-size rule, which says that the population of the urban area of rank n is proportionate to 1/n. In an earlier period, many scholars thought of the rank-size rule as a natural law of urban sizes. But perceptive students of the subject now realize that any of several closely related skewed distributions, such as log-normal distribution, fit most of the data about equally well.

The following are other important conclusions of urban size distribution studies:

1. The distribution varies considerably from country to country. In particular, the sizes of the largest metropolitan areas relative to the sizes of other large metropolitan areas vary greatly from country to country. This concept is referred to as primacy. The most common measure of primacy is the population of the largest metropolitan area divided by the sum of the populations of the four largest metropolitan areas. Industrialized countries mostly have smaller primacy measures than developing countries. The United States has a smaller primacy measure than most industrialized countries. See Mills [13].

2. The size distribution of urban areas changes only slowly over many decades within a country. In the United States, although the number and sizes of urban areas have grown rapidly, the size distribution has changed little in nearly 200 years. See Madden [11].

3. National policy can affect the size distribution of urban areas, but it requires massive national control over land use and construction. This statement is based on the experience of countries that have tried to control the growth of large urban areas in various ways. For example, governments in the United Kingdom have tried to slow the growth of London and the southeast of England since World War II by a variety of land-use controls and modest subsidies for people and businesses to locate elsewhere. But it has had no perceptible effect. Israel, on the other hand, has had a determined policy of population dispersal since independence in 1949, based on military and other considerations. The instruments of the policy have been large scale public ownership of land and complete central government control over construction. The result has been that Tel Aviv, the largest urban area, has grown little, and most population growth has occurred in small urban centers. See Mills [14].

The Economics of Urban Sizes

Unfortunately, economists have devoted relatively little attention to the determinants of the urban size distribution. Almost all the work that has been done stems from the work of Lösch [10]. The best recent theoretical paper is by Beckmann and McPherson [3].

The most basic reason for the observed urban-size distribution is that urban areas perform a variety of functions, and such functions are associated with scale economies that necessitate markets of various sizes. The smallest urban areas are mostly market and service centers for surrounding rural areas. These are activities that can be carried on efficiently on a small scale, and therefore a town in which they are performed needs only a small market area. Larger urban areas perform a variety of production and marketing activities. Some writers have identified manufacturing centers, regional marketing centers, national service centers, national financial centers, etc. See, for example, Duncan [5].

It is, however, a mistake to believe that all the urban areas in a particular size class perform the same set of functions. There is, in fact, great diversity in the amounts of various goods and services produced among urban areas in a given size class.

The theoretical analyses of urban size distributions have been based on the assumption that the geography of the country is undifferentiated. This is far from true. Geographical diversity has profound effects on the sizes and locations of urban areas.

Geographical diversity is of two kinds. First, natural resource availability differs from one region to another, and that helps to determine the comparative advantages that urban areas have in each region for producing certain kinds and amounts of goods and services. Second, geographical diversity means that certain places are much more favorably situated than others to ship and receive goods to and from other regions and countries. Navigable waterways are, of course, the main geographical features of this kind. Their importance is attested to by the fact that almost all large urban areas in the United States, and much of the postwar urban growth, are in places where navigable waterways give easy access to other regions and countries.

The observed urban-size distribution at any point in history is the result of these technical, economic, and geographic considerations. The similarity of urban size distributions among remarkably different societies, and especially over long periods of time, indicates that powerful and pervasive forces determine the relative sizes of urban areas.

I conclude this section with some summary statistics about the U.S. urban-size distribution.

First, the United States is less dominated by its largest metropolitan area, New York, than are many industrialized countries. See [13]. For example, the ratio of the population of our largest metropolitan area to the sum of our four largest metropolitan areas is less than that of France, West Germany, Japan, the Soviet Union, and the United Kingdom. In absolute terms, the New York standard consolidated area is, of course, among the world's largest. But it is not larger than the Tokyo area, even though Japan has less than half the U.S. population. And it is not much larger than the London area, even though the U.K. population is only about a quarter that of the United States. Perhaps more instructive is a comparison between the New York-Washington complex and the London-Manchester and Tokyo-Osaka complexes. All three complexes have roughly the same population and population density, again despite the large differences in the sizes of the countries.

Second, the United States has become progressively less dominated by its largest metropolitan areas in recent decades. The New York metropolitan area's population as a share of U.S. population fell from 8.9 percent in 1940 to 8 percent in 1970. As a share of total metropolitan population, it fell from 18.6 percent to 11.8 percent during the same period. The 10 largest metropolitan areas decreased from 51.8 percent of all metropolitan areas in 1940 to 39.3 percent in 1970.

Of course, these trends do not prove that our largest metropolitan areas are not too large. But the comparisons just made certainly do not lend support to the contention that our largest metropolitan areas are too large.

Human Welfare and Urban Sizes

In the last section, I discussed economic determinants of urban size distributions. In this section, I discuss the extent to which these economic forces produce a desirable urban-size distribution. The issue is whether a different urban-size distribution would be more efficient in promoting human welfare than the size distribution mainly determined by market forces and individual choices.

The first thing to observe is that it really makes no sense to talk about the optimum size of an urban area. Many popular writers discuss the best urban size, and some people have even conducted surveys to discover the urban size that people prefer. Most of this writing is unhelpful in studying welfare aspects of urban sizes because it takes as given many conditions of life that depend on urban sizes. Most such inquiries take as given the respondent's income and employment. But the implication of the theory and the evidence discussed in the previous section is that income and employment opportunities are not independent of the urban size distribution. Large urban areas have grown up because they have been able to offer more favorable income and employment opportunities than urban areas of other sizes. The crudest direct evidence of the importance of large urban areas is that no highly industrialized economy exists without at least one extremely large urban center containing millions of people and usually 15 or 20 percent of the country's population. See Davis [23] for a summary of the evidence. More directly, the evidence is that, despite the massive growth of large urban centers in the United States since 1940, incomes there are still considerably higher than in small urban centers and rural areas. See Hoch [8] and Mills [12, Chs. 9,10].

The right question to ask about optimum urban sizes is, "Would you prefer to live in a city of size A at an income B rather than in a city of size C at an income D?" The key point is that this is precisely the question that market choices put to people. If because of its large size or other reasons, city A is a less pleasant place to live than city C, then wages and salaries first compensate for undesirable features of each city. Nobody should think that this equilibrating process works perfectly. There are rigidities in both wages and prices. But there are large interurban differences in wages and employment opportunities, and they are important factors affecting the movement of human and other resources.

Of course, these processes of adjustment are long run in nature. But many studies, some of which will be referred to below, have shown that income and job opportunities are among the prominent causes of migration. It is clear that the massive rural-to-urban migration since World War II has been in large part a successful search for better economic opportunities. Likewise, the rapid growth of the Southwest and the Gulf States has resulted from the emergence of industries that could produce efficiently in those areas and would enable people to obtain the amenities of warm climates.

None of the foregoing is meant to suggest that everybody could improve income and employment opportunities by moving to large urban areas. Rather, the implication is that a high productivity economy requires a distribution of urban sizes, a few very large centers and many small ones. It is also important not to overemphasize the precision of our knowledge. Nobody knows exactly what loss of efficiency would be entailed if New York or Chicago had 5 million fewer people. All that can be said is that the small amount of available theory on the subject, and a considerable amount of direct and indirect evidence, fail to reveal any reason to believe that our large urban areas are too large.

This analysis leads to the conclusion that, if wages and salaries reflect the advantages and disadvantages of life in urban areas of different sizes and locations, then market forces will produce an optimum distribution of urban sizes.

Distortions Affecting Large Urban Areas

Why might economic opportunities not properly reflect the advantages of urban areas of various sizes? The answer most often given in the serious economic literature, such as [16], is that the growth of an urban area, either by migration or natural increases, might provide advantages to the newcomers that would induce them to live there, but that this growth of population might impose costs on other residents of the urban area. If so, migration decisions would fail to take into account all the social costs of migration, and a distorted distribution of urban sizes might result.

To be quite specific, consider the following example. Suppose a person lives in B and earns $7,000 per year. Suppose he leaves for a job for which he qualifies in A that pays $10,000. Suppose B is a small town and A a large urban area and that the person decides that the extra amenities of small town life are worth $2,000 a year to him. Then the move will improve his standard of living by $1,000 per year and he will make the move. Now suppose that each new resident of the large urban area adds to congestion there and that the marginal congestion costs to all residents of A resulting from the addition of a new family to A's population are $1,500 per year. (Suppose congestion costs in B are negligible.) Then the person is induced to make the move from B to A by market incentives even though total social costs of the move exceed total social benefits. The conclusion is that too many people will be induced to move to large urban areas and that their populations will be excessive relative to smaller urban areas.

This situation has been analyzed in an important paper by Tolley [21]. If the costs imposed on others are a function only of the urban area's population and if these costs are larger—the larger the urban area—then the conclusion is correct. Market forces will induce too many people to live in large cities and too few to live in small cities. That is, there will be too much dispersion in the size distribution of urban areas.

The key fault in this analysis is that costs imposed on urban residents are not a function just of the urban area's population. They depend specifically on how resources are allocated in the urban area. Suppose that whatever disamenity that results from large urban populations can be lessened by the use of resources for the purpose. Suppose further that there is a way of charging residents for the cost of the resources needed to reduce the disamenity. Then the use of resources to reduce the disamenity has two effects. First, it makes life in the urban area more expensive because residents have to pay the cost of resources to reduce disamenities. This induces people to live elsewhere and thus reduces the urban area's population. Second, it increases the amenity of life in the urban area. This has the opposite effect: It increases the urban area's population.

There is no way to predict the net effect on the urban area's population of the use of resources to improve amenities. It may increase or decrease. Much more important, it does not matter. The right issue for public policy is to find the justifiable amount of resources to devote to improving amenities in the urban area. That may increase or decrease the urban area's population. Whichever happens, public policy need not be concerned.

The foregoing is really an abstract and theoretical way of saying something that is merely good common sense. If there is a problem, it is much better to work on the problem than on a related phenomenon. The implication of this analysis is that public policy should aim to improve resource allocation in urban areas, but should not concern itself directly with the size distribution of urban areas. If resources are allocated appropriately, the size distribution of urban areas will take care of itself and need not be the object of specific programs. It may, of course, nevertheless be affected by public policies to improve urban resource allocation.

A variety of social disamenities is sometimes said to result from large urban size. An interesting analysis of the relationship of several such amenities to urban size is by Hoch [8]. I will illustrate the preceding theoretical analysis with some more detailed remarks concerning air pollution.

Air pollution is correlated with urban populations, although not strongly. With given techniques of production and given modes of transportation, larger urban populations and higher densities impose greater stress on the natural capacity of the urban area's air mantle to absorb the effluents discharged to it. The correlation is not high because air pollution indexes also depend on natural conditions and on the mix of economic activities in the urban area. The desirable public policy to deal with air pollution over an urban area is to limit discharges of pollutants to the air to the extent justified by benefits and costs of doing so. This can be done by regulating discharges or by effluent fees or by some combination of the two. Whichever way it is done, the cost of abatement should be imposed on those activities that result in effluent discharges. That will make those activities more expensive in this urban area and will, to some extent, limit the growth of the urban area's population. It will also cause resources to be devoted to abatement of discharges. That will increase the attractiveness of the urban area and will induce people to live there. The net effect may be to increase or decrease the urban area's population. But it does not matter. The important thing is that the atmosphere will be cleaned up to the extent that it is justifiable to do so. The effect on the urban area's population is incidental and is unlikely to be large.

As a practical matter, public policies to limit population growth of large urban areas directly are likely to have little effect on air pollution. The reason is that air pollution depends mainly on specific urban activities such as burning of fossil fuels and trash in specific and uncontrolled ways. Limiting population growth will have little effect on these activities. They need to be controlled directly by planning, regulation, taxation, etc.

The conclusion of this section is that there is no justification for a public policy that attempts to limit the growth of large urban areas. Historical comparisons and comparisons with other countries provide no evidence that our large urban areas are too large. Disamenities of urban areas, such as congestion and pollution, are only loosely related with urban size and should be dealt with by controls on specific activities that cause the disamenities. Effects of such controls on urban populations are incidental and unpredictable.

Distortions Affecting Small Urban Areas

Sometimes it is claimed that small urban areas are subject to distortions of a similar but opposite nature to those discussed in the previous section.

The most common claim is that if large urban areas are too large, then small urban areas must be too small. A variant is that urbanization is emptying small towns and rural areas of people and that public policy must try to reverse the flow. But, as I have said above, I do not accept the premise that big urban areas are too big. Therefore I do not accept the conclusion that small towns are too few or too small. As a practical fact, it is not true that small towns are being emptied of people. There is no evidence that the lower tail of the urban size distribution has changed in recent decades. The total number of people in rural areas has certainly grown, although their percentage has fallen. Of course, the massive migration of people to urban areas has resulted in large shifts among the rural population. This inevitably means that some rural areas have lost population.

A more sophisticated argument is that some small towns with a great growth potential are unable to realize that potential because they cannot reach a size at which they can realize scale economics. Crudely interpreted, the argument is faulty, because large numbers of relatively small urban places have reached substantial sizes in recent decades. On a somewhat more sophisticated level it can be argued that small urban areas must be placed in the urban hierarchy. Many of them serve rural areas and were prevented from growing because of the smallness of the rural market which they serve. Thus the fact that they could function more economically if they served larger markets does not imply that they should be larger.

The most sophisticated form of the argument is similar to the infant industry argument in international trade. It used to be argued that domestic industries had to be protected from foreign competition until they reached efficient size. So it is sometimes claimed, small towns, especially those with growth potential, must be assisted with outside funds until they are big enough to realize their potential. There might be something to this argument in a poor country in which development capital was scarce and expensive, and where there were few urban centers. In such countries there are often large-size gaps between the biggest urban areas and the rest. But the United States has a large number and a full range of urban areas. Urban areas grow and shrink throughout the size distribution, and there is no evidence of particular size barriers. Development capital is relatively plentiful and is mobile. In addition, the required magnitudes are not large by comparison with amounts of industrial capital. Including housing, the national capital stock is about twice the annual output. GNP is about $4,000 per capita, and reproducible capital about $8,000 per capita. (These figures are from 1970 data.) Thus, for an urban area to grow from 25,000 people to 50,000 people requires an investment of $200 million. This is less than the assets of a relatively small corporation, and much of the investment, especially the structures, provides excellent collateral. This suggests strongly that communities that are perceived to have genuine growth potential should have little trouble attracting the public and private capital over a period of years.

A final practical point is that I have little confidence that public officials could be successful in identifying urban areas with strong growth potential. Urban growth is a result of thousands of decisions, each decisionmaker searching for the most advantageous allocation of his resources. Many decisions turn out badly, and urban areas that grow are the result of a cumulation of successful decisions. I am confident that the national government can improve on this process.

Housing as an Instrument of National Urban Growth Policy

The conclusion of this paper as to this point is that there is no justification for the Federal Government to attempt to alter the size distribution of urban areas. In this final section on the subject, I want to argue that, even if it were desirable to alter the urban size distribution, housing policy would be a poor instrument for doing so.

Many migration studies have shown that employment opportunities are an important determinant of migration patterns. See [15], [17], and [22]. The most important consideration in most decisions to move is improved job opportunities. To the best of my knowledge, no important migration study has shown housing cost or availability to be a major factor in migration decisions. These findings confirm common sense. If good job opportunities appear in a community, people will migrate there, and market incentives will result in new housing. To reverse the procedure, and try to induce people to move by making housing, even subsidized housing, available is to put the cart before the horse. If it were decided that there should be a national policy to alter the urban size distribution, the focus of the policy should be the creation of jobs in areas where growth was to be encouraged.

Other Reasons for Federal Intervention in Housing Markets

The conclusion of Part 1 is that there is no justification for using housing policy to affect the size distribution of urban areas. In Part 2, I discuss other grounds for Federal intervention in housing markets. Residences constitute nearly a third of the Nation's reproducible capital, and housing expenditures exceed 10 percent of personal income. These figures are merely the statistical counterpart to the fact that—next to food—housing is the most important commodity in determining our standard and style of living. Clearly, optimum national growth policy requires that the Federal Government do anything it can to improve the efficiency of a sector that is such a large part of the economy and of human welfare.

The importance of the housing sector makes it equally important that the Federal Government not adopt programs that will impair the sector's performance. President Nixon said that many Federal Programs had precisely that effect, and I am sympathetic to that view. I believe that past public policies have underestimated the capability of private housing markets. I thus start Part 2 with a careful discussion of exactly what national housing policy should try to accomplish.

Housing as an Antipoverty Instrument

As with any public policy issue, it is important to distinguish equity from efficiency goals in housing policy. By equity goals I mean the use of housing policy to redistribute income from the nonpoor to the poor population. This has in fact been a major goal of past housing policies. The argument has been that because poor people cannot afford decent housing, the government should foot part of the bill by subsidizing public or private housing for the poor.

The view taken in this report is that income redistribution should not be a major goal of housing policy. Of course, any policy designed to improve the efficiency of housing markets will have some effect on income distribution, and the proposal made later in this section would indeed redistribute some income from nonpoor to poor people. But the income distribution effects of policies based on efficiency arguments are incidental and usually negligible.

Why should housing policy not be used to redistribute income? The answer is that housing policy is an inefficient means to redistribute income because it results in less improvement in recipients' welfare per dollar of government funds than do alternative redistributive mechanisms. It is a standard textbook result in economic theory that a given expenditure of public funds results in greater improvement in recipients' welfare if they are given money or general purchasing power than if the funds are spent to subsidize specific commodities.

In more practical terms, the implication of this is that a housing subsidy big enough to have a significant effect on income distribution would have to be large relative to housing expenditures. Since even the poorest groups spend less than a quarter of their income on housing, a housing subsidy that added only 10 percent to their incomes would have to be 40 percent of their (presubsidy) housing expenditures. That inevitably induces recipient groups to spend more than is in their interest on housing. In addition, since the supply of low income housing is less than perfectly elastic, it means that an excessively large part of the subsidy is eaten up by inflated housing prices.

Finally, the magnitude of the subsidy required to have a substantial effect on income inevitably tempts those responsible for administering programs to do so in ways that entail favoritism and, in extreme cases, corruption. It seems likely that the scandals in connection with existing housing subsidy programs resulted at least in part from the fact that large subsidies were potentially available. That tempts potential recipients to attempt to influence program administrations in unethical and sometimes illegal ways.

Of course, no means of redistributing income is free of all distortions. If less distorting mechanisms of income redistribution are realistically unavailable, then large housing subsidies may have to be used. Although the subject is beyond the scope of this report, I believe other, and better, means of income redistribution are available. The President's Family Assistance Plan is an example of a better means, as are various negative income tax programs that have been proposed and tried on experimental cases.

Housing and Neighborhood Effects

I turn now to the issue of Federal policy to improve the efficiency of housing markets. Homes are built, exchanged, maintained, improved, and demolished by private market decisions. The issue is whether competitive private markets perform these functions efficiently and, if not, whether Federal intervention could improve the situation.

There is an enormous and confused literature on the subject. The catalog of alleged causes and consequences of poor housing market performance is almost endless. I cannot survey this literature here. A brief survey and some references are in Chapter 10 of my text. See [12]. I believe there are only two causes of housing market failure that are so important and pervasive that the Federal Government might be able to do anything about them.

First is real estate taxes. Local governments raise most of their revenues by real estate taxes, and there is no prospect of changing that fact in the foreseeable future. The annual flow of housing services is usually estimated to be 10 or 15 percent of the house's market value. Urban real estate taxes are usually 2 or 3 percent of the houses' market value. Those figures suggest that real estate taxes are equivalent to a sales tax of between 10 and 30 percent of housing services. I will use 20 percent for illustrative purposes. A 20 percent sales tax obviously deters consumption of the taxed commodity. If, as the best research indicates, the price elasticity of housing demand is about minus one, a 20 percent sales tax on housing services will reduce housing consumption by about 20 percent. But this is obviously an overestimate of the distorting effect of real estate taxes because they are in large part simply a payment for local public services, especially public education. Starting with a paper by Tiebout [20], economists have developed the following abstract model of local government finance.

Suppose there is a large number of local government jurisdictions in a metropolitan area, and that there are several in an area where it is feasible for a given family to live. Then people can sort themselves into jurisdictions according to their demand for local public services. Those who want and can afford a high quality education for their children can live in a community where they vote the high taxes needed for such an education. In addition, they can avoid the free rider problem by zoning the community to exclude those whose houses will not pay their share of the community's high real estate taxes. The culmination of this line of research is a recent Princeton Ph.D. thesis [6], in which it is shown that, if this system of fragmented local jurisdictions works perfectly, there will be no distorting effects of real estate taxes. Each resident of each jurisdiction will correctly view his real estate taxes as payment only for the local public services he wants. If, for example, a family's income goes up, it can move to a community that provides the better housing and public services it presumably will now want. In this kind of 'Tiebout' world, real estate taxes have no distorting effect on housing consumption.

Nobody thinks we live in a perfect Tiebout world, and it is a matter of judgment how good an approximation the abstract model is. My judgment is that it is a fairly good approximation for the typical relatively high income resident of metropolitan suburbs. For such people, real estate taxes probably have little distorting effect on housing consumption. But it is certainly not a good approximation for low income central city residents. Especially if they are black, movement to suburbs is not a viable option. If their incomes increase, they can only increase housing consumption by proportionately increasing their real estate tax burdens, but with no corresponding increase in public services. In that situation, real estate taxes necessarily distort housing consumption.

It is unfortunate that we do not have precise quantitative estimates of this distortion. My best judgment is as follows: Real estate taxes are a bit more than 20 percent of the value of housing services in central cities, and a bit less than 20 percent in suburbs. But a larger fraction of the real estate tax has the distorting effect of a sales tax in central cities than in suburbs. A guess is that real estate taxes may have the distorting effect of a 10 percent sales tax in central cities, but of only a 1 or 2 percent sales tax in suburbs.

It should be emphasized that the purpose of the preceding analysis was to establish the presumption that real estate taxes are relatively much less distorting in metropolitan suburbs than in central cities. There are, of course, other distorting taxes in the U.S. economy. The corporate profit tax is an example, although the economics profession is divided concerning the degree of distortion it causes. But the point here is that, whatever their distorting effects, they pervade the economy. The foregoing argument implies that property taxes are much more distorting in central cities than in suburbs. That means that they are a greater burden, relative to their ostensible level, precisely where it can be least afforded, and that they distort housing resources most precisely where poor housing is the most serious problem.

Second is the alleged external economy from housing investment. The alleged effect applies to construction, improvement, and maintenance, so I will not distinguish among these kinds of investment in the remainder of this section. The basic contention to be analyzed here is that there are benefits from housing investment that accrue to others than those who make the investment or those who may benefit from it through a market transaction. The contention implies that competitive markets will underinvest in housing. Each investor will invest an amount such that, at the margin, his return will equal the cost to him. But if some of the return, or benefit, accrues to others, the investor fails to take it into account, and invests less than would equate the sum of all benefits and costs at the margin.

How valid is the contention? The first thing to say is that it is clearly less important than is often claimed. Some writers attribute many social evils to underinvestment in housing. For example, it is often claimed that underinvestment in slum housing breeds crime, alienation, drug abuse, and other ills. Undoubtedly, the important causes of these problems are poverty, racial conflict, etc., none of which represent housing market failures.

The real issue is a narrower one. To some extent, the price or rent that people are willing to pay for a particular house depends on the investment that has been made in neighboring houses as well as on the investment in the house in question. The magnitude of this effect is the real issue regarding external economies in housing investment. Answers are needed to conceptual experiments of the following kind. Suppose you paint the outside of your house at a cost of $1,000. That will yield you an annual flow of housing services which have a capitalized value to you of at least $1,000, or you would not make the investment. Suppose, to make the problem simple, that the paint job makes your house worth $1,000 more just after the painting than it would have been had it not been painted. Then the external economy contention is that your paint job also increases the flow of services to neighboring houses and therefore makes their houses worth more than they would have been had you not painted your house.

As a theoretical concept, the external economy argument is unexceptionable. Almost no one, economist or homeowner, doubts that the value of a house would go down if neighboring houses deteriorated badly. The important issue is the size of the effect. If a $1,000 investment in your house increased the value of all neighboring houses by only a few dollars—say 1 percent of the investment, or $10—then the effect is too small to be detectable or to be worth trying to correct. However, if the effect were substantial—say the $1,000 investment increased neighboring house values by $200, or 20 percent of the investment—then it would imply serious underinvestment by private markets in housing.

Unfortunately, to the best of my knowledge there are no estimates of this external economy. The best theoretical analysis of the subject is that by Rothenberg. See [18]. Statements by real estate professionals strongly indicate their belief in the external economy. For example, the American Savings and Loan Institute (see [2] p. 100) recommends that savings and loan associations not finance home improvements that significantly raise the cost of a house above values of other houses in the neighborhood, because such investments raise the value of the house only slightly. Almost the only attempt to quantify the matter is in a paper by Kain and Quigley [9]. Ranking appearances of neighboring houses on a scale of one to five, they show that, given the characteristics of a house, its market value is greater if it is in a neighborhood whose appearances place them high on the scale. Kain and Quigley have more data in an unpublished manuscript. But none of it permits quantitative estimates of the magnitude of the external economy.

It is clear that the magnitude of the external diseconomy falls off rapidly with distance. Residences very far away can hardly be affected by your paint job. This suggests strongly that the external economy is stronger in high than in low density neighborhoods. That implies that the external economy leads to greater underinvestment in central city housing, where densities are high, than in suburban housing, where densities are low. If the external economy were very large, it would provide strong incentive for single ownership of neighboring dwellings, especially in low income areas, where the effect is stronger than in low density high income suburbs, and where most dwellings are rented. In fact, there is little evidence of substantial common ownership of neighboring slum dwellings. See [19]. That does not prove that the external economy is negligible, because capital requirements, risk spreading, and transaction costs deter common ownership. But it does place an upper limit on the magnitude of the external economy. For example, if 50 percent of the return to home improvement went to neighboring dwellings, we would clearly see large amounts of common ownership of neighboring slum dwellings.

Based on everything I know of the subject, I find it hard to imagine that the external economy is of negligible importance, at least in high density areas. It would be amazing if it were extremely large, however. A guess that probably includes most urban areas is 5 to 15 percent. That means that a dollar of investment on a particular dwelling increases values of neighboring dwellings by a total of between five and fifteen cents.

National Housing Policies to Deal with Neighborhood Effects

Since Pigou, economists have analyzed tax and subsidy schemes to remove distortions from external economics and diseconomics. The basic argument is that private markets underproduce a commodity subject to an external economy. If there is a public subsidy to production of the commodity, that will induce markets to supply more, and consumers will, of course, consume more at the subsidized price. The right amount of the subsidy is the magnitude of the external economy evaluated at the price that clears the market. During recent decades we have developed a variety of programs to approximate this desirable situation. A recent book by Aaron [1] summarizes and analyzes these subsidy programs.

Aaron shows that by far the most important of our housing subsidy programs is the provision in the personal income tax for owner-occupied homes. The theoretically correct no-subsidy tax status for owner-occupied homes would be to require taxpayers to include in taxable income the net inputed rent of owner-occupied homes. Net inputed rent equals gross rental less the sum of mortgage interest, real estate taxes, depreciation, and maintenance expenses. Not only do we not tax net inputed rental, but also we do permit the deduction from other income of mortgage interest and real estate taxes. Aaron calculated that, at 1966 housing consumption by owner-occupiers, the tax provision reduced personal income taxes for owner occupiers by $7 billion. That figure overstates the loss of tax revenue to the government because—had the provision not been in effect—housing consumption would have been less, and therefore Federal tax revenues would have increased by less than $7 billion. For example, if the average owner-occupier were in the 30-percent marginal tax bracket, and the price elasticity of demand for housing were about minus one, then elimination of the tax provision would reduce housing consumption by owner-occupiers by about 7.2 percent. This of course, is a longrun effect.

Despite the above qualifications, the tax provision is a large housing subsidy to owner-occupiers. According to the national income accounts, personal consumption expenditures for housing were about $67.5 billion in 1966, of which about two-thirds was by owner-occupiers. These data suggest that the tax provision represents a subsidy of about 15 percent of housing costs to owner-occupiers. It is hard to imagine that a subsidy this large is justified by the considerations presented in the preceding section.

A second important criticism is that it has an undesirable regressive property. Given mortgage interest and real estate tax deductions reduce the tax liability of a high income taxpayer by more than the amount that the same deductions reduce the tax liability of a low income taxpayer. There is no justification for this to improve the efficiency of housing markets. It could be corrected easily by converting the deductibility provisions into an income tax credit under which the homeowner could credit a percentage of mortgage interest and real estate taxes against his Federal income tax liability. The percentage that would make the total value of the credit equal to the value of the existing deduction is equal to the median marginal income tax rate of owner-occupiers. Aaron [1] assumes this to be 22 percent.

An even better way to design the credit would be to make it a credit against net inputed rental income of owner-occupiers. Net inputed rental equals gross rental minus mortage interest, real estate taxes, maintenance expenses, and depreciation. Net rental is often estimated to be about half of gross rental in the United States. That would imply a credit against net rental of about 35 percent to have an equivalent effect on tax revenues to the existing deduction. A credit against net rental theoretically would be preferable to a credit against mortgage interest and real estate taxes, but it would be more cumbersome for taxpayers to compute and much more controversial. Most of the difficulty is in estimating gross rentals.

The following table compares the present deduction with a 22 percent credit by income bracket. The basic data are from Aaron [1, p. 37] and pertain to 1966. The table indicates that those with incomes below about $5,000 would

Annual Income	Marginal Tax Rate, %	Deductions	22% Credit
0–3,000	14–19	$ 3	$ 4
3,000–5,000	19–22	21	22
5,000–7,000	22–25	32	30
7,000–10,000	25–28	64	53
10,000–15,000	32–39	106	66
15,000–25,000	39–50	196	97
25,000–50,000	50–62	329	125
50,000–100,000	62–69	562	179
100,000	70	1,444	?

benefit from the swtich from a deduction to a credit, those with incomes between $5,000 and $10,000 would lose slightly, and those with incomes above $10,000 would lose considerably. Of course, the break-even income is $8,000.

Otherwise, the tax provisions are an efficient subsidy to owner-occupiers. Their main drawback is that they are unavailable to renters. The considerations in the preceding section indicate that subsidization is more justified for renters than for owners. Renters are more concentrated in central cities than owners are, and it was claimed that real estate taxes are more distorting in central cities than in suburbs. In addition, renters tend to live in higher density areas than homeowners, where the external economy is more important. I turn now to subsidy provisions for renters.

I can make only brief comments about the more pervasive objections to the programs. My comments are intended to apply to the public housing program (1937), the rent supplement program (1965), and the rental assistance programs (1968). I believe three factors account for the limited success of these programs, each of which applies to most of the programs.

First, they are needlessly complex. Their complexity stems from the fact that the programs entail direct interference in housing markets as well as subsidy. The programs require that qualifying dwellings be sound, that qualifying institutions be of certain kinds, etc. The goal of such provisions is, of course, to insure that beneficiaries obtain high quality dwellings in return for public subsidy. But that goal requires direct intervention only if the program is designed so that the beneficiary lacks incentive to get the best quality housing available for the money. The contrast is with the income tax provisions for owner-occupier. Nobody thinks that the Federal Government should intervene to insure that homeowners are getting decent housing for their subsidy. The homeowner has incentive to make the best housing bargain the market will permit. Under the rent supplement and assistance programs, on the other hand, the beneficiary stands to lose nothing if the owner overcharges the government for his housing. In addition, complex programs require substantial resources to administer, and the public intrusions into private affairs become increasingly irritating.

Second, the benefits are available only to selective groups of renters. Only a small fraction of low income renters actually obtain assistance from any of the programs. And, of course, the subsidies stimulate housing demand only for those who take part in the programs. Again, these programs contrast unfavorably with income tax provisions for owner-occupiers. Any homeowner can obtain these benefits merely by claiming them on his tax return. There are no waiting lists, no favoritism, and no delays.

Third, many of the programs entail excessive subsidies for those who take part in the programs. That is to say, a small number of needy renters receive large subsidies and the rest get nothing. This results from the goal of the programs to redistribute income as well as to improve housing markets. I have argued above that housing programs are not the best way to redistribute income. In addition, it is politically difficult to make enough money available under these programs to provide the large subsidies to all needy renters. Finally, the magnitude of the subsidies, plus the obligation to direct interference in housing markets, are an open invitation to favoritism and corruption.

Brief mention also should be made of accelerated depreciation of rental dwellings as an indirect subsidy. The subsidy results from the fact that, under certain circumstances, an owner of a rental dwelling can deduct for tax purposes depreciation that exceeds the property's loss of market value. These provisions are mainly available during the first few years of ownership. This is a subsidy, because it lowers the cost of rental dwellings and competition presumably forces a substantial part of the subsidy to be passed on to tenants.

I have seen no study of this provision, but my suspicion is that it is a poor subsidy. The reason is that it can be obtained only if the dwelling is sold every few years. That is probably not the way to encourage good maintenance practice. More important, it means that the benefits accrue mainly to dwellings for which there is a large and well-organized market. For other dwellings, the transaction costs of frequent sales eat up a large part of the subsidy. This suggests that the subsidy is most effective for large, urban, middle and upper income dwellings. It probably is of little value for slum tenements.

A Proposal for a National Housing Policy

The conclusions reached so far in section 2 are: A modest national housing subsidy is justified because of distortions from local real estate taxes, and the external economy in housing subsidy is more justified in central cities and high density areas than elsewhere; the income tax provisions for owner-occupiers are a tolerably efficient subsidy; these tax provisions are least available where they are most needed; the direct subsidy programs for low income renters work poorly.

This leads to the question of whether a housing subsidy can be devised that is free of these and other objections. Before discussing my proposal, I will make a few comments about housing allowance proposals. These are, of course, in the planning and experimental stages, and that means that there is no single plan whose characteristics can be discussed. I will classify proposals under two headings—those that entail direct interference in housing markets, and those that do not. The basic purpose of housing assistance plans is to provide purchasing power to low income families so that they can improve their housing. Proposals differ as to whether they would provide money or "housing vouchers," as to whether they would require stipulated housing expenditures, and whether they would regulate housing consumption to insure that recipients lived in standard housing.

Clearly, some of these possibilities would avoid the defects of existing programs. But I believe that housing assistance plans that entail market regulation would soon fail for the reasons given in the previous section for the failure of existing programs. They would be administratively complex and would result in the resentment, favoritism, and corruption of existing programs. A pure subsidy plan, without market interference, would be free of these defects, but has no advantages that I can see over my proposal. It would clearly be much more costly to administer.

As a consultant to the Rand Corporation, I have examined their proposed housing supply experiment. As an experiment, it can be monitored closely and should be instructive concerning supply responsiveness. But as a national policy, it has most of the defects of existing programs. Their experiment involves large-scale interference in housing markets in the form of arbitrary standards for qualified dwellings. In addition, their allowance formula impairs the tenant's incentive to seek the lowest rent for housing that meets his needs. Under the Rand formula, the allowance will be the difference between their estimate of the cost of standard housing at the experimental site and one-fourth of the family's income. The allowance will be in the form of a voucher that can only be used for rent. Thus, renters have no incentive to seek housing whose rent is less than their allowance. The resulting distortion of incentives will, of course, be most important for the lowest income housholds.

My proposal is to extend to renters the tax subsidy now available to owner-occupiers. This could be done by a provision in the tax law that would permit renters to credit against their Federal income tax liability a certain percentage of their contract rent. I have recommended above that the tax provision for owner-occupiers be converted from a deduction to a credit. Then the provision could be the same for owner-occupiers and renters. Each could credit a part of their housing costs against their Federal income tax liability. If it were desired to minimize changes in tax provisions, owner-occupiers' housing costs could be interpreted to be real estate taxes and mortgage interest. In the case of renters, housing costs would be contract rent. Low income people whose credit exceeded their tax liability would receive a small payment from the Internal Revenue Service.

This is an extremely simple proposal. It entails no housing market regulation. It entails no intrusion by officials in private affairs other than that which is inherent in an income tax system. It would be mainly self-administering, with the taxpayer doing most of the work. Low income people could continue to file their income tax return on a postcard as they do now. People whose credit exceeded their tax liability could receive quarterly payments, using the quarterly tax declaration scheme now in existence. There would be no selective eligibility and therefore no temptation to favoritism or corruption. The only government activity required would be tax return auditing, which would require only modest increases in present personnel. The subsidy would be a uniform percentage of housing costs and would thus avoid the undesirable characteristics of present programs that provide large subsidies to a few needy people and none to the rest.

Finally, and perhaps most important, it would remove what is probably the most serious inequity of our present tax laws, the housing subsidy they provide to middle and upper income taxpayers, but deny to low income people. If one does not believe the housing distortions discussed above are important, then either the existing subsidy to homeowners should be removed or it should be extended to renters. By all accounts, removal of the homeowner subsidy is politically impossible. Then simple equity demands that a similar provision be made available to renters.

The tax credit plan would be an efficient subsidy because it would do precisely what should be done to correct housing distortions from real estate taxes and from the external economy—namely, increase housing demand. Renters would demand more and higher quality housing than at present. A tax credit set at the right level would just offset the excessively low housing demand resulting from real estate taxes and the external economy. I believe there is little doubt that the market would respond by a nearly equal increase in the supply of rental housing. (That is, I claim that the supply of rental housing to low income families is quite elastic.) People who doubt this usually refer to the slowness and uncertainty of the filter-down process. In fact, there is little reason to believe that filtering would not accelerate in response to increased housing demand by low income households. But that is not the issue. The speed of filtering mainly affects the number of dwellings available at rents that can be afforded by poor people. The biggest single housing problem of the poor is that they cannot afford rents that can finance enough maintenance to keep dwellings in good condition. That is the source of the warfare between landlords and building code enforcement in large cities. The conclusion is that important improvements in low income housing can come about from improved maintenance, and nobody doubts that resources are available to maintain housing if money can be found to employ them. That is, the supply of maintenance services for low income housing is elastic, and maintenance costs would not rise unduly in response to increased demand.

My tax credit plan would, of course, require renters to fill out a tax return to be eligible for the subsidy. A few low income people do not now file returns. In fact, completing tax returns is not a great burden for low income citizens because the form is quite simple. Some may not now keep records of rent they pay, and they would have to do so. It would be important that the tax credit plan be well-publicized, so poor people would know of its existence. But those for whom it was worthwhile would quickly take advantage of it.

How much would the tax credit plan cost the government in reduced income tax revenue and the small payments it would entail? It was argued above that the existing deduction for owner-occupiers reduces their tax liability by about 15 percent from their living costs. I therefore assume a rent credit equal to 15 percent of annual rent. The following table shows the effect of the credit on tax revenues. The data are for 1969 and are from the 1970 Census of Housing (Housing Characteristics by Household Composition, Table A–2):

Annual Income	Median Monthly Rent	No. of People (millions)	Cost of 15% Credit (millions/yr.)
$ 0–4,000	84	7.1	$1,070
4,000–7,000	102	5.1	917
7,000–10,000	115	4.4	911
10,000–15,000	133	3.8	915
15,000	165	1.9	565
			$4,378

Thus, the total cost of the credit would have been $4.4 billion in 1969. It would be somewhat greater in 1973. Although I do not have current figures at hand, I believe that $4.4 billion is similar to the recent cost of housing programs the President wishes to phase out, at least if the cost of accelerated depreciation is added to them. It would therefore have little overall effect on the federal deficit. In contrast to tax savings from the current deduction provision—practically all of which goes to high income families—most of the rent credit would go to low income families. The table shows that two-thirds of the credit would go to households with incomes below the 1969 median of roughly $10,000. Rent per family falls rather gradually as income rises. Most of the progressivity of the rent credit results from the concentration of renters among low income families. Although 60 percent of families are owner-occupiers, the percentage is only 40 for families with incomes below $3,000, and rises gradually to over 95 for families with incomes above $100,000.

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Policies of Housing Support: Rationale and Instruments

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Summary

The paper focuses on the rationale for government support of housing and its implementation. To establish such a rationale, "merit good considerations" must be introduced according to which housing is considered a form of consumption which society views more important than allowed for by individual consumer choices. This social evaluation may be directed either at homeownership or at the provision of minimum housing levels, i.e., avoidance of "housing poverty." As the bulk of housing support now goes to middle and upper income housing via income tax preferences, the program should be redirected to emphasize low income housing. This should include rent support to the occupier conditional on own-expenditures being maintained at a set fraction of income. Such supports need to be supplemented by measures aimed at increasing the supply of low cost housing as well as improved public housing to deal with situations of particular housing distress.

Aspects of Housing Policy

Public concern with housing is not peculiar to the United States. It is a more or less universal phenomenon, with public involvement in housing in most European countries exceeding that to be found here. The widespread role of public policy in the housing sector suggests that there must be reasons why housing—as against, say, the provision of clothing or food—should be a matter of public concern. The purpose of this paper is to identify and evaluate these reasons and to explore their implications for the choice of public instruments.

Historically, the origin of current housing programs may be traced to the Great Depression of the 1930's, when public measures were needed to deal with bankruptcy in the mortgage market and when housing construction presented a ready and desirable channel of employment creation. In subsequent years housing continued to pose problems of credit market and stabilization policy, but the focus shifted towards social concern with the adequacy of prevailing levels of housing consumption. This included (1) concern with homeownership as a particularly "meritorious" form of consumption or investment, and (2) concern with inadequate housing conditions at the lower end of the income scale. In the latter connection, housing policy came to be viewed as a central part of the "urban problem" and the broader social and economic issues associated therewith. It is evident, therefore, that one should not look for a simple and single rationale for public involvement in the housing sector. Among the major concerns, we distinguish between:

1. Considerations relating to the support of housing as a socially desirable form of consumption, be it in terms of homeownership in particular or housing consumption in general, unlimited or with regard to provision of minimum levels of housing services at the lower end of the income scale.

2. Problems of imperfection in the housing market, arising from such factors as the fixed supply of land in urban settings, zoning and discrimination which reduces tenant mobility, linkages between location and job availability, lumpiness of housing outlays, credit risks, and so forth.

3. Aspects of stabilization policy, including cyclical fluctuations in the level of construction activity and repercussions of stabilization policies (especially monetary measures) upon the mortgage market.

Among these various concerns, this paper will be directed primarily at 1, considering both the rationale under which such objectives may be pursued and the way in which they may be implemented. Our emphasis is thus on the case for and implementation of housing subsidies, as distinct from primarily regulatory and stabilization aspects.

Should Housing be Subsidized?

Concern with the adequacy of housing, viewed as a matter of social philosophy, seems to be at the center of the current debate over the future of housing policy. The critical question is whether in the absence of public support the level of housing would be inadequate. If so, some form of public support is called for. The next question is how much support should be given, where, and why. For any given degree of support, there remains the question of how it should be provided, e.g., through low rent public housing, or through support to private housing, such as mortgage, rent, or tax subsidies. These matters of implementation are left aside for the time being, our initial question being why such support should be needed. This is the basic issue which must be decided upon before the technicalities of implementation can be considered.

The Social Goods Rationale

There are certain types of goods (referred to variously as social, public, or collective goods) which cannot be left to provision by the market. These are goods the consumption of which is nonrival—i.e., A's consumption does not reduce the benefit which B derives from a particular service. As such, they differ from private goods which are such that consumption by A excludes consumption by B. In the case of social goods, where consumption is nonrival, it would be inefficient to exclude users by making participation in the benefits subject to payment. Since the marginal cost of admitting an additional user is zero, no charge should be made; but if no charge is made, provision through the market mechanism becomes impossible. The good must be paid for by government and financed through the budget. Moreover, the nature of nonrival goods is frequently such as to make it impossible or excessively expensive to exclude users unless they pay. Thus, the use of the market mechanism is not only undesirable, but would in fact not be feasible.[1] While the social good must be paid for through the budget, it need not be produced publicly. It is perfectly possible for government to purchase the output of private firms and to provide it free of direct charge to its users.

Housing, it would seem, does not meet either of these conditions. A dwelling that provides living space for family A cannot also be used by family B. The "a man's house is his castle" view makes housing almost the prototype of a private good. Consumption, it appears, is strictly rival. Moreover, the nature of the product is such that exclusion can be readily applied, i.e., use can be made contingent on purchase or payments. In both respects, "housing" is a private good; and this being the case, the presumption is that provision thereof can be left to the market, just as can be done for food, amusements, or clothing. The standard social good reasoning, it appears, provides no basis for public provision.

The Externality Rationale

This conclusion needs to be qualified if we allow for the fact that most goods are not readily classified into the polar categories of "social" and "private." In few instances can it be said that benefits are totally nonrival or totally private. Thus, even measures of national defense (usually considered the most clearcut illustration of a social good) may be more helpful to residents of the east or the west coast, or to urban or rural areas; and even A's consumption of food (considered to be the epitome of a private good) may affect B as he comes to deal with a more or less healthy neighbor. All categories in economics—such as the definition of a product, and the distinction between consumption and investment, like that between private and social goods—fade into each other and no absolute lines can be drawn.

External Benefits and Costs: Many goods are "mixed goods," where A's own provision and consumption may be of primary benefit to himself, yet generates additional or "external" benefits that accrue to B and C. In such cases, provision through the market mechanism will not fail in the sense of total nonprovision; but it will fail partially in the sense that the good in question will tend to be undersupplied. Such is the case because A will value his consumption only in terms of his own benefits, while overlooking the external benefits derived by B. Where the numbers involved are small, this benefit-spillover may be adjusted for by the market. B may find it in his interest to compensate A, so that all benefits are allowed for. But given large numbers, B will act as a "free rider," leaving it to others to pay compensation. Because others feel the same way, no compensation is paid and under-provision will result. As a consequence, partial provision through the budget—i.e., a subsidy—is called for to secure efficient allocation.

Similar considerations apply where A's consumption (or, for that matter, production) activity gives rise to external damages or costs which

[1] Indeed, situations may arise where exclusion is not readily feasible even though consumption is essentially rival, so that the market mechanism would be efficient if exclusion could be applied.

are suffered by B and C. Consumption of such goods is higher than would be the case if all costs were internalized and had to be paid for by the consumer. In the large number of cases, this now calls for a selective tax (the opposite of the subsidy needed to internalize external benefits) to provide the necessary correction and to secure an efficient consumption pattern.

The fact that housing is a (or perhaps *the*) major area of public subsidy suggests that housing consumption may generate significant external benefit, thus calling for at least partial provision or subsidy. Thus, poor housing is said to give rise to social alienation, crime, disease, and a poor educational environment for children. Housing improvement in turn is expected to generate external benefit by reducing these costs. Saving may take the form of reduced remedial costs—e.g., fire protection or clinics—or it may accrue in the form of improved social environment—e.g., a lesser probability of being caught in a fire or being exposed to infection. On grounds such as these a subsidy policy to provide minimum housing might be justified. However, similar arguments can also be applied to other forms of consumption, and it is not at all obvious that housing improvement generates more external benefits per dollar than does, say, improved food consumption; yet such a conclusion is needed if housing subsidies in particular (as against a general form of low income subsidies) are to be justified on externality grounds.

Joint Product Aspects: Next, some externality-related considerations involving housing as a "joint product" may be noted. The availability of housing determines the immediate location and neighborhood in which people spend most of their time, so that, to the individual consumer, housing and neighborhood constitute a "joint product." Since some components of the joint product (e.g. government services available in the particular environment) are in the nature of social goods, housing itself assumes social-good qualities that do not apply to the living space as such. To the individual, the cost of the housing and social-good package includes a private price component (housing cost) as well as a public or tax component. This consideration, however, points to public policy concern with the structure of the housing market (i.e., who is to have access to which community) and control thereof, rather than to the proposition that the absolute level of housing services is too low and need be supported.

Another aspect of the "joint product" nature of housing arises from the need to service housing with public utilities such as water, sewers, power, roads, etc. The structure of housing (with regard to location, type of occupancy, etc.) thus has important bearing on the cost at which these services can be supplied. This points to the need for city planning as isolated individual housing choices may give rise to external economies and diseconomies for other residents. Group decisions are needed to secure efficient arrangements. Considerations such as these once more point to a role for public policy in the housing market, be it through zoning, transportation or planning, or other devices; but once more the problem seems to be one of regulation rather than of general housing support.

Spatial Concentration of Poverty: Because the availability of low cost housing tends to be concentrated in particular locations, the inability of low income families to pay more results in locational concentration of the poor. Housing differs in this respect from other goods, such as food, because families in the same location may readily differ in their level of food outlays. Spatial concentration of low income families in turn limits job availability and generates an environment which makes it more difficult to escape from poverty. In a perfect housing market, this aspect of low cost housing would not arise because such housing would become available where needed, but in fact this is not the case. Given the existence of ghettos and widespread housing discrimination, combined with the importance of housing not just as a matter of consumption but of job opportunity, the structure of housing markets is evidently a matter of public concern. It is also evident that spatial shifting in low income housing may require selective subsidies (as distinct from zoning measures), but even then the primary objective is to shift the location rather than to secure an increase in overall housing supply.

Conspicuous Misery: Poor housing makes poverty visible and is thus more discomforting to the nonpoor than are other deficiencies in the living standard of the poor. As noted below, this may be a reason why society is more willing to deal with poor housing than to face the broader problem of redistribution. On the other hand, similar considerations explain less constructive "solutions." Measures such as exclusive zoning may be used to relegate low income housing to the slums, thereby segregating the poor so that they need not be seen. The issue in this case is once more one of controlling the structure of the housing market, rather than of increasing the overall housing supply.

As the preceding discussion shows, housing generates numerous externalities which in turn offer various reasons why housing should be a concern of public policy. But the argument in most cases appears to point to a need for structural controls over the housing market rather than to a general case of housing subsidies. While public provision of, or subsidies to, housing may be in order to deal with particular structural problems (i.e., to introduce low income housing into suburbs or to redirect inner city housing into more suitable structures), these objectives do not address themselves to a general support of the level of housing services such as visualized in the housing acts of 1949 and 1969.

Table 1. Summary of Major Housing Programs, 1970 (Gross budgetary costs in billion dollars)

Thrust of Benefits by Income Groups [1]	Tax Prefer-ences [7]	Other 1970	Public Housing 1970	Total
Renter Subsidies				
Upper	—	—	—	—
Middle-high	—	—	—	—
Middle-low	.1	.9[4]	—	1.0
Poor	.2[2]	—	1.3[6]	1.5
Total	.3	.9	1.3	2.5
Owner Subsidies				
Upper	3.8	—	—	3.8
Middle-high	4.3	—	—	4.3
Middle-low	1.2	.5[5]	—	1.7
Poor	.2	—	—	0.2
Total	9.5[3]	.5	—	10.0
Renter and Owner				
Upper	3.8	—	—	3.8
Middle-high	4.3	—	—	4.3
Middle-low	1.3	1.4	—	2.7
Poor	4	—	1.3	1.7
Total	9.8	1.4	1.3	12.5

Source: Committee for Economic Development, *Financing the Nation's Housing Needs*, April 1973.

1 "Upper" equals households with incomes above $20,000; middle-high equals households with income between $10,000 and $20,000; middle-low equals households with between $5,000 and $10,000, and low equals households below $5,000.

2 Accelerated depreciation on rental housing.

3 Includes gains from deduction of mortgage interest and property tax and from non-inclusion of net imputed rent. For further discussions see text, footnote 3.

4 Title 235.

5 Of this .4 is accounted for by Title 236 and .1 by rural housing.

6 Includes rent supplements.

7 For further discussion see Appendix A.

The Merit Good Rationale

The efficiency concept of economic analysis usually rests on the premise that resources should be used so as to satisfy the preference of the individual consumer. This holds with regard to the efficient functioning of the market in providing for private goods, as well as for our preceding discussion of social goods and externalities. Social goods and externalities are troublesome and call for special attention (through the political process) because they involve market failures, but this attention does not imply an inherent departure from the principle of individual choice.

The question now arises whether public concern with housing is not in fact based on a different hypothesis—i.e., the notion that society looks upon expenditures on housing as particularly "meritorious" and more valuable than free consumer choice would suggest, and hence deserving of public subsidies. This "merit good" rationale may be related to total housing expenditures or to the provision for minimum housing only; moreover, it may apply to housing consumption in general or to ownership in particular.

The Virtue of Homeownership: As shown in Table 1, by far the largest part of housing subsidies (implicit or explicit) is given in the form of income tax preference for homeownership. Such subsidies, which account for about 80 percent of the total, relate to owner-occupiers as distinct from rental payments, and the benefits thereof accrue largely to the middle income groups. These subsidies, given through tax savings due to exclusion of net imputed rent from taxable income (or exclusion of gross imputed rent while allowing deduction of mortgage interest) now totals about $6 billion, with tax savings from property tax deductions adding another $3.5 billion.

Inclusion of these tax savings as subsidies is based on the proposition that such items should in fact be included in the tax base, a proposition which is detailed further in the Appendix. Here it need only be noted that there is no difference in principle between an explicit subsidy paid through an expenditure program and an implicit subsidy paid in the form of tax relief. While the massive support to homeownership due to tax relief has grown as a byproduct of increased use of income taxation, rather than as a direct subsidy, this does not render it less real; and as tax reformers who have tried to deal with this particular loophole well know, such endeavor meets with overwhelming opposition. This opposition transcends the efforts of the real estate lobby and the natural desire of middle income taxpayers to fight off an increase in their tax bills. It derives strength from a social attitude that attributes merit-good qualities to homeownership and renders such ownership sacrosanct with regard to the income tax.[2]

Homeownership may be considered meritorious because it serves as a symbol of a man's independence and the privacy of his family life; and because it increases the owner's stake in the *local* community in which the property is located and, more generally, as a means of integration into a social order in which private ownership of property is a critical component. The latter argument might point to similar support for all forms of ownership, but homeownership is of particular importance because it is the primary form of wealth within the middle income range.

This is the case because housing property serves the dual purpose of consumption and investment, and because mortgage financing provides a leverage which is otherwise not readily available to small investors, a leverage which is of particular importance under conditions of inflation. For these reasons, the ratio of home value to net worth is relatively high over the lower and middle income ranges, and subsidizing homeownership serves the double purpose of supporting small wealth holders and broadening the bases of property ownership at large.

While this reasoning is not presented to justify the prevailing tax preferences, it is offered to explain the merit-good type attitudes which support them. The problem, however, is not merely whether such values are appropriate, i.e., whether homeownership should be given special support. Since these attitudes exist, the more pertinent question is whether, given the objective of ownership support, the present form of tax preference is an efficient way of accomplishing it. The answer is clearly in the negative. By adjusting the present system through transforming the deduction of mortgage interest into a tax credit and setting a ceiling for the amount of interest thus creditable, the cost of the subsidy could be greatly reduced without significantly weakening (or even while strengthening) the resulting ownership inducement.[3]

The Evil of Housing Poverty: We now turn to a second version of the merit-good rationale which relates to housing consumption generally (including both rental housing and ownership) but is limited to the provision of minimum housing levels. This is the proposition that every American family should be assured a decent home and a suitable living environment. Adopted first in the Housing Act of 1949 and reaffirmed in the Housing and Urban Development Act of 1969, this approach singles out the elimination of poverty in housing as a particularly important target of antipoverty policy. The question is why, within the broader objective of eliminating poverty at large, such a priority should be established.

We begin with the standard economic argument that selective support is inefficient. If there is to be redistribution in favor of the poor, this will be done best by way of a general income support. Suppose that high income household H is to be taxed X dollars to improve the position of low income household L. From L's point of view an untied cash transfer of X dollars would be the best solution and preferable to being granted X dollars worth of free housing services or—which would be the same for present purposes—a cash grant of X dollars which must be spent on housing. The reason for L's preference is obvious: The cash grant will permit him to place himself in the same position as the in-kind grant, but it leaves other options. Only if his preferences are such that he would have wanted to spend the entire cash receipt on housing would L be indifferent between the two policies. This being an unlikely case, L would prefer the cash and obtain a larger welfare gain by using part of the proceeds for expenditures on items other than housing. This being the case, selective support of housing in particular cannot be justified. Such redistribution as occurs should be implemented via a general income grant.

Before rejecting the selective approach out of hand, let us see what alternative rationale may be developed in its support. Society may hold a view of distributive justice that calls for each family to enjoy no less than a minimum level of consumption with regard to "basic needs." In defining "basic needs," food, clothing, and shelter are obvious candidates for inclusion, while trips to Europe, second cars, or sum-

[2] Current demands for property tax reduction appeal to the same set of values even though the property tax is at least partly a benefit tax and even though the tax burden on home ownership as an investment is less than on investment in corporate equity.

[3] By moving the effective support down the income scale, the ownership inducement could be strengthened further through a curtailment of the standard deduction, combined with a corresponding reduction in low bracket rates.

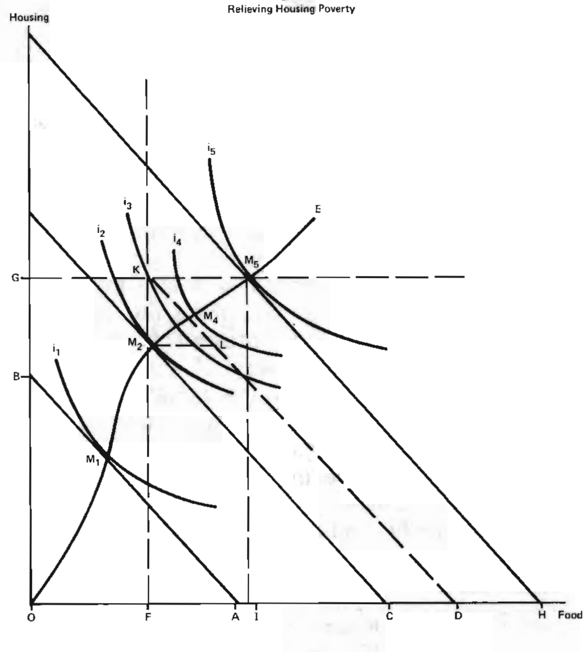
mer homes are not. Within each category a basic standard must be set and the cost of meeting it may be determined on more or less objective grounds. Drawing on nutritional requirements for food, on floor space and plumbing requirements for shelter, and on climatic conditions for clothing needs, the cost of minimum requirements in the various categories may be priced.

To be sure, this is not an entirely "objective" process. Social judgment as well as biological and physiological considerations enter into setting levels for consumption; and what is considered acceptable bears some relation to, and changes with, the level of average income and living standards. Yet this approach differs in spirit from the preceding view of the matter, by which the poverty floor is conceived in terms of a minimum income level which is set independent of (or perhaps in relation to average) income use. In the one case society holds (a) that a given set of "necessary" consumption items should be made available to all households; in the other case it holds that (b) all households should have a "minimum level of income" at their disposal. This income level in turn may be defined as a fraction (say, one-half) of mean income, or it may be set in relation to the consumption bundle purchased by the "average" family at such an income level. Whatever criteria are used in defining (b), its view of setting a poverty floor differs from the (a) approach.

Following up the latter, we may now compare the minimum bundle of "necessities" with the bundle of goods typically purchased at various income levels. It may then turn out that, in the absence of interference, minimum food and clothing standards come to be satisfied by household purchases at a lower level of income than is needed to meet the minimum housing standard. In this sense, a family of four with an income of $4,000 may be considered as food- and clothing-adequate, but as housing-poor. An income in excess of, say, $4,800 may be needed to overcome housing poverty thus defined, even though the household would be above the poverty line of other items. In this case, the poverty problem is essentially one of relieving housing poverty, and this can be done at lesser cost if selective support is given to housing in particular than if incomes have to be raised to a level at which the stipulated minimum housing consumption occurs.[4] This would seem to be the rationale underlying the concept of "housing poverty" as used in a recent paper by the Committee for Economic Development.[5]

The argument is illustrated further in Figure 1. Assuming consumer expenditures to be divided between housing and food, the budget line AB shows the combination of food and housing available to a household with income OA as measured in terms of food. The household in absence of government intervention chooses housing-food mix M_1. At income OC, mix M_2 is chosen while income OD leads to a choice of M_4, and so forth. Line OE thus indicates the locus of successive mixes of food and housing as income increases. Now suppose that the minimum level of food consumption is set at OF while that of housing is set at OG. A household with income OA and located at M_1 is in poverty with regard to both

Figure 1
Relieving Housing Poverty



[4] It is pertinent to note in this context that the concept of minimum income as developed by the Department of Agriculture appears to be determined independently of the costs of "minimum housing needs" as developed by the Bureau of Labor Statistics.

[5] See *Financing the Nation's Housing Needs*, Committee for Economic Development, New York, 1973, p. 9.

food and housing. A household with income OC and located at M_2 is adequate in food but remains in poverty with regard to housing. This remains the case for a household with income OD and located at M_4, adequate consumption for both budget components being reached only at income OH and location at M_5.

Consider now what can be done to move the household located at M_2 out of housing poverty. One approach would be to give an income subsidy (measured in terms of food) equal to CH, in which case the aided household would voluntarily choose position M_5. Here the minimum level of household consumption would be reached while food consumption would exceed the minimum by FI. Alternatively, the government might take steps to move the household from M_2 to K, i.e., to give a tied subsidy which would be reflected totally in increased consumption of housing. Assuming that this could be done, the cost to the government would be much less.[6] The cost (in terms of food) would now be M_2L = CD only. As compared to the general income subsidy, the cost savings would be DH. Therefore, if the objective is to eliminate "housing poverty" in particular, the efficient approach is to give a tied housing grant rather than a general income grant.

The usual objection to this reasoning was that the household will prefer a general income subsidy of CD only to housing services costing CD. The latter will permit the household to divide the gain between housing and other purchases, placing itself at M_4, which lies at a higher indifference curve than does K. Once this view is taken, it becomes in fact pointless to set the size of the subsidy as CD, i.e., the amount that would be needed to remove housing poverty in particular. If free consumer choice is to be adhered to, the proper policy is to make an income grant while leaving its use to the recipient. It makes no sense in this case to speak of a household as being "housing poor" while showing adequate consumption standards in other items.

The rationale of setting the subsidy cost equal to CD and to place the household at K (both of which go together) is thus based on the proposition that households should not fall below set minimum consumption levels of food and housing rather than falling below a set overall level of income. The concept of "housing poverty" thereby implies interference on the part of society with consumer choice. More specifically, it involves an interference which is linked to consumption floors and is thus operational over low income ranges only.[7]

The issue, it appears is between two philosophies of viewing the problem of poverty floor, with U.S. policy experience over the last four decades reflecting both approaches. The welfare program itself has been a mixture of general income support and selective aid, while the outright negative income tax or income maintenance approach is of more recent vintage. Although the latter has captured professional attention and support, the public is far from willing to undertake the massive transfers that would be required to meet adequate standards. Provision for specific consumption floors in housing has retained strong support as evidenced by the 1968 legislation. Nor are recent suggestions for substitution of rent subsidies for public housing in conflict with this approach. As shown below, rent subsidies, like public housing, are members of the selective-support family. They both differ from general income subsidies in that they are earmarked for housing use.[8]

While public support for the selective approach may be discounted to some degree as reflecting the special interests of the housing lobby, it would be a mistake to consider this the entire story. A view of distributive justice as setting poverty floors in terms of meeting "essential needs" is part of our country's social mores and not just a reflection of special pressures or failure to grasp the underlying economics. This being the case, one must take a somewhat skeptical view regarding the conclusion reached by standard economic reasoning that housing support is inefficient because the welfare gain,

[6] To avoid leakages into other expenditures, it would be necessary not only to earmark the subsidy for housing use, but also to require the household not to reduce its own-financed outlays on housing.

[7] It might be argued that if society is concerned with minimum intakes of particular consumption items, the required level of consumption should apply also to occasional households at higher income levels which choose to distribute their expenditures in a "perverse" fashion. Given relatively low income standards, this situation is likely to arise in rare instances only. Moreover, if the income floor under the minimum income approach is set sufficiently high, the mix of outlays under free choice comes to exceed the minimum consumption level for essential items, and the minimum level's approach becomes redundant. But if the general income floor is set at a level which is inadequate—which certainly will remain the case for income maintenance in the forseeable future—deficiencies on various outlays remain and the two views lead to different policies.

[8] At the same time, public housing is more selective than rental supports in that it interferes further in the type of housing choice. Opponents of selective support are therefore consistent in preferring rent support as the lesser evil. See R. F. Muth, *Public Housing,* American Enterprise Institute for Public Policy Research, Washington, 1973, p. 43.

as valued by the receiving household, would have been larger with a cash grant.[9] Such is the case only if the policy objective is taken to be general income support without interference in income use. If, on the other hand, the objective is precisely to increase housing consumption, then the selective approach is more efficient because it accomplishes the objective at lesser cost. Putting it more generally, the conclusion that selective subsidies or selective taxes are inefficient is applicable only where there is no explicit intent on the part of public policy to reduce or encourage particular types of consumption.

Conditional Giving

In the preceding section we have considered the reduction of "housing poverty" as reflecting a view of distributive justice that is not inherently unreasonable and seems to reflect the value judgement on which much of our housing subsidies have been based. An alternative or more pragmatic explanation views the matter in terms of voluntary giving and the political process of redistribution.

As has been argued in recent years, the concept of optimal distribution may, to some degree, be viewed in terms of the traditional efficiency economics. Beginning with a given state of distribution, individuals at the high and upper income scale may derive satisfaction (whether from "doing good," avoiding "feelings of guilt," or as a matter of general altruism) by using their income to render subsidies to households at the lower end of the income scale. In other words, household's utility function not only includes the satisfaction derived from own-consumption, but the satisfaction derived from consumption by others or from giving to them. Such giving in turn may be outright and without strings attached or it may be conditional on certain uses by the recipient. Thus, a high income household may derive more satisfaction from the use of its gifts for housing than for other purposes. As a result, the high income household may be willing to make conditional but not general grants.

The same problem may be viewed in the political context, where redistributive measures have to be voted upon. Suppose that a majority for redistributional measures can be found if the "donors" who pay for the cost of such programs are permitted to impose their own preferences on the donees who benefit. Thus, there may be a majority (among donors and donees) for the expenditure of $1 billion for a program to increase low income housing consumption, whereas there is a majority for a transfer program of only $500 million in the absence of earmarking. Such being the case, the donees may well opt for the tied but larger program as the best available solution, even though they would prefer an untied transfer of $1 billion if such were available. The tied transaction then becomes efficient in the sense that it leaves all parties concerned (including donors and donees) better off than they would have been if the transfer of earmarked funds were ruled out and only general transfers were permitted. The rationale for selective grants, aimed at the elimination of "housing poverty" may thus be viewed in these terms.

What then is to be made of the argument that tied transfers are "ethically repugnant" because they restrict the recipient's freedom to use his funds as he wishes? The answer to this question is one thing if tied support is compared with equal expenditures on free support. But it is another if larger tied support is compared with less free support. In this case, the ethical objection to loss of freedom in the use of nonexisting income becomes rather dubious. If interference is repugnant, so is the toleration of poverty in a wealthy society. Ethical concern about interference with choice in the absence of prior concern for setting a poverty floor is of questionable sincerity. While the economist who eschews ethical judgements in matters of distribution may voice efficiency concerns about tied grants, he is hardly eligible to voice ethical concerns in the matter.[10] Such is the case especially if social mores tend to approach the avoidence of poverty in terms of minimum levels, so that the poor (even if valued in terms of their own prefer-

[9] This type of inefficiency thus differs from inefficiencies which result because housing subsidies are given in ways which cause structure to be excessively capital-intensive so as to minimize maintenance. Whereas the latter is an obvious element of inefficiency which can readily be avoided by redesigning the grant terms, the former involves a judgment that distributional adjustments should be ruled out and that the entire approach in terms of minimum consumption levels (and its implicit merit good judgment) should be held inadmissible.

[10] See R. F. Muth, op. cit., Chapter 2.

ences) are likely to be benefited by such a strategy.[11]

The Lumpiness Rationale

Two further considerations that come to mind when exploring the rationale for housing support relate to the "lumpiness" of housing expenditures. This includes the nature of housing as demanding a large share of low income budgets, as well as the potential indivisibility of house purchases.

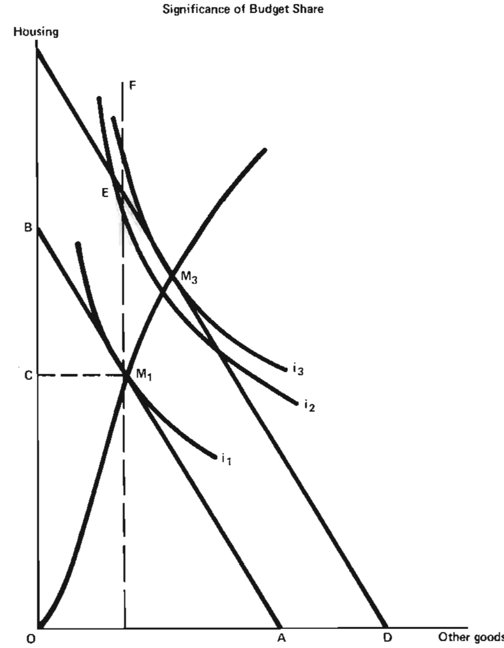
The "Large Share" Feature: Housing is the largest single item in low income budgets, absorbing, say, one-third of the total. This in itself may suggest that housing is of particular importance and therefore deserving of special support. In the absence of merit-type considerations, this is not a valid conclusion.

In Figure 2 we show a situation where a low income household with income OA (as measured in terms of other goods) and the prevailing price ratio OB/OA places itself at M_1 and chooses to spend a large share OC/OB of its income on housing. Line OM_3, showing the budget mix at various levels of income, is also drawn so that the housing share continues to be large as income rises above OA. An income subsidy equal to AD would move the household to M_3 while additional housing consumption of equal cost would place it at E, which is an inferior position.

What matters in comparing the welfare effects of a general income grant with an equal cost increase in housing is not how the budget was divided initially, but on what the response to an increase in income will be. If the household desires to spend the entire increase on housing —i.e., if the price-budget line is vertical, as shown by MF—the two approaches will lead to the same result, but short of this the general income subsidy remains superior. The fact that housing is initially a large share has no bearing on the argument. The share would be significant only if we were to compare a matching grant on housing expenditures with an equal rate matching grant on a smaller item, but in this case the comparison would be misleading as it did not involve equal cost.

The Indivisibility Feature: Another aspect of the problem relates to the "lumpiness" of expenditures on homeownership. This lumpiness arises in the absence of perfect capital markets because a substantial downpayment is required.[12] Because of this requirement, households may be unable to purchase homes even though they would do so otherwise. An income grant raises the household's ability to make the downpayment, but leakages into other uses result. A selective grant earmarked for housing use and contingent on house purchases, on the other hand, goes directly to reduce the net downpayment which the purchaser must make out of his own resources. Note that this problem is peculiar to ownership and does not arise with regard to rental housing, where no downpayment is needed.

Figure 2
Significance of Budget Share



[11] To clarify the point further, we distinguish between the normative and political aspects of the problem. The first question is whether one would prefer to see the poverty floor defined in terms of (a) income maintenance or (b) minimum consumption levels for essential items. Evidently, many voters take the (b) position and would opt for this approach as a first best solution. The second question is whether those who prefer (a) are willing to resort to (b) if (a) is unavailable or to an inadequate degree only. In this case, (b) is supported as a second best solution only. Selective supports such as housing programs, may thus draw on two groups of supporters, those who choose it as a "first best" approach and those who accept it only as a "second best" alternative.

[12] In the absence of a down payment requirement, the ownership case is similar to that of the rental case.

The lumpiness argument may thus make a case for selective support, but it would seem that better remedies for dealing with the problem can be found. In fact, mortgage guarantee policies permitting a longer amortization period and for a larger ratio of loan-to-value are designed precisely to deal with this problem.

Incentive Aspects

One of the major difficulties with income maintenance and welfare programs is that effective support for low incomes within a national budget constraint inevitably involves the need for letting the support decline as earnings rise. The loss of support thus reduces the take-home value of earnings, just as would the application of a high marginal rate of tax. As a result, the terms at which leisure can be traded for income are worsened, and the incentive to work is reduced.

The question is whether housing in lieu of general income support might reduce the magnitude of the disincentive problem. Various considerations are involved, and the outcome seems to be inconclusive. Just as the negative income tax may be viewed as a sum of (1) a lump-sum basic income grant, and (2) a progressive tax upon earnings, so may low income housing be viewed as the sum of (1) a lump-sum type of basic housing provision, plus (2) an excise tax on housing, the rate of which rises with earnings. With regard to (1), the lump-sum income grant will lead to an increased purchase of both goods and leisure, i.e., some reduction in work effort. The lump-sum housing provision will tend to do the same. However, if housing is complementary to leisure (or more so than are other outlays), the incentive to enjoy more leisure and to work less may be greater under the housing than under the income grant.[13] By the same token, the labor-adverse substitution effect of the marginal tax rate will be dampened if the tax is an excise on housing rather than an income tax on earnings, leaving it open whether the net detrimental effects on work effort will be more or less severe than under the negative income tax approach.

However this may be, a different line of reasoning points in favor of the housing approach. It does not seem unreasonable to expect that increased housing consumption by low income households will tend to raise expectation levels and—by associative factors such as the "Jones Effect"—lead to increased effort, in order to supplement increased housing with other forms of increased consumption, e.g., furniture. Quite possibly, this effect will be stronger with housing than with general income support, where the increase in consumption is dissipated over a variety of less "status creating" goods.

Finally, it may be noted that the entire efficiency argument as developed previously in connection with Figure 1 was based on the assumption (among others) that choice is limited to that between housing and other consumption. If a further choice between consumption and leisure is allowed for, a priori judgments regarding the efficiency ranking of general income support as against selective housing supports become more difficult.

Strategies and Instruments for the Support of Low Income Housing

Only a small part of the total cost of housing support is now directed at low income housing. As shown in Table 1, this share is below 20 percent if income tax preferences are fully included and below 50 percent if they are excluded. Nevertheless, the discussion in the first section suggests that a much better case can be made for housing support at the lower end of the income scale than over the middle and upper ranges. Moreover, much of the current discussion is directed at improving this part of the program. The present section, therefore, addresses itself to the critical problem of how support to low income housing can best be provided.

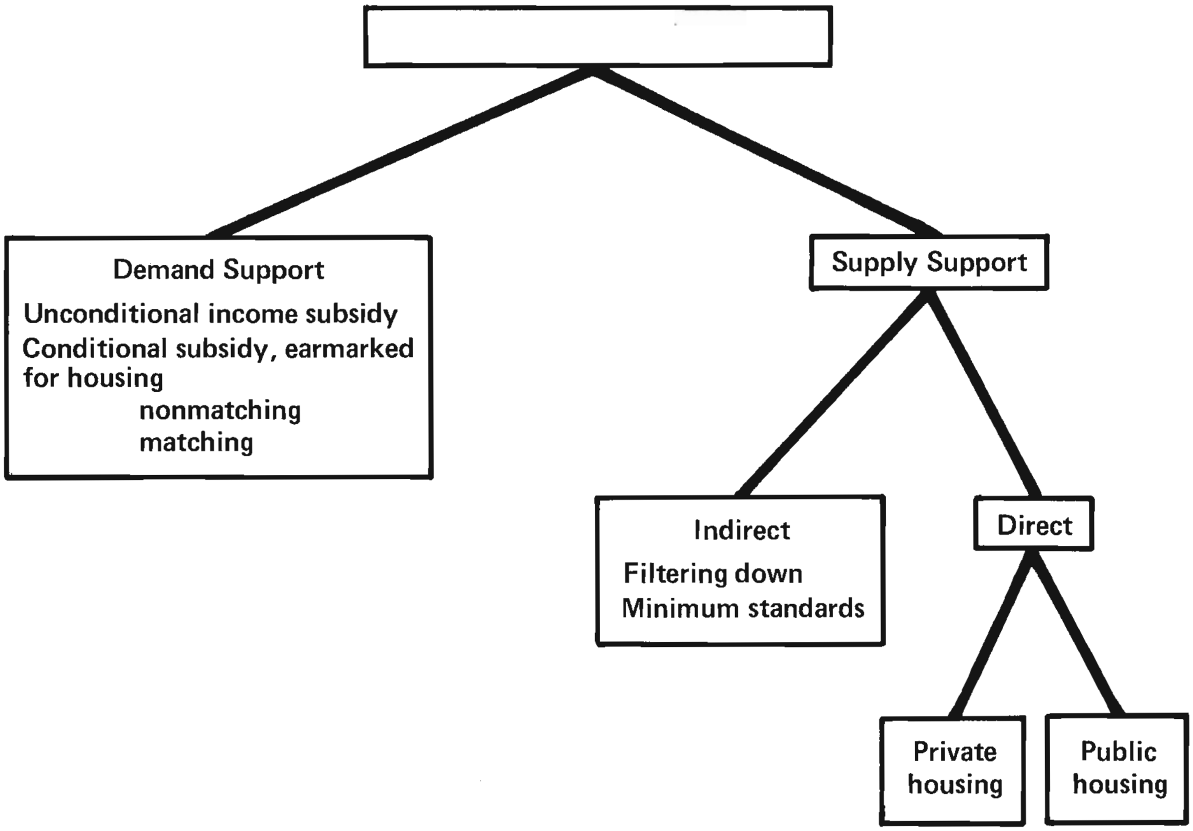
The various forms in which such support can be given may be broken down as shown on page 225.

Types of Demand Support

We begin with various types of demand supports, i.e., supports given to the owner or tenants directly.

General Income Maintenance: General income maintenance is a highly ineffective approach to our objective, since the larger part of the payment will be diverted into other ex-

[13] We assume that the grant is made conditional on the retention of own-expenditures at the pregrant level.



penditures. To close a poverty gap in housing of, say, $4 billion, it might be necessary to raise the income of low income families by, say, $15 billion. To make these transfers without imposing an exorbitant implicit tax rate, net payments to families well above the poverty line are needed, calling for a total transfer of, say, $50 billion, or over 10 times the housing gap.

Earmarked Grants: The efficiency of earmarked transfers may or may not be superior to general income payments. If the earmarked grant G to household X with income Y falls short of X's voluntary housing expenditures V at income Y + G, no purpose is served by earmarking. Household X can simply substitute the earmarked grant for prior own-outlays and spend the latter on other items. The result, therefore, is the same as under a general income grant. Only if G exceeds V will housing expenditures be increased by more than under a nonearmarked grant, and even then a substantial spillover into other outlays will remain. Since the level of grants under foreseeable programs will hardly be so large as to exceed the voluntary expenditure level V, earmarking is, in fact, redundant, and a program of general income support should be applied in the first place. But such a program is obviously inefficient for policy which (we assume) is to aim at raising low income housing.[14]

Matching Grants: A more efficient way of increasing the housing expenditures of low income families is through a matching grant or approach (3). By matching own-expenditures, the household experiences a favorable substitution effect, leading to increased own-expenditures. As a result, the desired level of housing consumption can be obtained at a lower program cost. Such a

[14] R. Muth (op. cit., p. 47) in fact supports his recommendation for a rental subsidy program by arguing that it will be ineffective in increasing housing expenditures even though earmarking occurs. If the objective is, in fact, to give income support without interfering in expenditure choices, there would seem to be no point of recommending a rent support program to begin with.

policy however, would, induce low income families to reduce their outlays on other items, so that "food" or "clothing poverty" might be substituted for "housing poverty." For this reason the matching grant technique—although it is the appropriate instrument for dealing with most merit good situations—is less suitable in the context of our problem, where the stated policy objective is to relieve housing poverty without inducing poverty levels in other items.

Theoretically, leakages would be best avoided by combining an earmarked grant with the condition that the pregrant level of expenditures must be retained, thus assuring that the grant payment is in fact used for the purchase of additional housing. Unfortunately, this solution is ruled out by administrative difficulties. As a second best and feasible approach, the grant might be made contingent on an expenditure equal to, say, 25 percent of income, and the amount granted might be set equal to the difference between needed expenditures and the level provided by such a 25-percent outlay.[15] As a result, spillover into other expenditures would be limited to own-expenditures in excess of 25 percent of income, and replacement of housing with other poverty gaps would be avoided.

Types of Supply Support

We now turn to forms of support which are directed at the supply side of the low income housing market. Insofar as the leakage problem is concerned, subsidies to the supply side are more or less similar to matching grants on the demand side, because they reduce the cost of housing to the occupier. Like the latter, they are a more effective way of stimulating housing consumption than are general income supports and superior also to earmarked but nonmatching grants to the occupant. At the same time, application at the supply side of the housing market makes for significant differences in application and possible effects.

Minimum Standards: A policy which sets and effectively enforces minimum standards for low income dwellings but does nothing else will reduce the supply of housing available to low income families. If the standard is limited to new construction which becomes more costly, low income families (finding new housing more costly) will bid up the price of old substandard housing. Rents in such housing will rise, so that a "filtering-up" of benefits will ensue. In the longer run, all housing will have to come to meet the standard, and low income families will be forced to purchase more expensive (though better) housing. They may be forced to move out of "housing poverty" (or to reduce their housing shortfall) but only at the cost of being forced into poverty standards on other outlays. As seen from their point of view, minimum standards without financial support impose a burden rather than a gain. If the objective is merely to force a shift in the expenditure patterns of low income families towards housing, such a policy may make sense; but if the objective is to improve the welfare of low income families in the process, the policy is counterproductive. Minimum standards without aid are similar in this respect to a minimum wage policy without supporting measures of training, job creation, or unemployment relief.

Although it is evident that a minimum standard policy by itself cannot do the job, the above reasoning does not make a case against the use of minimum standards as part of a broader policy package. Combined with financial support, elimination of substandard units serves the purpose of assuring the use of earmarked grants for housing purposes. In situations of highly inelastic supply of low income housing, enforcement of service standards may be equivalent to a tax on landlord profits, with the proceeds used to provide services to the tenants. In other situations, it may induce the owner to abandon rather than to improve old structures. In the longer run, minimum standards that require new construction of low income housing to be of higher quality may generate economies of scale and technological advances. By reducing costs, these will raise the level of low income housing as well as provide a general gain in the welfare of low income families. Finally, standards may serve to protect uninformed tenants against inadequate rental contracts or be needed to assure public safety. For these and other reasons, minimum standards play a useful role as part of the total policy package, but taken by themselves they are not adequate to improve the position of low income families.

The "Filtering-Down" Strategy: Indirectly, the supply of housing to low income families may be increased (so it is argued) via a filtering-down strategy. To simplify, we divided families into "high" and "low" income families and assume that the policy objective is to raise the level of housing consumption by low income

[15] For such a proposal see Henry Aaron, op. cit., p. 167.

families. It would seem obvious in this case that the best approach is to use the funds in direct support of low income housing. Support of high income housing may benefit low income housing through a filtering-down process, but one would expect the resulting gain to low income housing to be less than that which would result from its direct support. The discarded houses may be unsuitable for low income families and their decline in price may be dissipated in the case of "filtering down." If so, U.S. housing policy (see Table 1) can hardly be described as having followed a "filtering-down strategy" in the support of low cost housing. Rather, the housing program (primarily via income tax preferences) should be interpreted as a policy aimed at aiding middle and high income housing, while viewing benefits to low income housing (generated by a filtering-down process) as a more or less incidental byproduct only.

To view "filtering down" as a primary (rather than byproduct) strategy for the support of low income housing, it must be argued that the results for low income housing will, in fact, be superior to low income families than would be the case with direct support to low income households.[16] To explore this possibility, suppose that a grant of $10,000 is given to high income household H on a matching basis so that the net price that H must pay for a given housing level is reduced. Such is done, in fact, through income tax preferences where exclusion of housing costs from the income tax base is equivalent to a matching grant equal to the taxpayer's marginal bracket rate. As a result, H will purchase more housing. Not only is his housing demand increased because his tax is reduced (the income effect), but also because housing has become cheaper relative to other goods (the substitution effect). Suppose also that his increased consumption is met through a new and better house. As a result, he will sell his old house, which will now become available to low income households at a lower price. This is the gain to L which is referred to by the "filtering-down" argument. Given a cost of the matching grant to H of $1,000, can the filtering down gain to L exceed $1,000, the amount which he would gain if the grant were made for low income housing directly?

Provided the grant is in matching form, it is quite possible that H's increase in housing expenditures will exceed the amount of the grant, i.e., that the substitution effect will lead to an increase in his own-expenditures on housing. Such will be the case especially if his demand for superior housing is price-elastic and if supply is elastic as well. Assuming also that the increase will be directed at new housing (whether the improvement is real or imaginary does not matter), more old (and previously considered superior) structures will be discarded and become available for purchase by L. Thus the "filtering down" gain to L will be greater. At the same time, the net value of the grant to H (the effective matching rate) will be less if a large discount has to be taken in the sale of the old residence. Thus, further down the line, L's gain becomes self-limiting as a larger reduction in the unit cost of discarded houses will also reduce the demand for new and superior construction, and hence the discard of old houses. While the factors involved are complex, it is possible, though not likely, that L's gain could exceed $1,000 or the value obtained through a direct grant to low income housing.[17]

Subsidies to Private Housing Supply: Except for income tax preferences in support of ownership and the limited rent supplement program in support of tenants, the traditional approach of U.S. housing policy has been to direct supports at the supply rather than the demand side of the housing market. Thus, ownership support has been given in the form of support to the suppliers of mortgage credit while rental support has been given in the form of credit and tax support to the suppliers of rental housing. In a perfect market this would not be a major problem. The benefit incidence of the housing subsidy scheme would be the same on whichever side of the market it is applied. In the real world setting, this may not be the case, and the impact point comes to be of importance.

Support which is to be conditional on the maintenance of own-expenditures or to be adjusted to the economic position of the family unit, must clearly be occupier-related. This establishes a presumption in favor of direct aid to the occupier, just as the personalized individual income tax must be assessed on the household, as distinct from an in-rem type payroll tax which can be assessed on the employer. Nevertheless,

[16] Otherwise, the support for high income housing can be rationalized only if such support is included in the "objective function" as an explicit policy objective.

[17] The value of the filtering down process to L will be less if the grant to H is made not on a matching but an outright basis, in which case H's own-expenditures on housing will fall and the discard of old houses will be less.

given the lumpy nature of housing outlays and the imperfect structure of the housing market, there may be reasons for directing aid at the supply side.

Thus, mortgage guarantees and underwriting (involving subsidies to the lender) have been powerful vehicles of broadening the ownership base. By reducing credit risks, lowering down-payments, and facilitating longer amortization periods, they have greatly lowered the threshold at which ownership becomes possible. These objectives could not have been accomplished as effectively by interest subsidies to the owner, such as are given by income tax preferences. However, the benefit impact of such programs in support of ownership has been largely over the upper and middle rather than the lower end of the income scale. While the rural poor frequently own their substandard housing, they are not readily able to make use of mortgage facilities.

Regarding rental housing, which remains the major form of housing consumption at the low end of the income scale in urban areas, it is tempting to argue that rent subsidies to the occupier (rather than to the landlord) are the obvious solution. Support of rental payments, by raising demand, should cause the desired increase in supply to be forthcoming; and by leaving the choice of the unit to the tenant, he is left with a wider range of options. All this, however, assumes that supply is elastic. If supply is inelastic, increased demand will simply bid up prices and raise the rental income of landlords. The benefits of the program are then shifted to the landlord, and the objective of improved low income housing in not accomplished. Just as in the design of tax policy, the shifting of tax burdens must be accounted for and the policy judged in terms of the ultimate burden of distribution; so must expenditure policy allow for "benefit snatching" and focus on the final benefit incidence which will result.

One need not be an expert in housing markets to recognize the existence of important rigidities. Inelasticities in supply arise from limitations of space, the dead weight of existing structures, housing discrimination, and other factors. While an increase in demand, financed by rent subsidies, may call forth improvements in existing structures, it will not readily increase the overall supply, except indirectly where abandonment is prevented. On the demand side, inelasticities arise from limited employment options and housing segregation. For these reasons, rent subsidies may be dissipated at least in the short run. This difficulty can be avoided if supply is made more elastic by giving incentives to suppliers, i.e., if the subsidy is made conditional on increased supply of low cost housing. Supply incentives and their integration into a housing-oriented concept of urban development therefore remain necessary, especially in the urban (inner city) setting, where supply rigidities are especially pronounced. At the least, rent subsidies need to be linked to enforcement of minimum standards, including improvement of existing structures. More likely, an efficient program of support for low income housing—especially inner city urban housing—must include measures aimed at both sides of the market.

Public Housing: The next question is whether, to the extent that supply support is to be given, it should be in the form of publicly owned or publicly supported private housing.

Much of the criticism that has been heaped on the "ogre" of public housing is directed at avoidable defects which are not a necessary feature of public housing. These include the presumed "ugliness" and barracks-like nature of public housing developments, an incentive structure which penalizes maintenance and therefore induces excessive capital intensiveness of new structures, inadequate supporting services such as police protection, and so forth. These are defects which should be avoidable by better program design and correction of which would improve the image of public housing.

Many of the difficulties that have been associated with public housing in the United States are not problems of public housing in general, but problems of public housing for the very poor. These problems have not arisen in other regions—such as the United Kingdom and Scandinavia—where public housing furnishes a large share of lower-middle income housing and of housing for the aged. It thus appears that our public housing has run into difficulties precisely because it has been the part of the housing program directed at the most urgent aspect of the housing issue or a provision of housing to the very poor. If public housing has been defective, it has also been the only part of the housing program which was truly needed.

Nevertheless, consideration needs to be given to improving this part of the housing program. On the one hand, assigning a limited supply of public housing to the poor helps to assure that it will be used where most needed.[18] On the other hand, such limitation imposes the stigma of poverty on the tenants of low cost housing projects, a stigma which they hope to leave behind. While long waiting lists for public housing openings suggest that the fear of stigma might be exaggerated, or in any case is outweighed by the need for more adequate facilities, it nevertheless poses a problem. To some extent the solution might be found in the dispersal of public housing facilities and the breakup of low income housing projects into smaller units. Also the problem might be approached by increasing public housing facilities and making them available (with the use of differential rental charges) to family units with income above the poverty line, or by supplying public housing (following the example of European countries) to the aged. Finally, the need for low income public housing would be reduced by an effective increase in the supply of low income private housing.

The choice among these alternatives should be seen not as a matter of principle but in pragmatic terms. For the more comfortable (and also less necessary) part of the housing program which deals with support for lower and middle income housing, the preference of the American public is clearly for owner-occupancy and hence private housing. For the more crucial part of the housing problem which deals with low income families, the primary concern remains with rental housing and, for that matter, with rental housing in the inner city. Adequate provision for such housing is not only a matter of inability to pay the necessary price. Structural aspects of the housing market, including political and social factors, must also be considered. Given these limitations, it does not seem feasible to deal with the urban low income housing problem exclusively in terms of demand support (which is subject to dissipation into higher rents) or through support of increased supplies of private housing for low income tenants. While these approaches should be used, the urban concentration of low income families and the difficulties in the way of securing an adequate supply of private housing for such families suggest that public housing can hardly be dispensed with. Moreover, it should be emphasized that the "publicness" of public housing is a matter of degree. In a situation where private housing is heavily government-supported and the risk is largely government-assumed, the concept of private ownership becomes quite relative. The problem then is one of managerial arrangement rather than ownership as such.

[18] Another point given much emphasis by R. F. Muth, is that the benefits of public housing can be shared by only a few thus involving a "lottery" feature, which is avoided by a rent support program the benefits of which can be spread more broadly. Public housing is thus criticized for its lottery characteristics. The validity of this criticism, however, depends on how the limited supply of public housing is rationed out. If it is given to those most in need of support, the lottery analogy fails and the results will correspond to allocation of cash grants to the most needy families. Comparison of highly limited public housing with a very ample general grant system is hardly legitimate. Moreover, the lumpiness of public housing benefits may be reduced by combining an increased supply of facilities with higher (and scaled) rental charges to residents.

Conclusion

The preceding discussion has dealt with the rationale for government support of housing and its effective implementation. Other aspects such as regulation and stabilization have not been examined. The present housing program consists of three parts: (1) Ownership support given in the form of income tax preferences and accruing largely to middle and upper income housing, (2) various credit supports benefiting middle and lower middle income housing, and (3) public housing and rent supplements aimed at distinctly low income housing. Of the total cost involved, the figures given in Table 1 suggest that (1) absorbs about 80 percent while the remaining 20 percent is divided about equally between (2) and (3). Even if the estimated 80-percent ratio should prove somewhat high, this does not add up to a satisfactory structure of housing support.

Rationale for Housing Support

We have examined various reasons on which a case for housing support through the public budget may be based and have concluded that:

1. Shelter is essentially a private good, so that the social-good rationale for public provision (based on free consumer choice) does not apply.

2. Although housing generates external benefits and costs, as do other forms of consumption, there does not appear to be a clear case pointing to unusual external net benefits which would justify general support for housing as distinct from other consumption on these grounds.

3. Externalities generated by housing at the same time call for a regulatory or planning concern with the housing market, as do market imperfections, but such measures differ from the general case for financial support, which is our primary concern here.

4. As against this framework of individual choice, society appears to consider homeownership as especially "meritorious" and hence deserving of particular support.

5. Society's concern with relieving poverty may take the form of providing a general income floor or it may take the more selective form of assuring minimum levels of consumption for essential items. The desire to assure minimum levels of shelter, i.e., to relieve "housing poverty," appears to have been the rationale for assistance to low income housing.

Among these various considerations, the concern with elimination of housing poverty appears to offer the strongest case for support, yet it is given least attention in the overall program. In my view, this calls for a substantial reorientation of housing policies.

Ownership Support

As noted before, government support for housing is dominated by the massive aid to homeownership given through the present income tax treatment, which permits deduction of interest without requiring inclusion of imputed rent. While this aspect of the tax law is not usually considered part of the housing program, it should be treated as such since the loss of income tax revenue due to this allowance is, in fact, equivalent to a "tax expenditure" on such support. One question which arises is whether the objective of homeownership is in fact sufficiently important to merit such support. Beyond this and more readily dealt with there is the question of whether the present income tax treatment offers an efficient way to induce homeownership. Closer consideration shows this not to be the case. Even if the more difficult move towards inclusion of imputed rent is set aside, transforming the interest deduction into a limited credit against tax, and imposition of a credit ceiling, would permit substantial savings in cost and improvements in tax equity, without thereby reducing effective inducement to ownership over those income ranges where it is most needed.

Other supports to homeownership, such as mortgage insurance and related credit supports, have not suffered from these defects. They have been generally constructive means of broadening the base for homeownership and should be continued.

Supports for Low Income Housing

In dealing with instruments for the support of low income housing, the problem is largely one of rental housing, especially in the urban setting. Here we conclude that:

1. General income support is not an efficient way of dealing with the objective of reducing housing poverty.

2. Limited earmarked grants, but unrelated to the level of own-expenditures, are not much better.

3. The matching grants, though generally appropriate in dealing with merit goods are less suitable in this context.

4. The best (or for that matter practicable second-best) solution is given by earmarked grants, given conditional on the maintenance of own-expenditures at or above, say, 25 percent of income.

Regarding the implementation of grant design, we further concluded that:

1. Rent supplements to occupiers (tied to an own-expenditure floor) should be used but combined with measures aimed at the supply side of the housing market. An all-out switch to rent support payments to the occupier would not be desirable.

2. Policies aimed at the supply side should include incentives to increased supply of private housing, but public housing will remain an indispensable part of the program in dealing with situations of greatest distress, and major attention should be given to its improvement.

In all, the design of support for low income housing must make due allowance for the particular circumstances of the low income housing market, circumstances which, for various reasons, make more or less exclusive reliance on the market mechanism more difficult than is the case in other areas such as for food supports given through a food stamp program. While this is not to counsel against the use of a general rent support program for low income families, I would emphasize the continuing need for accompanying such a program with other measures.

Appendix A
Are Housing Provisions of the Income Tax Part of the Housing Program?

As shown in Table 1, inclusion of income tax preferences as a regular part of the Government's housing program changes the benefit pattern drastically. Whereas the program excluding income tax provisions yields benefits which are divided about equally between middle and lower income groups, inclusion of tax benefits yields a pattern showing that up to 80 percent of benefits accrue to high income households. The question of whether or not these "tax preferences" are properly included as regular parts of the program is therefore of crucial importance in evaluating the Government's effort in the housing field. The problem involves certain principles of income taxation which will be considered briefly here.

Three Premises

We begin with three premises which we believe fair observers can agree upon without too much difficulty. They are as follows:

1. An arrangement which bestows benefits on particular forms of consumption or investment is a subsidy, whether it is given in the form of outright payment under an expenditure or as tax relief under the income tax. Thus an investment credit under the income tax is no less an investment subsidy than is an investment grant which is given outside the tax system. Similarly, if homeownership is given the benefit of tax reduction, the benefits to the homeowner and the cost to the Treasury (and hence to other taxpayers) is the same as if an identical cash payment were made without giving a tax benefit.

2. There is much to be said for giving subsidies, whether to housing or other forms of consumption in a direct way and outside the tax system. This is the case for a number of reasons. Use of the tax relief approach is likely to involve a less careful design of the subsidy structure. For instance, by permitting benefits to the homeowner to accrue through a diminution in his taxable income, rather than as a credit against tax liability, the benefit per dollar of housing expenditure (or the Government's implicit matching rate) becomes a function of the homeowner's marginal rate of tax and hence increases with income.

3. An expenditure program providing matching grants for private housing expenditures would hardly follow this line, but would more likely show the opposite pattern. Moreover, formulation of the support program through an appropriation committee with expertise in the matter is likely to develop a better design than the tax committees, which are less well equipped to deal with housing matters. Finally, if supporting legislation has to be voted as explicit expenditure programs, the public will be better informed with what goes on so that there will be a better ordering of expenditure priorities. For these reasons, housing support programs should be taken out of the income tax and (to the extent that they are to be continued) transformed into explicit expenditure measures.

Given the preceding premises, it remains to be shown that the current income tax treatment of homeowners does involve, in fact, "tax preference," i.e., offers advantages which accrue from homeownership alone and cannot be justified for reasons other than desire to give special support to such consumption. The issue must therefore be viewed in the broader context of how taxable income should be defined for income tax purposes. To this we now turn.

The Concept of Income for Income Tax Purposes

To decide what constitutes "equal treatment" of homeowners, or—as a corollary thereto—what constitutes preferential treatment of this group, one must first establish how the concept of income is to be measured for tax purposes. Income for tax purposes should be measured so as to give a meaningful and comprehensive index of taxpayers' ability to pay. For this purpose, income should be defined as comprehensively as possible and the tax should then be imposed so as not to discriminate among various sources of income, and it should be independent of how such income is to be used. While costs of earning income should be deducted, as the underlying concept must be one of net income, all such net income should be included in the base. This clearly takes in all the money income, but certain forms of imputed or unrealized income must also be included.[19]

Treatment of Imputed Rent and Mortgage Interest

In the absence of preferences, a person's tax liability should be the same whether he (1) purchases a $30,000 house outright, (2) purchases a $30,000 house which is financed by mortgage while using his own funds for other investments, (3) rents a $30,000 house while investing his funds otherwise, or (4) chooses to consume less housing services under any of the three indicated approaches. The present treatment, which does not include imputed rent in the tax base and permits deduction of interest payments, favors a taxpayer following patterns (1) and (2) as compared to (3). The renter, following pattern (3), must pay tax on his investment income while enjoying no housing deductions. The mortgage owner, following pattern (2), may offset his earnings from other investments by his interest deduction and thus also pays no tax on such income. The equity owner, following pattern (1), similarly receives no taxable income and hence pays no tax. If one were to disallow the interest deduction, the taxpayer following pattern (1) would still remain tax-free, while deduction of pattern (2) would not involve the same tax treatment as for pattern (3). Only inclusion of imputed rent (i.e., net rent without interest deduction, or gross rent with interest deduction) would subject pattern (1) to the same tax treatment as the other two groups. The same holds with regard to equalizing the position of those who consume $30,000 of housing services with those who, following pattern (4), consume less.

The present practice, by favoring patterns (1) and (2) is regressive in its burden incidence because rental housing is of particular importance at the lower end of the income scale. Disallowance or limitation of interest deductions alone would improve matters, but it would still leave a substantial advantage for equity owners, i.e., for a pattern of housing consumption which is more readily acceptable to high income groups.

The inclusion of imputed rent is thus needed for a neutral treatment of homeownership. Given the rather obvious conclusion, it is surprising that imputed rent is universally disregarded in the income tax base. While the determination of imputed rental values poses certain difficulties, they are not insuperable, especially not in conjunction with an effective administration of the property tax. The answer, rather, lies in the somewhat subtle nature of the imputed income concept and the fact that homeowners everywhere are a powerful force in tax legislation.

At the same time, it must be admitted that the case for disallowing the interest deduction is more readily explained than that for inclusion of imputed rent.[20] While it is evident that interest incurred as a business cost should be a deductible charge against the income earned with such borrowed capital, it can be readily seen that there should be no such deduction if the income earned therewith is in imputed form (i.e., imputed rent) which is not included in the tax base. The inclusion of imputed rent itself is a more subtle issue, and the question might be raised whether a similar problem does not also arise with regard to other durable consumer goods, such as automobiles and appliances. In principle, the answer ought to be in the affirmative, but it must be noted that the amounts involved are very much smaller than is the case with housing, especially over the middle and higher income groups. In all, it is therefore reasonable to focus on the housing case without attacking the problem on a universal basis. Taxation, like other phases of public policy, cannot hope to establish the best of all worlds, and efforts must be concentrated where the payoff will be greatest.

Treatment of Property Tax Deduction

The case for or against property tax deduction should be viewed along with that for other State and local taxes. If such taxes are interpreted as household expenses for the purchase of State and local government services, a case can be made that all such deductions should be disallowed. If, on the other hand, they are viewed as preempting the income available for household use, deductibility is in order. Between these two extremes, observers are generally in agreement that deductibility of typical benefit taxes such as gasoline taxes should be disal-

[19] Another major aspect of the Intertax problem relates to the treatment of capital gains, including the question whether realized gains should be taxed at preferential rates and the further question, whether at some point unrealized gains should be included in the tax base. This problem has some bearing on the housing issue as housing, via the mortgage leverage, is the best instrument by which middle income investors may secure capital gains. However, this is somewhat of a side issue and therefore not dealt with in this connection.

[20] Inclusion of imputed net rent implies inclusion of imputed gross rent minus depreciation charges and minus interest on mortgage debt.

lowed. Similarly, disallowance would be in order for special assessments levied at the local level. At the same time, some allowance for State income taxes (whether in the form of deductions or credits is a different matter) seems in order. The question then is how the property tax fits into this spectrum. There seems little reason for thinking of the property tax as a benefit tax in the sense that the expenditures which it finances will accrue in proportion to homeownership. Rather, the property tax has come to be more or less a general revenue tax at the local level, covering the bulk of education expenditures as well as other local outlays. For this reason, it seems questionable whether deductibility of the property tax should be considered a particular "homeowner preference"; certainly the basis for such interpretation is weaker than in connection with interest deduction and/or failure to include imputed rent. As noted before, exclusion of the property tax deduction from the preference concept reduces the part of the housing support granted by other income tax structure from $9.5 billion to about $6 billion, thereby, lowering to 50 percent the benefit share received by homeowners in the upper and middle-high income ranges.

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Appropriate Role of Government in Housing

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Introduction

Like Topsy, the Federal Government's commitment to massive housing and urban rehabilitation programs "just grew." The initial impetus was largely humanitarian and based on the widely held observation that families with "inadequate" housing were often prey to the problems of poverty, crime, and bad health. Without necessarily implying a causal mechanism, a national housing policy was regarded as a useful, albeit partial, solution for the problems of the poor. Further impetus for these programs came from the desire to rescue downtown areas from economic and physical decay; widely held esthetic and ethical concerns also required the removal of blighted areas from our cities.

Whatever the reasons for the growing national commitment to housing and urban redevelopment, these programs, as well as other social programs that give consumers specific products, are widely believed to have been largely unsuccessful and are now under fire from many quarters. One set of critics argues that the direct product approach is justified for housing, but that the programs have not met the high expectations set for them because they were hastily and somewhat thoughtlessly put together, badly administered, and insufficiently financed. Another set of opponents attack either the goals of the housing program or argue that these goals can be better achieved with income transfers. This paper deals with the issues raised by the second group of critics and evaluates the arguments and proposals for government intervention in the housing sector largely from the perspective of welfare economics.

Ever since Adam Smith's discussion of the "invisible hand," welfare economists have been seeking to demonstrate that a "competitive economy" is, in some sense, "best." A widely accepted result—the two optimality theorems of welfare economics—serve as the basis for much of the current discussion. Arrow [2, pp. 942–943] states them as:

> (First Optimality Theorem). If a competitive equilibrium exists at all, and if all commodities relevant to costs or utilities are in fact priced in the market, then the equilibrium is necessarily "optimal" in the following precise sense (due to V. Pareto): There is no other allocation of resources to services which will make all participants in the market better off. . . .
>
> (Second Optimality Theorem): If there are no increasing returns in production, and if certain other minor conditions are satisfied, then every optimal state is a competitive equilibrium corresponding to some initial distribution of purchasing power.
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> Operationally, the significance of this proposition is that if the conditions of the two optimality theorems are satisfied, and if the allocation mechanism in the real world satisfies the conditions for a competitive model, then social policy can confine itself to steps taken to alter the distribution of purchasing power. For any given distribution of purchasing power, the market will, under the assumptions made, achieve a competitive equilibrium which is necessarily optimal; and any optimal state is a competitive equilibrium corresponding to some distribution of purchasing power, so that any desired optimal state can be achieved.

In the rest of the paper we shall have occasion to refer back to these results to illuminate some of the problems of housing policy. These theorems help make the competitive equilibrium model (where all consumers and producers take the same set of prices as given and supply equals demand in all markets) serve as a useful benchmark against which to evaluate an economy. Most economists understand this model, know what happens when its assumptions are violated, and are therefore likely to accept the policy prescriptions implied by its analysis. By now there are standard lists enumerating the ways that the assumptions of the model might be violated along with possible remedies. (For an excellent summary see Steiner [17] and Arrow [3].)

To some extent my task is different from most of the members of the study group; it is to provide a framework for decisions on housing policy and to stake out areas for further analysis. In doing so I have examined the housing sector in the context of the standard arguments for government intervention in the economy. The relevance of each of these arguments is an empirical, not a theoretical, issue, so that the results of this paper are largely taxonomic rather than descriptive or prescriptive.

The first section deals with questions of efficiency in a competitive economy. The First Optimality Theorem requires that "all commodities relevant to costs or utilities are in fact priced in the market." When this assumption does not hold, we shall refer to the situation as one of nonmarketability. Most of the discussion centers on externalities and uncertainty, the two major examples of nonmarketability in housing markets. The problem of increasing returns will also be touched upon.

A true social optimum also requires the appropriate distribution of income. In the second section we are concerned with both the effects of the distribution of income on housing markets and the effects of housing markets on the distribution of income. Another set of problems, which we discuss in the third section, arises if either housing or some other market is noncompetitive or if there is government intervention in the economy. There are also equity and efficiency considerations in macroeconomic policy; the optimality theorems do not hold when there are involuntarily unemployed resources, since these resources could be used to increase someone's happiness. The relation between housing policies and economic stability will be discussed in the fourth section. The last section provides a short summary of the results.

Textbook discussions find it easy to separate clearly the issues that are raised when the assumptions of the model do not hold. In the analysis of actual policy problems, when one of the assumptions necessary for Pareto Optimality is violated, then others are likely to be violated as well. This may often make the analysis less clearcut, but one hopes more realistic, than this outline indicates.

Housing Policy and Efficiency in a Competitive Economy

Using the competitive economy as a guide, we will explore the conditions that lead to an inefficient allocation of resources in the housing market. The major source of difficulties, within a competitive framework, arises from the nonmarketability of relevant inputs and outputs and from the costs of organization and information required to internalize the externalities. Other difficulties arise from the problems of increasing returns.

Externalities

In housing policy, as in other areas, the key argument for government intervention comes from the presence of externalities. The market mechanism does not make the externality economically relevant for the decisionmaker, so that government intervention may be needed to reach a social optimum. Two kinds of externalities are considered important for housing policy—"neighborhood externalities," whose effects are largely limited to the local area, and externalities deriving from interdependent utility functions (i.e., a consumer's utility depends on the happiness or consumption of other consumers), which affect a wider segment of society.

At this point it might be useful to clarify some of these distinctions. For illustrative purposes, let us assume that bad housing causes serious illness. If only the residents of the housing were made ill, then this is analytically similar to peeling paint and bad plumbing; it is another characteristic of the general unpleasantness of bad housing and part of the burden of being poor. There are no externalities and the price of housing presumably reflects the increased likelihood of illness, so no intervention is called for on efficiency grounds. If, however, the illness were infectious over a clearly defined geographical area, then the neighborhood externalities are clear, and we might expect some cooperative attempts by the residents to improve their housing. Nonneighborhood type externalities would occur if the amelioration of the illness of residents of this area were a concern of the residents of other areas. (This case of interdependent utility is clearly related to the idea of "merit wants"—wants that are so meritorious that they should be met. It is also related to the problems of income distribution discussed in the second section.) Since those concerned with the health of others are likely to be geographically widespread and have other concerns as well, the costs or organization will be very high and, on efficiency grounds, some form of government intervention may be called for. The strongest case for intervention, however, can be made when the illness caused by the poor housing is communicable to the rest of the population. Here the costs are likely to be large and clear and the costs of organization high. Improving housing then would become a clear national goal. The appropriate policy then depends crucially on the actual facts of the case, though the theory can indicate where we might look for them.

The type of externality caused by neighborhood effects is clearly illustrated; if the value of a house depends on the level of maintenance of all of the other houses in a neighborhood, then if each landlord ignores this externality he will maintain his house below the social optimum. In fact, it is common for intermediate economics textbooks [15, pp. 304–313] to combine this externalities argument with strategic problems and conclude that the private housing market is inefficient and some government intervention is necessary. The strategic elements are often of the game theoretic "prisoner's dilemma" type, for it can be shown that if the neighborhood effects are strong and no collusion between landlords is possible, then it will be rational to undermaintain property [6]. A given landlord knows that if others improve their property and he does not, he will benefit, while if the others do not improve their property, he surely will not benefit by improving. It is then "rational" not to improve the property. If all property owners act this way, the area will become rundown, even though if all improved their property and took advantage of the neighborhood effects their joint rate of return would be higher. Thus externalities and strategic elements prevent a social optimum. The detailed "prisoner's dilemma" is probably a useful parable for understanding the continuation of blighted areas, though for most purposes the presence of neighborhood externalities is sufficient to demonstrate that there is an underinvestment in housing maintenance. The traditional solution to this problem is government intervention—it could either subsidize maintenance or penalize nonmaintenance (i.e., fines for the violation of building and zoning codes).

In the absence of large organizational costs or strategic elements, government intervention may not be necessary; the propertyowners in the area would agree on a joint-maximizing solution that makes them all better off—the externalities would become internalized. If the costs of organization, "free rider" and other strategic problems arise, then the propertyowners may wish the government to police the agreement. It might be noticed that the "prisoner's dilemma" always appears in the section on noncooperative games. If cooperation can occur, then bargaining may achieve the social optimum. Government has a clear role in helping the property owners to cooperate but, in this case, a subsidy is not necessary.

Although this view of neighborhood externalities is widely held among analysts of the housing market, it does leave some puzzling questions. Our discussion of these externalities did not necessarily involve the terms "bad housing," "slum," or "blight." The argument for neighborhood effects probably applies to all housing, and yet no one would argue that a housing maintenance subsidy should be given to propertyowners in Chevy Chase, Md. A number of hypotheses are possible. A likely one is the existence of a "threshold effect"—even though all property owners undermaintain their property by ignoring the neighborhood effect, once a certain level of maintenance is reached the ratio of external to internal benefits becomes small. If this is true, it would argue for a differential subsidy for poor neighborhoods. Another possible explanation, most relevant for single family and small multifamily dwellings, stems from the observation that better neighborhoods are more likely to have the propertyowners in residence. They are also more likely to be subject to pressures from their neighbors to take account of neighborhood effects and achieve joint utility maximization. Similarly, "good" neighborhoods are often stable neighborhoods where the pressures for maintenance are strong. Since costs of organization are likely to be much less where propertyowners are in daily contact, a subsidy to residential ownership of property can be regarded as a good substitute for more expensive alternative costs of organization.

There is still another problem with the presumption that the neighborhood externality effects are large; if this presumption is true, why do not developers buy up slum neighborhoods and why do not government redevelopment agencies reap huge profits? Proponents of this view respond by pointing to strategic problems of dealing with individual parcel holders. Clearly this cannot apply where the government has exercised its right of eminent domain; and one can discover many situations where developers have assembled numerous plots of land despite strategic complications. It may be that the neighborhood externalities are not that large and that urban blight is due to other causes.

Neighborhood externalities are not the only ones considered relevant for housing policy. It is argued that most American citizens are concerned about the housing of the poor. The illustrations run the gamut from the child who becomes a ward of the State because of brain damage caused by lead paint in old housing, through the unhappiness caused all of us by the relationship between bad housing and other social ills, to the commuter who is upset while driving to work by the ugliness of dilapidated housing.

I assume that the other papers are evaluating the empirical relevance of these and similar examples of nonneighborhood externalities. Except for the case in which the quality of one individual's housing enters directly as an argument in the utility function of another, the presence of externalities need not imply additional expenditures on housing. There may be cheaper ways to eliminate the externality. For example, the commuter might be helped by planting large elms along the road adjacent to the slums, or expenditures on public health nurses may more than compensate for the health effects of bad housing. Or, as many have advocated, giving income to the poor may be the most efficient way to eliminate these externalities.

Another form of the interdependent utility argument relevant for homeownership stems from a belief that at any level of income homeowners are likely to be more conservative and responsible citizens who increase the stability and welfare of society. The argument is similar to that made for the necessity of minimal citizen education for a democracy. Historically, it seems to be linked to views about the English yeoman class and the growth of parliamentary democracy. While this opinion is widely held, it is difficult to evaluate but probably explains conservative support for government aid to homeownership.

Unborn Generations

The welfare of future generations is another commodity that is not properly priced by competitive markets. It is very difficult to know what the needs of our descendants will be, though it is quite likely that they will want as much of everything, including housing, as possible. There is no way in which their preferences as to the level and composition of the capital stock enter into market decisions. Needless to say, the issues are complex and revolve around the savings rate and the fungibility of the stocks of plant and equipment and housing. This consideration implies that government may have a legitimate concern in seeing to it that the housing that is currently built will either be useful to the future or easy to demolish.

Decreasing Average Costs

Still another argument for government intervention in the competitive economy occurs where there are sizable economies of scale resulting in decreasing average costs. In this case competitive firms suffer a loss and a competitive equilibrium may fail to exist. Though this argument is less intuitive to noneconomists than some of the others we have discussed, it is part of the standard elementary economics textbook literature [14, pp. 501] and can be easily sketched.

Competitive firms maximize their profits by setting price equal to marginal cost. (This is a major reason for the optimality of perfect competition; the resources used by producers to take an additional unit of the good, the marginal cost, is equal to the resources that the consumer is willing to forgo for an additional unit of the good.) From the relationship between average and marginal costs it follows that if average costs are falling, then marginal cost must lie below average cost. For example, if the average height falls as an additional man enters the room, then the height of the additional, or marginal, man must be below the average. Since competitive firms find their profit-maximizing quantity where price is equal to marginal cost, their total receipts (price times quantity) will be less than their total cost (average cost times quantity) at this optimal quantity. Competitive firms in this industry would lose money and leave the industry, so this could not be a true longrun competitive equilibrium. The usual illustrations of longrun economies of scale come from the public utilities sector; such economies in the provision of housing services might occur if larger subdivisions lead to significantly lower average costs. In this situation monopolies might be able to make a profit, but would not be producing at the socially optimal quantity where price is equal to marginal cost. The presence of decreasing average costs in housing is an empirical question, but its presence would be an argument for regulation, subsidy, or nationalization.

Income Distribution

If the economy were operating at a Pareto Optimal resource allocation, we might nevertheless require government intervention in the housing market to improve the distribution of income. In a competitive equilibrium we might still have poor people living in "substandard housing" as a natural consequence of their "substandard" income. As the Second Optimality Theorem points out, however, we need not directly intervene in the housing market to help the poor, for with appropriate lump sum transfers of purchasing power, competitive markets achieve a socially optimal allocation of resources. Because of the political and technical difficulties of arranging feasible nondistorting income transfers, it may at times be necessary to sacrifice some efficiency in order to achieve greater equity.

Possible conflicts between equity and efficiency can be illustrated by extending our discussion of neighborhood externalities for rental housing in low income areas. Assume that the property owners recognize that by cooperating and improving maintenance they can all raise their rates of returns. Unless the higher maintenance expenditures somehow reduce other costs, higher rents are needed to get higher rates of return. These higher rents are more likely to be paid by new middle class people moving into the neighborhood, rather than the established residents. The poor would move to other areas, and if they could not afford to pay for good maintenance, new slums would appear. Only propertyowners would benefit and the improvement in efficiency caused by the internalization of the externalities might decrease equity.

This could be remedied by rent supplements to the poor so that they could continue to live in their improved neighborhood, or, if this is not possible, then current tenants might be given property rights that allow them to profit from the increases in efficiency.

To a large extent the arguments for more housing programs stem from a desire to help the poor. Traditionally, economists reply "supply equals demand" when confronted with allocational problems; today, when confronted with distributional issues they usually reply, "Use a negative income tax." The logic of the case for income as opposed to product grants is compelling. With additional income poor consumers can choose the commodities they wish. Barring externalities, they can be no worse off than if the government spent the money directly on the commodity; if there are wide differences in tastes there may be large gains in welfare. Although there is wide agreement on this view among economists, there are some dissenters such as James M. Buchanan. He argues that:

> The mere fact that some members of the community are poor does not, in and of itself, normally impose an external diseconomy on many of the remaining members. What does impose such an external diseconomy is the *way* that certain persons behave when they are poor. It is not the low income of the family down the street that bothers most of us; it is the fact that the family lives in a dilapidated house and dresses its children in rags that imposes on our sensibilities. And we are willing to pay something to remove this external effect; it is relevant for behaviour. Ordinary citizens are probably quite unwilling to finance substantial transfers of general purchasing power to the poor in their communities. But they are probably willing to finance specific transfers, either directly as income-in-kind or indirectly in purchasing power that is earmarked for specific items of spending (vouchers). [5, pp. 189–90]

Buchanan is arguing that there are important nonneighborhood externalities and that the housing of the poor and not the welfare of the poor should be the primary concern of a housing policy. Buchanan's argument is not convincing for, as Mishan [10, p. 192] points out, the externalities caused by poor people living in hovels could be internalized either by having the rich pay the poor to live in better housing or by having the poor compensate the rich for the unpleasantness they have caused. Since the latter would never be seriously entertained, we need to take equity, as well as efficiency, into account. Buchanan may well be correct in arguing that politically a housing policy will be more acceptable than an income distribution policy. If this is the case, then housing policies might serve as a useful tool for redistributing income. Although we shall discuss this matter in the following section, it is important to note that there is wide agreement that current housing programs (including income tax provisions) benefit the nonpoor. A concern for income distribution should require policies that compensate for this effect.

Any housing policy will affect not only the real income of the recipients but also the returns of factors of production and consumers of other products. The extent to which the recipients of the subsidy get its benefits depends, as is widely known, on the relevant elasticities and lag structures. Aaron argues that there are three effects:

> Those who receive the subsidy are encouraged by reduced costs to consume more housing services. The total demand for a capital intensive product rises, driving up the return on capital relative to that on labor. As a result, the price of all capital intensive goods rises relative to that of all labor intensive goods to the benefit of consumers who spend more of their incomes than average on labor intensive goods and to the detriment of those who spend less. [1, p. 50]

This type of general equilibrium approach is useful for clarifying the issues, but further empirical and theoretical work is required for its application to the housing market.

One likely effect, however, is that there will be large benefits to owners of factors of production that are in relatively inelastic supply to the housing industry. Landowners would be obvious beneficiaries of the subsidy, and we would expect part of the subsidy to be capitalized in land prices. Skilled building tradesmen with restrictive practices will also benefit—this will especially be true if the housing is government-built and subject to the provisions of the Davis-Bacon Act.

Second-Best Problems

To this point, our discussion of the housing sector has concentrated on competitive markets.

In this section we examine the effects of government intervention (e.g., the investment tax credit) and other noncompetitive elements (e.g., restrictive union practices) on efficiency and equity. When these imperfections can be removed, then the analysis simply follows that of the previous sections. However, when for political or other reasons these additional restrictions cannot be removed, then perfect competition elsewhere in the economy will not lead to a Pareto Optimum—the best that can be achieved is a constrained optimum—hence the term "second best" (or if we are really unlucky, "nth" best). In general, advocating perfect competition in the nonconstrained sector is not the second-best solution. There is no general theory, and second-best solutions are difficult to find—each case depends crucially on the detailed nature of the constraint. Though there are no elegant theorems to guide piecemeal second-best analysis, this type of approach is necessary for the understanding of housing sector policies.

Government Action Elsewhere in the Economy

Government behavior toward other sectors can often have a strong effect on the housing market. Analysis is difficult, since one is never sure if policymakers planned to affect the housing market or whether the effects were merely the unintended consequences of actions in other sectors. A good example of this problem is to be found in the Investment Tax Credit (ITC) whose primary stated purpose was to stimulate investment in plant and equipment. As Harberger [9] makes clear, it had a major impact on housing. It is a fact of national income accounting that savings is equal to investment; and since the ITC does not appear to have changed the savings rate, it cannot have changed the level of investment. In a fully employed economy, assuming appropriate stabilization policies, the primary effect of the ITC is not to increase gross private domestic investment, but rather to change its composition. It moves investment away from residential structures toward plant and equipment.

Depending on one's perspective, the ITC can be viewed as an unintended distortion of investment or as an attempt at a second-best solution, which compensates for the distortions already introduced into the system by government subsidies to housing and the corporate profits tax. In the first case, we assume that the pre-ITC world was optimal. The second argues that returns to corporate investment are much more highly taxed than housing and that consequently social returns are higher there; efficiency considerations thus require that corporate investment should be increased. Needless to say, a full evaluation of this argument requires knowledge of the incidence of corporate and housing taxes and subsidies.

In any case, it is clear that government actions directly affect the allocation of savings to housing. Since the housing industry is relatively unorganized, it might be useful to have housing's interests represented in a single place in the government.

Government Intervention in the Housing Sector

Zoning and minimal-maintenance-standards laws have been traditionally used to internalize neighborhood externalities. In the last section we mentioned some of their negative equity effects, but there are other problems as well. Zoning and maintenance standards laws are not changed as often as might be socially warranted—these outmoded standards raise costs to everyone and often prevent the building of housing that the poor could afford. (A standard example is the overelaborate, nonuniform detail that makes mass production impossible.) The obvious solution would be to modernize and coordinate these laws, but if that is politically impossible, then a second-best solution might require a housing subsidy.

The government encourages the consumption of housing through a variety of direct and tax subsidies; the effect has been, ceteris paribus, to increase the stock of housing and to alter the distribution of income along the lines suggested in previous sections. Some critics [1, Ch. 4; 8] have focused on the homeowners' preference provisions of the personal income tax code, which allow mortgage payments and property taxes to be taken as deductions while excluding the imputed rental income of housing from the tax base. These provisions, the critics argue, unfairly discriminate against renters and, because of the progressivity of the personal income tax, they are of most benefit to high income groups.

To evaluate these arguments we will first assume perfect markets and a proportional income tax. The tax subsidy to homeowners is usually calculated by estimating the increased tax that homeowners would have to pay if their tax preferences were eliminated. In general, we would not expect this estimated tax saving to be the same as the subsidy to current owners of housing since presumably some portion of the increased subsidy has been reflected in the price of owner-occupied housing. This point may be illustrated with reference to the subsidy received by owners of tax-exempt State and local bonds. Would anyone argue that the subsidy to State and local landholders is equal to the interest on the bonds multiplied by the tax rate? Of course not, since if anyone holds equivalent taxable bonds the interest rate on the nontaxable bonds must be lower. Clearly this interest rate differential must be taken into account when estimating the subsidy to holders of tax-exempt bonds. Many of the tax preferences in the present law have already been capitalized into the price of assets. Herbert Stein [16, pp. 20, 21] expressed this view when explaining his diminished enthusiasm for reducing tax loopholes and converting to a comprehensive income tax base:

> . . . many of the provisions of the law which 25 or 30 years ago I regarded as serious loopholes have remained there for all this time and a great deal of water has run under the bridge subject to these provisions of the law. People have acquired assets or liabilities in the expectation of the continuation of these provisions. The value of these preferential provisions has been capitalized into the value of assets and people have acquired the assets subject to this higher valuation. The beneficiaries of these preferences in most cases, or at least in many cases, are not the present holders of the assets subject to the preferences but those who held them at an earlier time and sold them with the value of the preferences reflected in the price.

If capital markets are perfect, then equilibrium in the housing market requires that for any consumers with identical tastes, income, and assets, the after-subsidy cost of equivalent housing must be the same whether the housing is renter- or owner-occupied. (If this were not true, consumers would move to the lower cost facility and raise its price until the costs were equalized.) To the extent that owner-occupied and rental housing are equivalent, we would expect a conversion to owner-occupied status until very little housing was available for rental purposes.

Aaron [1, Ch. 4], although he realizes that it is a rough approximation, makes the standard assumption of a perfectly elastic longrun supply curve for housing services (i.e., after all adjustments, housing prices do not change with quantity). A consequence of this assumption is that as homeowners' preferences are put into effect, they are capitalized and the price of houses rises; in the long run, however, rental housing is converted and new owner-occupied housing built until the original presubsidy price prevails. Since the price of owner-occupied housing does not change, all of the benefits of the subsidy accrue to the homeowner, but now since homeownership is cheaper there will be no equivalent new rental property. If rental property could not be converted to homeownership, the price of rental property would fall until the after-subsidy cost of housing to homeowners and renters was the same.

Whatever the longrun situation, in the short and intermediate runs there are likely to be higher costs associated with an increased supply of housing, especially with regard to desirable housing sites. In any case, it seems clear that homeowners' preferences in the tax laws are worth considerably less to current homeowners than their current tax savings.

Even if the homeowners' preferences in the personal income tax code were fully capitalized, the progressivity of the income tax allows homeowners a small possible tax advantage. Once again we shall use tax-exempt State and local bonds for illustrative purposes. As we saw, with a proportional income tax the after-tax yield would be the same for both tax-exempt and non-tax-exempt bonds. The progressivity of the personal income tax makes it possible for rich taxpayers to benefit from the tax exemption of State and local bonds. Supply and demand for tax-exempt bonds equalize the after-tax return on these bonds and equally risky corporate bonds. This equality is achieved for individuals with a marginal tax rate, say X percent, that is below the maximum marginal rate. Just as in the proportional tax case, individuals in the X percent bracket are indifferent as to whether they hold tax-exempt or taxable bonds. When there is a progressive tax, individuals, who are in a bracket greater than X percent will then get a higher rate of return holding tax-exempt rather than taxable bonds; this is the tax advantage. Similarly, if homeowners buy property where most of the other people have a lower marginal rate, they can benefit. If, as we observe, people of similar incomes live together, then the subsidy disappears.

With these caveats the original conclusion remains—with perfect capital markets the tax advantage to current homeowners is less than the conventional wisdom would argue.

Market Imperfections

In the long run, if capital markets are imperfect and assets have not been properly capitalized, there might continue to be a differential between owner-occupied and rental housing; we would expect these differentials to exist for the poor and to be magnified for minority groups subject to discrimination. Even at a given level of permanent income, it will be more difficult for the poor to borrow since they lack the necessary liquid assets for a downpayment. Poor people may also be higher risks and usury law restrictions may make it difficult for them to borrow; in periods of credit rationing they are most likely to be frozen out of the market. Efficiency could be increased by government intervention to improve the functioning of capital markets for the poor. This is not an argument for a subsidy; in fact, because of the risk premium, higher rates may be necessary. Additionally, if the imperfections of the market are due to racial discrimination, and these cannot be removed, then a second-best subsidy may be called for.

Since there are a large number of landlords and tenants and unlimited entry, the observed price appears to be a competitive equilibrium price. While this is true in the long run, in the short run the landlord may possess some monopoly power. The costs of moving for a tenant are likely to be higher than those for a landlord of attracting new tenants. This makes it more likely that rents will rise in a tight market than that they will fall in a loose one. Thus, these quasi-rents of market adjustment are likely to accrue to the landlord. Some form of regulation or moving subsidy for tenants would make them less vulnerable to these effects.

Labor unions are quite powerful in the construction industry and are made even more powerful by the provisions of the Davis-Bacon Act. As with the other distortions, if this monopoly power cannot be removed, then a second-best solution may require some other form of government intervention.

Macroeconomic Stability and the Housing Industry

We now turn from the microeconomic analysis of the efficiency and equity aspects of housing policy to an examination of the relationship between housing policy and the problems of economic stability.

The production of housing is strongly influenced by monetary policy. As with other forms of investment, it is a function of the cost of capital and hence of the interest rate. Additionally, in cases where tight money leads to credit rationing (because of usury laws or some other controls), housing has traditionally been the last to be served. Because it is so dependent on monetary policy, the housing industry is a strong countercyclical element in the economy—it functions almost as a built-in stabilizer. It is ideally suited to this role, since there is a very high degree of mobility of resources into and out of this industry. The strong countercyclic tendencies of the housing industry have been known for a long time [7], and we would expect that factors of production receive the higher rates of return necessary to compensate them for the added uncertainty. After all, an old stabilizer is a good stabilizer.

Largely as a result of government policy, there is a great deal of uncertainty and higher costs in the homebuilding industry. While the benefits of a stable economy accrue to all citizens, the costs of the increased stability are borne by the housing sector. Equity considerations would then require a subsidy to housing.

Summary

The following list attempts to summarize the economic arguments we have examined for government intervention in the housing sector.

1. To internalize neighborhood effects. No subsidy is in general called for, but government action can serve as a catalyst in overcoming organizational and strategic problems. We may also wish to subsidize local ownership of property.

2. Interdependent utilities may call for government intervention because of strategic problems and organizational costs.

3. Government intervention may be required to accommodate the interests of unborn generations.

4. Declining average costs in housing constitute a classic argument for intervention, if they can be shown to exist.

5. Government may have to give income or property rights to the poor to produce an equitable distribution of efficiency gains from internalizing the economies of housing maintenance and improvements.

6. Housing policies may be a useful second-best vehicle for income distribution.

7. Since government policies affect the allocation of total savings among various sec-

tors, it is important that housing's interests be represented in the decisionmaking process.

8. Obsolete zoning laws, and union and other monopolistic practices may raise costs. Unless they are removed, there is an argument for a subsidy.

9. Government intervention may be necessary to protect tenants from shortrun redistributions of income during periods of excess demand.

10. Imperfect capital markets and lack of information about risks on both sides of the market argue for government mortgage and insurance policies for poor people. When combined with racial discrimination, it may call for a subsidy.

11. Stabilization policy may require that the housing industry be subject to a great deal of uncertainty and instability, thus making for higher costs. These costs should be borne by the public at large.

Whether, given other societal needs, these arguments are persuasive, must be left for others to decide. I would merely like to add one caveat—bad market solutions do not necessarily imply good governmental solutions. As the second-best section made clear, many of the problems with the housing sector derive from attempts to solve the housing and other social problems.

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A Rationale for Government Intervention in Housing: The External Benefit of Good Housing, Particularly with Respect to Neighborhood Property Values

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Summary

One justification for subsidizing good quality housing, such as public housing, is that the improved quality would increase the welfare of neighbors in surrounding houses by reducing fire and health hazards. Surveys of studies that test for the existence of such externalities by determining the impact of good housing on the property values of surrounding houses shows that no such externalities are observable. The reason may be that building code regulations have improved the quality of even slum housing beyond that level at which additional improvements in quality generates external benefits. Any building code regulation increasing housing cost may cause house rents to rise above what poor families can pay, thus requiring subsidies.

Introduction: Externalities

One reason for government to interfere with markets is that externalities exist. In the housing market, such an externality might be that the quality of housing occupied by one person causes benefits or costs to surrounding households. In the early colonial towns, for example, fires were a chronic hazard. Eventually laws were established in cities to insure that all buildings would be more fireproof to keep down the fire hazard. In St. Louis, all houses were built of brick. If housing below a certain standard quality created social costs to surrounding households, such as increased fire hazards, health problems, and increased death rates, then it would pay for the government to improve housing to a quality that would reduce the social costs by as much as it would cost to improve the quality of housing.

Housing reformers have claimed that "decent housing instead of slums means less crime, less juvenile delinquency, lower costs for police and fire protection; it also means better health, lower death rates, and lower costs of medical care."[1] The research that these statements were based upon was not strong. Most studies asserted that better housing would obviously improve a child's health and education. Studies were made showing the correlation between infant mortality, crimes, incidence of tuberculosis, incidence of venereal disease, and substandard housing.[2] Edith Wood argued that poor housing was not the only cause of these social problems, but that the problems could be solved by improved housing.[3] The evidence was the before-and-after studies in England, Scotland, and the Netherlands, of families removed from slums and placed in good housing.

The evidence, however, nowhere makes adequate comparision of the measures of crime, mortality, and incidence of tuberculosis for families before and after the new housing with those remaining in slum housing. There are statements by teachers that schoolchildren who move to better housing look, act, and perform more intelligently than before the change. Knowing the difficulty of measurement, one wonders how much of the improvement was in looks. The people moved into the better housing were closely supervised by inspectors. If the family did not maintain better housing they were told what to do. If improvement was impossible, they were removed from better housing. Furthermore, as John Dean has shown, they did not account for the selection of families by the public housing authorities.[4]

In an earlier study called for by President Herbert Hoover, more care was taken in attributing a reduction in crime to better housing. The experts argued that housing was only one of a

[1] Dillon S. Myer, Commissioner of the Federal Public Housing Authority at the Hearings before the Committee on Banking and Currency, United States Senate, 80th Congress, on S866 (Washington, D.C., Government Printing Office, 1947), p. 118, quoted in John P. Dean, "The Myths of Housing Reform," *American Sociological Review* (April 1949), p. 283.

[2] Edith Elmer Wood, *Slums and Blighted Areas in the United States*, U.S. Federal Emergency Administration of Public Works, Housing Division, bulletin no. 1 (Washington, D.C.: U.S. Government Printing Office, 1935).

[3] Ibid., p. 111–121.

[4] Dean, loc. cit.

complex of social forces causing crime, and that these would also have to be modified before crime could be expected to be reduced. The study's assertions on health were based on expert opinion with no empirical evidence.[5]

Only the recent case study in Baltimore by Wilner, Walkley, Pinkerton, and Taybeck carefully determines the environmental impact of better housing with appropriate controls.[6] Groups of poor families from slum areas, some of whom stayed in slum housing and some of whom moved into public housing, were compared for differing rates of morbidity. Better housing improved the health and school peformance of children because they had fewer accidents and days of illness. The differences were not found among persons over 35 years of age. A weakness of the study, however, is that no statistical test of significance was used to determine how different the test and control sample means really were.

Neverthless, these studies refer to the benefits of good housing received by the occupants. The externalities to other households are obviously part of the benefits. Although it is not mentioned explicitly, the arguments by the reformers were about the whole environment. Not just one family's house, but all houses in the neighborhood must be improved to reap the benefits attributable to good quality housing. An additional benefit to people living elsewhere in the same city was that city costs to control fires, crime, and health hazards would be reduced. Studies showed that slum areas were a net economic drain on cities, that expenditures were greater than revenues from such districts. It was thought that improved housing would not eliminate all these costs, but would reduce the incidence of social costs to the city average.[7] John Dean, however, points out the faults made in calculating costs in these studies. Police protection costs, for example, were allocated to the areas where criminals lived rather than to the areas where the crimes occurred. Educational costs were doubled for slum areas because a greater percentage of children in slums went to public schools![8]

Direct reference to the impact of good housing on surrounding houses and occupants is hard to find. In the foreword to the Hoover study, Ray Wilbur states, "The right of each individual to do as he thinks proper with his own property, often leads to the lowering of property values in an entire neighborhood, because of a single dilapidated and run-down house."[9] No evidence for the statement is cited. In the same volume, under the benefits of improved housing, we find the statement, "A well-kept modern home in the community tends to influence neighbors to recondition and modernize their homes, when necessary, and thereby assists in upholding community standards."[10] Still there is no evidence cited. In 1948, Senator Mike Monroney argued, "One of the principal arguments, with which I go along, is that the establishment of a modern housing project in a city raises the assessed valuation for blocks around it and puts back onto the municipal tax rolls a great deal more money than is taken off by the land that is occupied by these public-housing projects. That has been one of the principal arguments that I have heard through the years from public-housing agencies."[11] There seems to be a well-known argument, but no evidence up to 1962. The recent work in the field will be discussed in the next section.

Since appraisers are most interested in whatever might influence property values, it would be useful to see how the appraisal literature views the impact of good housing on surrounding families. Richard Hurd, a mortgage lender, argued that a new building placed on a vacant site would enhance the value of surrounding buildings if it was appropriate for the site, and if it was equal or superior in construction, arrangement, and appearance to neighboring buildings. If it was inferior, values of neighboring buildings would be depressed.[12] He also stated that cheap, old, and dilapidated buildings constituted a nuisance for any residential district. One more principle is important. Hurd makes the point that a small cheap house in the midst of larger expensive houses will be enhanced in value, while a large and better house in the midst of cheaper smaller houses will be

[5] President's Conference on Home Building and Home Ownership, *Housing and the Community—Home Repair and Remodeling* (Washington, D.C.: National Capital Press, Inc., 1932), especially pp. 1-222.

[6] Daniel M. Wilner, Rosabelle Price Walkley, Thomas C. Pinkerton, and Matthew Taybeck, *The Housing Environment and Family Life* (Baltimore: The Johns Hopkins Press, 1962).

[7] Wood, op. cit., pp. 20-21.

[8] Dean, op. cit., pp. 285-286.

[9] President's Conference on Home Building and Home Ownership, op. cit., p. vii.

[10] Ibid., p. 226.

[11] House Banking and Currency Committee, *Hearings, General Housing*, 1948, p. 247, cited in Robert Moore Fisher, *Twenty Years of Public Housing* (New York: Harper and Brothers Publishers, 1959), p. 195.

[12] Richard M. Hurd, *Principles of City Land Values* (New York: The Record and Guide, 1924), p. 111.

depressed in value. Neighborhood house values tend to be depressed or enhanced to the level of the dominant housing in the neighborhood.[13]

The same discussions may be found in modern valuation literature.[14] In all of the appraisal literature, however, the physical structure has less to do with value than the social characteristics of families in the neighborhood. Hurd says, "On the other hand, the basis of residence values is social and not economic—even though the land goes to the highest bidder—the rich selecting the locations which please them, those of moderate means living as near by as possible, and so on down the scale of wealth, the poorest workingman taking the final leavings, either adjacent to such nuisances as factories, railroads, docks, etc., or far out of the city." [15] More recently, in *The Appraisal of Real Estate,* we find, "The value levels in a residential neighborhood will be influenced more by social characteristics of the people occupying or in prospect of occupying the area than by any other factor." [16] Thus, a poor quality house in a neighborhood would be enhanced in value if it was surrounded by better housing occupied by families with good income. On the other hand, if a newly dilapidated house is taken as the first signal that the social class of the neighborhood is changing, values throughout the neiyhborhood, as mentioned above by Wilbur, would decline.

Only one of the above studies was a good test of the benefits from good quality housing, and it referred to the benefits to both the occupants and to those in surrounding housing units. The slight benefits found indicate that it would be unlikely for surrounding neighborhood households to benefit much from improvement of one household's housing quality. In the next section we will survey the empirical work testing whether improving the physical quality of a house will affect surrounding property values.

Previous Empirical Studies

Three studies have tested whether there were social benefits or costs to neighboring families by comparing whether there was any effect on neighoring property values.[17] Changes in site values express the changes in the relative value of one neighborhood environment over others. Site value itself is difficult to measure, but changes in property value can be used as a measure of these changes so long as care is taken with respect to changes in improvements occurring on each site. The technique requires comparing the changes in property values in blocks surrounding a given project, such as public housing, with changes in property values in other neighborhoods that were of comparable quality and accessibility prior to the introduction of public housing.

Changes in improvements, other than depreciation, may increase the property value without any change in the land values. Other major influences on property prices, except for changes in land values, would be depreciation and inflation. Inflation can be taken into account by deflating by a building cost index. Depreciation on the improvements, however, would tend to make increases in market prices less than increases in land values, or would tend to make decreases in market prices greater than decreases in land values. Although changes in land values in one neighborhood may be underestimated, a comparison between two neighborhoods of change in property prices does not distort the comparision of the underlying change in land values if we assume that depreciation affects the improvements in both neighborhoods equally.

Two additional problems should be considered. The first is that the property price may decline greatly from one sale to the next because of economic obsolescence while the land values have increased. In fact, the increased land values may cause buildings to become uneconomic if they do not furnish enough return to cover the rent of the land. A particular example of the above problem would be the sale of a tenement whose best use would be a parking lot. The buyer will have to tear down the building. In this case the building has no value or even negative value. The second problem is that the slum properties are quite often small plots. They are too

[13] Ibid., pp. 103-104, 117-118.

[14] Richard U. Ratcliff, *Modern Real Estate Valuation* (Madison, Wisconsin: Democrat Press, 1965), pp. 151-152. American Institute of Real Estate Appraisers, *The Appraisal of Real Estate,* 4th (Chicago: American Institute of Real Estate Appraisers, 1964), p. 27.

[15] Hurd, op. cit., pp. 77-78.

[16] American Institute of Real Estate Appraisers, op. cit., p. 93.

[17] Hugh O. Nourse, "The Effect of Public Housing on Property Values in St. Louis," *Land Economics* (Nov. 1963), reprinted as Chapter 2 in Hugh Nourse, *The Effect of Public Policy on Housing Markets,* (Lexington: D. C. Heath and Company, 19, 3).
Salvatore V. Ferrera, "The Effect of Urban Renewal and Public Housing on Neighboring Property Values and Rents in Chicago," unpublished Ph.D. Dissertation, Department of Economics, The University of Chicago, 1969.
Robert Schafer, "The Effect of BMIR Housing on Property Values," *Land Economics* (Aug. 1972), pp. 282-286.

small for industrial or commercial use, and if a speculator bought up several contiguous parcels and tore down the buildings, he might enhance the value of the land. Thus, part of the increase in value represents return on his investment and is not due to any public improvements such as public housing. These problems would be important for these studies only if they influenced one area more than its comparative area.

The first study, by Nourse, compared the trends in prices of property located in a ring two to three blocks wide surrounding three public housing project areas in St. Louis with three control neighborhoods for the period 1937–1959.[18] The three public housing areas included eight housing projects. The time span began before public housing was constructed and ended after the last project in the study had been completed. Prices of property that sold at least twice were linked in a special regression index.[19] The great advantage of the index is that it controls for differences in type of housing sold in any given year. A statistical test of significance was used to compare whether the price indices in each public housing and control area were significantly different. It was found that there was no significant difference in the indices with the exception of one comparison in 1 year. In this and other studies described, statistical significance will be determined at the .05 level of significance. Even with no difference in indices, chance could cause a significant difference in 1 out of 22 years.

Two factors may have accounted for different price trends or in comparable price trends when, in fact, they were different: More improvements may have been made to buildings between sales in one neighborhood than in another; or some other influence may have been operating in one area that was not in the comparative area. In particular, as pointed out previously, one area may have been changing in the proportion of land devoted to a new use. A comparison of building-permit information revealed no significant difference between control and public housing neighborhoods in the value of additional improvements to buildings during the period studied. There was a significant change in land use to trucking terminals in one area, but it kept public housing neighborhgod values slightly —but not significantly—higher than in the comparable control area. The difference in price, as we noted, was not significant.

The second study, by Salvatore Ferrera, compared the trends in contract rents of tenants in housing units in two rings around public housing projects and urban renewal areas in Chicago.[20] The test areas were Hyde Park-Kenwood and Lake Meadows-Prairie Shores. Ferrera regressed relative changes in average contract rent per census block from 1950 to 1960, and from 1940 to 1960, against several explanatory variables, such as percent substandard, percent crowded, percent occupied by nonwhite households, and vacancy rates. Included in the independent variables was a dummy variable indicating whether the block was in the first or second ring around a public housing project. This variable was only used in the Lake Meadows-Prairie Shores test area, since public housing was not located in Hyde Park-Kenwood. He found that the relative change in rents in the first ring around public housing units was significantly different from general changes in the neighborhood from 1950 to 1960. He did not find any significant impact in the second ring, however, nor did he find a significant impact for the period 1940 to 1960. Although Ferrera contended that this was a significant result, the results for the longer period cast doubt on his conclusions. It may merely reflect the time period chosen. Unlike the other studies, Ferrera's could not use annual data for comparisons of long trends. The weakness of his study is that it utilizes data only for 3 census years.

Furthermore, Ferrera concluded that this rise in rents resulted from the demand for property for commercial uses and from the desire by families to put their children in the schools in the public housing area. The public housing projects increased the number of families in the area relative to the number before public housing. No commercial facilities were included within the projects, so that property in the first ring around the projects became important for commercial use. Particular services available in the projects included new schools, playgrounds, community recreation facilities, social welfare, and health facilities. Significantly, the boundary for the new school in the public housing complex rarely extended more than a block or two outside of public housing. Thus, amenities within public housing, particularly the school, attracted families to the first ring. The intensity of demand, however, did not extend beyond the first ring.

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[18] Nourse, ibid.

[19] Martin J. Bailey, Richard F. Muth, and Hugh O. Nourse, "A Regression Method for Real Estate Price Index Construction," *Journal of the American Statistical Association* (Dec. 1963), pp. 993-1010. Reprinted as Chapter 3 in Nourse, *The Effect of Public Policy on Housing Markets.*

[20] Ferrera, Ibid.

At the same time, Ferrera also used a dummy variable for the first and second ring of blocks around urban renewal projects in the Hyde Park-Kenwood and Lake Meadows-Prairie Shores test areas. The same procedure was used. This time, however, he also used the relative change in average property value of single family houses for the Hyde Park-Kenwood area. In the other areas he compared only the relative change in rents. It would be possible that the newer houses and shopping areas would increase property values in surrounding areas. The results were completely negative. There was no significant difference between the change in rents and values immediately adjacent to urban renewal and change in housing rents and values many blocks away. In this case it is possible that the control area is inadequate. The control area is the whole neighborhood, so that if the impact covered the entire neighborhood, Ferrera's test would not catch the differential impact on values and rents. His test only catches the effect if it has a declining impact with distance from the urban renewal project.

The third study, by Schafer, compared the trends in value of houses around a Below Market Interest Rate Project (221(d)(3) or 236) with trends in a comparable test area.[21] Both the control and test area were in the San Fernando Valley within Los Angeles, and mainly included white middle income families. The housing project consisted of 132 units built prior to 1965. A price index, the same as that used by Nourse, for the period 1958 to 1970, was constructed for both the control and test areas. Two tests of significance were used. Shafer tested the differences between indices in the test and control areas and found no significant difference from zero. He also used the Chow test, which revealed no significant difference in the regression indices from that constructed from pooling the data in the two areas. In his study, Schafer makes the excellent point that the occupants of the project were of the same socioeconomic class as those within the test and control neighborhoods. Thus he avoided the impact of change that might have resulted if a different socioeconomic class of people from those occupying housing in the surrounding neighborhood occupied the project. Surely, it is best to test the impact of the housing environment by controlling for the socioeconomic class of occupants, as was done.

It is in fact true that no socioeconomic change in neighborhoods resulted from the construction of any of the projects tested in the above three studies. The projects were placed in neighborhoods in which the class of the occupants was the same as in the surrounding neighborhood. In more recent work by Nourse it was found that changing income class had far more impact on prices of houses in a neighborhood than aging of housing structures.[22] Comparisons were made in the income and price trends of several neighborhoods and communities with different ages of development in St. Louis. Income trends were estimated by determining the occupations of a sample of heads of households in the West End, Wellston, University City, Normandy, and Webster Groves from 1930 to 1970. Median income ranks were estimated by determining the decile in the income distribution that each occupation held. The ranks went from 1 for the lowest decile to 10 for the highest. Price and rent data were taken from the decennial census of 1940, 1950, 1960, and 1970. Webster Groves was developed prior to University City, but was not adjacent to other areas of declining income as was University City. In 1950, prices and rents were higher in University City than in Webster Groves. By 1970, however, income ranks in University City had begun to drop, while in Webster Groves they remained the same and even increased. The income rank of occupations in both areas had been 9 (includes such occupations as artists, draftsmen, pharmacists, insurance agents, electricians, foremen, linemen, and printing craftsmen) prior to 1965. After that, those of University City fell to 6 (which includes welfare workers, salesmen, bricklayers, foremen, and managers of eating and drinking places), while those in Webster Groves rose to 10 (college professors, authors, engineers, managers, professionals, and locomotive engineers). The pattern was similar for prices and rents. Relative prices and rents in Webster declined from 1950 to 1970, as one would expect from older housing, but those of University City fell far more. By 1970, prices and rents were higher in Webster Groves than in University City. Although relative prices fell, absolute prices rose in both places.

Further Comments on the Empirical Evidence

Thus, one is inclined to cite the last test as evidence that income of households is more important than age of structure in determining

[21] Schafer, Ibid.

[22] Nourse, *The Effect of Public Policy on Housing Markets*, Chapter 10, "The Effect of Aging and Income Transition on Neighborhood House Values."

prices and rents. It would be interesting to run a test on the property values surrounding a project which did change the socioeconomic character of a neighborhood. Only the study of Hyde Park-Kenwood by Ferrera may have included such a change. The dominance of students and faculty in the area even before Urban Renewal may have resulted in no change in the socioeconomic class even in this case.

All of these tests were cases of particular projects in a specific place. The weakness of the tests is precisely that they are only small case studies. There is no proof that, in other places, different results might not have been obtained. Nonetheless, they are three different areas scattered about the United States, and they are consistent with the careful study of the direct impact of the quality of housing on morbidity conducted in Baltimore.

The above studies indicate that improvement in housing is unlikely to have an impact on neighborhood property values unless other market changes are present. There is evidence that changes in the socioeconomic character of a neighborhood would affect values more, although this has not been tested directly for public housing or BMIR projects. The evidence certainly does not support any contention that the subsidies provided in the cases of the above projects were justified by external benefits, or reductions of social costs to households in the surrounding neighborhood. Ex'ernal benefits, as measured by changes in property values, were not found.

Building Codes: An Alternative Control on External Social Costs

The reason why external effects of good housing may not show in statistical testing is that building codes have already eliminated the hazards to health and property that would significantly affect neighbors. Government subsidies to improve housing provide improvements to the occupant rather than to his neighbors. The impact of building codes on neighborhood property values has never been tested, although several papers have explored the theory.[23]

From the point of view of the economist, the ideal building code standard is one that improves the quality of housing to that quality at which the additional costs of quality improvement are exactly equal to the additional gains in benefits to the neighborhood or community. The theory is identical to that justifying air pollution control, and in fact has the same problems in determining the appropriate standard. There is evidence, however, that the standards may be too high. During the 1940's and 1950's, for example, when there was a serious housing shortage, building codes were not enforced, but we did not observe massive fires burning down whole neighborhoods, nor did we observe the kind of epidemics that are created by unhealthful surroundings. Yes, slum housing probably did lead to illness, but it was the kind demonstrated in the Wilner study of Baltimore that we have earlier reported.

In a recent study of urban decay in St. Louis, it was found that rents on apartments declined at the boundary of the ghetto with adjacent neighborhoods.[24] This might be construed as evidence that substandard housing does indeed have a negative impact on surrounding neighbors, except that it is difficult to differentiate between the impact of socioeconomic class and the physical quality of housing. There was no analysis of whether the building code was enforced within the ghetto or in the areas immediately adjacent, but it was found that prices declined as vacancies rose in the border areas. The implications drawn from the facts, however, were that these results were caused by families not wanting to live in an environment with a different race and socioeconomic class, rather than with the building code violations, should they have existed. In fact, the changes in the ghetto boundary were accompanied by drastic changes in socioeconomic class from the 9th to 4th decile rank, as described in our previous discussion of income ranks.

Furthermore, the detailed conflicts over minutiae about whether plumbing can use plastic pipe, or whether 2x3 studs can be used in non-load-bearing interior partitions, or whether preassembled plumbing cores can be used, describe labor disputes more than they do a discussion as to whether a particular feature will increase fire hazards, damage health, or cause walls to fall down on neighbors.[25] The discussion itself

[23] A. H. Schaaf, *Economic Aspects of Urban Renewal. Theory Policy and Area Analysis,* Real Estate Research Program, Institute of Business and Economic Research Report 14 (University of California, 1960). Nourse, "The Economics of Urban Renewal," *Land Economics* (February 1966), reprinted in *The Effect of Public Policy on Housing Markets* as Chapter 6. In the same volume see Chapter 11, "Economic Analysis of Standard Quality Housing." L. Charles Miller, Jr., "The Economics of Housing Code Enforcement," *Land Economics* (Feb. 1973), pp. 92-96.

[24] Institute for Urban and Regional Studies, "Urban Decay in St. Louis," Washington University (Mar. 1972).

[25] Allen D. Manvel, *Local Land and Building Regulation,* Research Report No. 6, The National Commission on Urban Problems, Washington, D. C., 1968, pp. 11-19.

would appear to be evidence that the codes in use are more detailed than they need to be in order to prevent external social costs.

Side Effects from Building Codes

Any code requirements that increase building costs, whether they reduce social costs or not, are going to have an impact on rents or prices that families pay for housing. Owners will comply with the building codes so long as the increase in costs incurred will generate future revenues sufficient to justify the expenditure at current interest rates. If the rents are not expected to rise sufficiently, the building would be abandoned.

We need to outline a market model that would show the impact of the code on prices, occupancy, and abandonment.[26] The housing market can be divided into two submarkets. One includes those families who can afford to buy new housing; the other includes those families whose incomes are so low that they cannot afford new housing. The two groups of families also tend to live in homogeneous neighborhoods. Houses for higher income families who can afford new homes will be valued at a discount if they are located adjacent to, or in the path of, change to neighborhoods occupied by low income families. On the other hand, low income families would be willing to pay a premium for housing adjacent to higher income family neighborhoods because of the possibility of better public services—schools, parks, etc. The only way for low income families to expand the housing available to them is through bidding housing away from other groups who can afford new housing. With the increase in the number of poor families in a city through natural increase and through migration, crowding would occur, prices for poor families would rise, and housing would be transferred from use by higher income families to use by lower income families.

The introduction of a building code that increases the cost of construction and requires older houses to be upgraded will cause the following impact on the market. By increasing the cost of building, it increases the number of families in the low income group who cannot afford new housing. By increasing the cost of maintaining older housing, it increases prices and rent of older housing. If incomes are so low that families cannot afford the higher rents required to support code enforcement, families will have to live in more crowded quarters, some owners will abandon structures, or the code will not be enforced. Our analysis assumes a static population. If the low income population is expanding rapidly, and little new housing is being constructed, housing would be in short supply.

In such a situation, one similar to the 1940's and 1950's, codes would not be enforced. In today's market, however, migration to large metropolitan areas has declined, and there has been a rapid expansion of new housing. Enforcement of the code is possible without creating a worse housing shortage. As a result, we are observing the increasing number of abandonments in central cities and suburbs. Low income families cannot afford the rents required to maintain houses at code levels. It does not help, of course, that vandalism increases the cost of maintaining standards. Nevertheless, one can question whether such vandalism would occur if housing were indeed in short supply. As housing is destroyed or abandoned, and families in the higher income groups flee from housing near, or expected to be near, low income areas, the housing is transferred to use by poor families because the prices in the areas adjacent to low income areas decline to a level that can be afforded by the poor.

The lower price of a capital stock is an evaluation by the market that the income stream coming to that property is declining. In such a situation, one way to reduce costs so that the net return is equivalent to other investments is to reduce maintenance. The quality deteriorates to that level supportable by rents from tenants or by incomes of homeowners. If this is not equivalent to the building code standard, the investment may be abandoned.

Thus, whether the code is justified or not by external social costs, and there is some doubt as to whether current standards are so justified, rising building costs will likely increase abandonments and the chewing up of housing resources in metropolitan areas. If such a process is to be stopped, the Government will have to see that building codes are less restrictive, or that poor families are subsidized so that they can live in housing that meets the code standards. The codes are standards that can be enforced only to the extent the public is willing to subsidize poor families so that they can live in the standard desired.

[26] Nourse, Ibid.

Implications for Policy

In this paper I have indicated that external benefits from improving housing quality have not been proven to exist by the evidence from studies on property prices and rents. There is evidence that the socioeconomic class of families in a particular neighborhood is more important than quality of structure in determining neighborhood house values. These results may have been found because the external benefits that affect value have long since been covered through building code enforcement. Only those quality standards that prevent epidemics and fire holocausts may have external benefits for surrounding property. In fact, building codes go far beyond these simple restrictions. Whether they are too restrictive or not, however, they will cause an increase in building costs. These increases in costs may make it impossible for some poor families to live in housing conforming to standards without some form of subsidy. If there is no subsidy, then houses will be continually reduced to standards below code, abandoned, and demolished. It would also cause an acceleration of the movement of income levels of neighborhoods throughout cities.

There is no evidence supporting subsidization of the poor in standard quality housing in order to improve surrounding property values. Furthermore, there is an implication from the work in this paper that some subsidy is required to maintain houses at the code standards apparently wanted by people today. If that subsidy should take the form of a rent subsidy or negative income tax so that families could locate anywhere, rapid acceleration of decline in some neighborhoods may occur. This is a paradoxical implication since we usually imagine that it would scatter poor families throughout the city. If that in fact should happen, then no neighborhood would decline especially. Nevertheless, if some neighborhoods through political power prevent entrance by the poor, only marginal areas will be occupied by the poor, accelerating declines in social class and property values in those neighborhoods and pushing middle income families to newer areas.

The Criteria for Evaluating the Role of Government in Housing Markets

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* The statements expressed in this paper reflect the views of the author. They do not necessarily represent the position of the Federal Home Loan Bank of Cincinnati or the Federal Home Loan Bank Board.

Summary

Economic analyses of housing show housing consumption to be an important element in the family budget. They also show the budget to be an important constraining influence on the housing consumption of families that are large and have low incomes. Housing problems are indicated for reasons that have largely, though not exclusively, to do with the low incomes of some families. But it is impossible to determine exactly which families have what kind of housing problems and how many of them there are on the basis of the findings of positive economic analysis. "Normative" knowledge is required as well as a clear understanding of the meaning of housing consumption.

The criteria for evaluating the role of government in housing can be construed as "norms" against which performance is measured. To the economist, this means a concern with allocative efficiency and equity considerations. Since housing is made available largely through the operation of the market mechanism, the role of government is therefore seen as one of dealing with the problem of market failure. The nature of that problem in terms of allocative efficiency criteria is straightforward and unambiguous. Problems arise when market activity generates "externalities" leading to market outcomes that do not represent the best use of our resources. Government intervention in housing can then be rationalized on the basis of the presence of allocative inefficiency in the market. And the fact that we encounter difficulties in attempting to use these criteria in no way detracts from their importance to policymakers.

But allocative efficiency is not enough. We also want equitable outcomes; we want results that satisfy our sense of fairness. Unfortunately, the meaning of fairness cannot be specified as easily as that of efficiency. In housing, it comes to focus on the issue of minimum housing standards. While no one disputes the goal of everyone's living in a decent home and suitable living environment, its meaning in terms of the distribution of housing consumption among households is by no means clear.

Current research concerned with delineating the elements of housing consumption will help in the sense of clarifying the meaning of housing standards in general. But there remains the issue of what constitutes a minimum standard. Undoubtedly more could be said about fairness in housing consumption if we were to integrate better what we know from the various disciplines about the impact of housing consumption on the welfare of the family. But there would still remain questions of ethics that must be addressed.

Were we willing to disregard the question of equity, the rationalization of housing policy would be a relatively simple matter. But equity considerations cannot be ignored. And to deal with them effectively will require the output of research that clarifies precisely what is involved in the concept of housing standards and how this links up to what is determined as the ethical criteria appropriately applied to the consideration of minimum standards.

The Elements of Housing Consumption

The notion of housing consumption warrants discussion at the outset. Housing is a durable asset that provides a wide range of services to those who use it—the occupants—over an extended period of time. Housing can thus be considered as both a stock and a flow of services. But if the concern is with housing consumption, it is the flow of services that is important.

The services provided by the dwelling flow from the physical facility itself, the site upon which that facility is situated, and the neighborhood in which the site is located. The physical structure is composed of a number of elements, each of which provides a service to its occupant. These elements include sheltered living space or space for sleeping, food preparation, storage, and the like. They also include such things as water, solid waste, and heating and ventilating systems. The site of this structure encompasses the dimensions of size, terrain, and location. The land space that makes up the site is used, of course, to house the physical structure. That space that is exterior to the dwelling also can serve work and recreational purposes. How well it serves in this latter capacity depends on its size and certain topographical features such as slope and foliage. The site also provides "locational services" to its occupant, not the least of which is access to the place of work of the family head. The housing services that flow from the neighborhood in which the site is located include those provided by its sewerage systems, water systems, refuse removal services, parking space, traffic safety, streets and roads, public transportation, and education services.[1]

While admittedly an abbreviated description of the package of housing services consumed, it does serve to make clear an important property of that package: it consists of a large number of elements that vary considerably in terms of the particular need they serve. People do many things during the course of a day and different people do different things. Housing enters into these activities in that it assists people in what they are doing, and it does so in many different ways. Housing is thus a very complex bundle of services consumed by people who vary considerably in their requirements for the services a dwelling supplies. This fact alone stands as an explanation of why we have so much difficulty in even talking about the meaning of housing consumption, let alone providing useful measures of it.

What does it mean to say that there are differences in the level of housing consumption? When talking about such differences one can focus on the differences in housing expenditures —rents paid by renter-occupiers and the capital and operating costs of homeowners. For some purposes, the focus on housing expenditures may be appropriate.[2] But as will be made evident subsequently, when our concern is with the question of how much consumption is enough, it would help considerably to have measures of output.

To my knowledge, no satisfactory measures of housing output are currently available. Yet, recent research, stimulated in part by the requirements of simulation models concerned with the city, has addressed in a serious way the question of the meaning of housing output.[3] And from this research have come regression equations that suggest that the elements of consumption alluded to above do show up to be correlated in the appropriate ways with various measures of housing expenditure and/or the capital value of the assets. While these studies can only be considered as providing us with tentative conclusions, they nevertheless do suggest that expenditure measures can be taken as rough indexes of quantity consumed. Granted this, earlier studies of the impact of budget elements on housing expenditures and/or value of housing assets purchased should be revealing of how the budget of the family influences its housing consumption. And this is subject matter that should stand as a first order of business in studies of the rationale of our public policies with respect to the housing of low income families.

The Influence of the Budget on Housing Consumption

Economic theory, of course, provides a basis for believing that family income and prices have important bearing on consumer choice, including the one concerned with housing. Taken together, they are considered as the budget constraint. How they operate to constrain consumption has occupied much time and attention of economists, a good deal of which has come to focus on attempts to estimate demand functions for various commodities and income and price elasticities of those demands.

The question of how important the constraining influence of income and price are with respect to housing expenditures is one that, at first glance, seems easy: they are very important. As a component of the family budget, housing expenditures show up as being the most important element in that budget, accounting on the average for about 15 percent of the house-

[1] For other discussions of what is or should be incorporated in that bundle of services, see American Public Health Association, *An Appraisal for Measuring the Quality of Housing* and the National Swedish Institute for Building Research, *The Quality of Dwellings and Housing Areas*, Stockholm, 1967.

[2] What we need generally depends on the purposes of the investigation. Yet, Olsen argues that for an important range of economic questions concerned with housing, we can do much by simply introducing a theoretical entity called a housing service—an entity assumed to be homogeneous. Links to the real world can be established by deductive implications from the model. See E. O. Olsen, "A Competitive Theory of the Housing Market," *American Economic Review*, Sept. 1969, pp. 612–622.

[3] See, for example, R. B. Struyk, "Estimating the Value of Housing Services with the Census Users Sample: Comparative Results for Five Areas," UI 208–10 (Washington, D.C.: The Urban Institute, June 1972) and J. Kain and J. M. Quigley, "Measuring the Value of Housing Quality," *Journal of the American Statistical Association*, June 1970, pp. 532–548.

hold's income.[4] Yet the fact that housing expenditures are such a large element in the family budget, by itself, is not that revealing of the way in which this spending is influenced by income and costs. For the fact that families spend a sizable amount of their income on housing could be just as easily explained by sets of tastes and preferences that make them inclined to spend relatively more on housing.

More insight can be gained about the importance of the budget constraint with some knowledge of the household's consumption response to changes in income and price—that is, a knowledge of the income and price elasticities of demand. For if the household is indeed restrained by the budget, it will respond sharply to changes in that budget.

Research concerned with estimating income and price elasticities of housing demand,[5] while lacking in conclusiveness, does provide notions about orders of magnitude. One view of the current state of knowledge (deLeeuw) suggests that the income elasticity of demand to be around unity.[6] His review indicates an overall income elasticity of rental housing demand to be in the range of 0.8 to 1.0 and that for owner-occupied demand to be slightly higher. The various recent estimates of housing price elasticities also suggest a coefficient that is in the neighborhood of 1.0 with an upper limit in the vicinity of 1.5.[7]

Elasticity coefficients of this sort provide the warrant for asserting that households do adjust their housing consumption in a predictable way to income and price changes. Yet, that response must be characterized as "average." It is difficult to see how one could argue that households are severely constrained by the budget in their housing decisions, with elasticities that are in the neighborhood of unity.

It is not at all clear, however, that these coefficients are applicable to all households. For they are a reflection of an averaging process, and there are indications of a considerable amount of variation in the housing behavior of households. In fact deLeeuw reports the results of some elasticity calculations that show marked differences in the income coefficient by size of family—the larger the family, the larger the elasticity coefficient.[8] There are in addition tabulations of census and other data that indicate families with low incomes spend relatively more of their incomes on housing.[9]

Although there are still statistical and theoretical problems that plague efforts to estimate these elasticities, problems that limit the extent of their usefulness in policy discussions, the research to date has shown consistency in findings with respect to certain orders of magnitude. And one area of consistency concerns the housing consumption of relatively large households with low incomes. There is thus in the economic literature some scientific warrant for asserting the not very surprising result that relatively large low income families are severely constrained in their housing consumption by their incomes and the price tags that attach to the bundle of housing services they consume.

Other Influences on Housing Consumption

Tastes and Preferences: While elasticity coefficients indicate incomes of families have bearing on housing consumption as to the price tags attached to the bundles of services consumed, research involving cross-section data indicates a degree of variation in that consumption that can by no means be explained by income and price differences. Maisel and Winnick characterized housing expenditures some time ago as being subject to intrusive variances and talked of the elusive laws of housing consumption.[10] How can we explain these variances?

While it does not really constitute an economic explanation, much of what is involved can be subsumed under the heading of tastes and preferences. In economics, the utility functions of households are considered as having important bearing on consumption in general and individual items of consumption, e.g., housing, in particular. Having said this, however, it is not quite clear just how much has been added to the discussion. For there is little in economics that provides a basis for explaining why some things

[4] See Tempo, "United States Housing Needs, 1968–1978," in the *Report of the President's Committee on Urban Housing,* Volume I, (Washington, 1968), p. 14.

[5] While the list of contributors to this literature is relatively long, mention should be made of M. Reid, *Housing and Income,* (Chicago: University of Chicago, 1962); R. Muth, "The Demand for Nonfarm Housing," in Harberger (ed.) *The Demand for Durable Goods,* (Chicago: University of Chicago Press), pp. 29–96; Tong Hun Lee, "Housing and Permanent Income: Tests Based on a Three Year Reinterview Survey," *Review of Economics and Statistics,* Nov. 1968, pp. 480–490.

[6] F. deLeeuw, "The Demand for Housing: A Review of Cross Section Evidence," *Review of Economics and Statistics,* Feb. 1971, pp. 1–10.

[7] Tong Hun Lee, "The Stock Demand Elasticities of Nonfarm Housing," *Review of Economics and Statistics,* Feb. 1964, pp. 82–89.

[8] F. deLeeuw, op. cit., pp. 8–9.

[9] Tempo, op. cit., pp. 14–15.

[10] S. Maisel and L. Winnick, "Family Housing Expenditures: Elusive Laws and Intrusive Variances," in I. Friend and R. Jones (eds.) *Consumption and Savings,* (Philadelphia: Wharton School of Finance and Commerce, University of Pennsylvania, 1960), pp. 359–435.

are preferred to others.[11] As matters stand now, the answer to that question must come from other disciplines. Yet, it is evident from cross-section data that some people consume more housing than others for nonbudgetary reasons. To suggest these differences have to do with the structure of preferences of the households involved can simply be taken as a reminder of the nonbudgetary elements that have to be reckoned with in explaining housing consumption, factors about which sociologists and others should have some useful things to say.

Discrimination: Residential segregation by race is a well-documented fact in virtually every American city.[12] The probability that the neighbor of a black family will be black and the neighbor of a white family will be white is quite high. While this could simply be a reflection of the fact that whites prefer to live with other whites and blacks prefer to live with other blacks, there is evidence that suggests it is more a consequence of restrictions placed on the housing alternatives being made available to blacks. For many black families, market forces have not come into play in an impersonalized way. The result is generally believed to be a restriction in the supply of housing units made available to blacks, which in turn has meant blacks pay more than whites for housing of the same quality.

This latter point—that blacks pay a premium for housing—is currently shrouded in controversy. The evidence that they do is clear to some;[13] to others, the differentials can be just as well explained by alternative hypotheses.[14] The fact of segregation, however, combined with an overt expression of residential integration as a goal by significant sections of both the black and white communities does suggest that actions of whites against the blacks do operate to restrict the housing opportunities of blacks. Explanations of the housing of black Americans must thus take into account market discrimination and its effects.

Market Imperfections: Market imperfections, of course refer to aspects of the institutional framework of the market that have the effect of restricting competition among buyers and sellers in a market. Discriminatory practices fall under this heading. But the notion of market imperfections is broader in scope. It not only encompasses activities the purpose of which is a conscious restriction of alternatives to some group of buyers or sellers, it also includes market elements that have the same effect but for which no such intent holds.

The housing market is, of course, not perfectly competitive. While we can conceive of housing as units of a housing service that are homogeneous, what is exchanged is highly differentiated. Such differentiation means that not all units are competitive with one another nor are all households in search of housing accommodations in competition with one another. Owners of 30-room mansions do not really compete for customers with those who own buildings filled with efficiency apartments. Nor do families earning in excess of $100,000 a year compete for dwellings with those who make less than $3,000.

Market segmentation of this sort is a fact that, when combined with the complexity of the dwelling and the inaccessibility of information about certain important aspects of that dwelling, can make the necessary job of comparing units an extraordinarily difficult one. The consumption of any given household can very well reflect these difficulties in that the household may be consuming more or less than what would have been possible if more had been known about the alternatives. That housing alternatives and, by implication, knowledge of the alternatives can have impact on choice has been shown to be of consequence.[15]

Financial Factors: Credit is used extensively in the various housing transactions for a number of reasons, not the least of which is the size of the transaction in relation to the current income of the purchaser. Its importance to the market process through which housing transactions in-

[11] Proxy measures of certain social and demographic factors, e.g., life cycle, show up in cross-section studies as being correlated with expenditures including housing. See A. R. Winger, "An Approach to the Problem of Measuring Upgrading Demand in the Housing Market," *Review of Economics and Statistics*, Aug. 1963, pp. 239–244. Such measures can be construed as reflections of factors that are in some sense a part of the preference structure of the family. But in what sense this is the case is never really made clear, which is to say that there is really little in economics that allows us to make the kinds of statements about tastes and preferences that can be made about income and prices.

[12] See K. E. Taeuber and A. R. Taeuber, *Negroes in Cities*, (Chicago: Aldine Publishing Company, 1965) and R. Zelder, "Racial Segregation in Urban Housing Markets," *Journal of Regional Science*, Apr. 1970, pp. 93–105.

[13] See C. Rapkin, "Price Discrimination Against Negroes in the Rental Housing Market," in *Essays in Urban Land Economics*, (Los Angeles: The University of California Press, 1966) and J. Kain, "Effect of Housing Market Segregation on Urban Development," in *Savings and Residential Financing: 1969 Conference Proceedings*, U.S. Savings and Loan League, pp. 89–110.

[14] M. J. Bailey, "Effects of Race and Other Demographic Factors on the Value of Single Family Homes," *Land Economics*, May, 1966, pp. 215–220 and R. Muth, *Cities and Housing*, (Chicago: University of Chicago Press, 1969).

[15] A. R. Winger, "Housing and Income," *Western Economic Journal*, June 1968, pp. 226–232.

volving both new and used dwellings are consummated is undeniable. The impact it has on monthly housing expenditures is another question.

It is difficult to see much direct connection between financing conditions and the housing demands of renters. The interest cost of debt-financed rental units must, of course, be recouped. But such financial claims are capital costs and as such can be considered in the same way as any other cost of owning and operating such units. For homeowners, on the other hand, the availability of credit, by providing the basis for financial leverage, may have direct bearing on housing consumption. Families with given levels of income can conceivably purchase a larger bundle of housing services by using mortgage credit than by not using it. And many no doubt have done so as mortgage terms became more liberal.[16] In fact the shift into homeownership, which for most results in upgrading, was made possible in quite a number of cases because of the liberalization of mortgage credit terms. But the influence of credit on the amount purchased and hence subsequently consumed is by no means clear.[17] There is no doubt that the timing of homeowner purchases is strongly influenced by credit facts. Whether the family buys more or less because of these credit factors is less certain. What can be said is that the mortgage market apparently works in a way that benefits those with higher incomes for reasons that cannot be construed as irrational.[18] Thus, knowledge of the way in which housing credit markets operate may provide insights into the housing consumption of those with low incomes.

Housing Consumption of Low Income Families

Several things seem to come through from the discussion to this point. One is that while the budget shows up in statistical studies to be a moderately important element in the housing consumption of the average family, there is also evidence that it becomes an increasingly important constraining influence the lower the income of the family. Perhaps because of this, it is not difficult to find arithmetic simulations using income and rent data taken from the U.S. Census Bureau or other sources, the outcomes of which are taken to represent a clear demonstration of the fact that many low income families would be forced to spend too much of their budget on housing if they were to live in standard housing.[19] Nor is it difficult to find estimates of the magnitude of the problem based on analyses in which a central element is a set of maximum housing consumption-income ratios. In these studies, anyone who is found spending a greater proportion of his income than that indicated by the maximum for the group of which it is a part is counted as a household that has a housing problem. One such study commissioned by the President's Committee on Urban Housing concluded that there were 8 million such households in the Nation in 1968.[20]

But there are difficulties with estimating the dimensions of the problem in this way that are clearly manifest in the weakness of the rationale generally given for the choice of a particular figure taken to represent maximum income allotments and/or minimum housing standards. The problem here is twofold. One aspect concerns the fact that housing problems of low income families cannot be attributed solely to income. Race is an important element in the difficulties that surround the housing decision of many of these families. Financing and market imperfections are also contributing factors. And there are census data that hint at the possibility that some families live in unsuitable housing accommodations for reasons that might be best subsumed under the heading of tastes and preferences.[21]

Yet even if one could take these aspects of the problem into account, there are questions that remain about the amounts of housing consumption that constitute the minimum below which no family should be allowed to fall. For it is not enough to talk about expenditure levels when the concern is with minimum standards. We have to specify the elements of consumption that make up that standard. But this creates a

[16] See C. McFarland, "Major Developments in the Financing of Residential Construction Since World War II," *Journal of Finance*, May 1966, pp. 382–392.

[17] For one discussion of the connections between housing credit and housing expenditures, see R. Muth, "Interest Rates, Contract Terms, and the Allocation of Mortgage Funds," *Journal of Finance*, Mar. 1962, pp. 63–80.

[18] There is some indication of this in the fact that homeownership —which involves the use of credit—is strongly correlated with income. That low income families are restrained from buying homes because of credit factors is likely and, as noted above, not necessarily indicative of irrational lender behavior. Studies have shown the risk exposure of lenders increases if the loan is made to finance the acquisition of property that houses someone who has a relatively low income. See G. M. von Furstenberg, *Technical Studies of Mortgage Default Risk*, Center for Urban Development Research, Cornell University, Ithaca, N.Y., 1971.

[19] See for example M. L. Isler, *Thinking About Housing*, (Washington: The Urban Institute, 1968).

[20] See Tempo, op. cit., pp. 13–23.

[21] Tabulations of 1960 census data, for example, show that while most families who live in substandard housing have low incomes, not all low income families live in substandard housing, nor is all substandard housing occupied by families with very low incomes. See Tempo, op. cit., p. 11.

serious problem, for the meaning of housing output or consumption is by no means evident. It consists of a great many different kinds of services provided both by the dwelling and its environs, and it is by no means clear how these various elements should be fitted together in a composite to be designated as a unit of housing output. Moreover, even if a satisfactory index of housing consumption could be established, when it comes to the specification of some kind of a minimum standard, there is a need for "normative" knowledge. While one cannot come away from a review of the literature on housing consumption without a feeling that there may be warrant for public concern with the housing of low income families, that is essentially what it is —a feeling. If our concern is with which households have what kind of housing problems and how many of them there are, what can be learned from a review of the findings of positive economic analysis will not suffice. Before we can begin to talk about the magnitude of the problem and hence the scope for possible government action, we must have criteria that can be used as a basis for judging the adequacy of the housing of the American family. But what criteria are these? What are the criteria for evaluating the role of government in low income housing?

Criteria for Evaluation of the Role of Government in Housing

Economic discussions of the role of government in the economy and/or particular segments within it usually focus on two sets of criteria. One of these is implicit in the concept of allocative efficiency; the other can be gleaned from discussions of income distribution and is sometimes labelled as equity considerations.

When the focus is on allocative efficiency, the concern is with the assignment of scarce resources to alternative uses in a way that achieves the "best" use of these resources. While the meaning of best is a troublesome matter, if the distribution of income is given, conditions of best or optimal resource use—the so-called marginal conditions—can be specified.[22] A general and popularized expression of these conditions focuses on the social benefits and social costs associated with resource use and postulates the equation of such benefits and costs out at the margin of use in all uses.

Studies of economic efficiency have shown that these marginal conditions are fulfilled in a system of competitive markets. Thus, competitive markets are the focal point of discussions of economic welfare and welfare problems tend to be viewed by economists as departures or deviations from competitive market outcomes—that is, the "norms." Viewed in this way, the welfare problem is taken to mean the problem of market failure, and the central point of inquiry is one of identifying the kinds of conditions that give rise to such failure.

As this issue has been studied by economists, a distinction has emerged among three sets of contributing conditions generally called externalities.[23] One set of these is called technical externalities or difficulties. These arise from production technologies that reward large- or mass-scale levels of output. When output within the firm has to be taken to very high levels to get full advantage of the benefits possible from current technology, competition breaks down. Firm adjustments to such a set of technical conditions generates fewness in number within the industry; hence monopoly elements emerge. And when there is monopoly in the market, it can be easily shown that production will not be taken to the point where marginal social benefits are equal to marginal social costs. Thus, the market fails or there is market inefficiency.

So-called ownership externalities also constitute conditions that give rise to allocative efficiency problems. When economic activities associated with the use of some scarce resource —owned by someone—have impact or spillovers on parties that are not directly involved with that activity, externalities emerge in the sense of costs or benefits imposed on persons who are not directly involved in the activity itself.

Externalities of this sort are legion. There is, of course, the legendary old widow who takes in laundry and hangs it out to dry in an atmosphere that is polluted with the smoke and soot belching from the stacks of a factory located down the street. Here the spillover is a cost imposed by one on another who has no transactions with the first. There are also many illustrations of benefits bestowed on parties who are not a part of the transactions from which benefit flows. What is important about all of this is that it

[22] There is a vast literature concerned with allocative efficiency, most of which comes under the heading of welfare economics. One summary statement of the state of the art is by J. deV Graff, *Theoretical Welfare Economics*, (Cambridge: Cambridge University Press, 1967).

[23] The literature on externalities is also quite large. One recent statement that summarizes and interprets most of the recent work is E. J. Mishan, "The Postwar Literature on Externalities: An Interpretative Essay," *Journal of Economic Literature*, Mar. 1971, pp. 1–28.

means the social and private costs and/or social and private benefits are no longer equal. The private costs of the polluter above, for example, do not include the pollution costs imposed on the old woman who takes in the washing. But if owners of the resources that generate these externalities respond to private costs and benefits in their decisions, they will not adjust their use of these resources to a point of equality between marginal social benefits and marginal social costs. Ownership externalities can lead to too much or too little resource use in terms of allocative efficiency criteria. Hence, markets involving the use of resources generating such externalities will generate inefficient results no matter how competitive they are.

Finally, there are the conditions that give rise to public goods externalities. Such externalities arise when activity involving the use of scarce resources generates goods that can be consumed by one person without diminishing their consumption by others. National defense is a time-honored example. The point is, given the condition of "nonexclusion," the social benefits of the good will not be reflected in the price people are willing to pay for it; hence, the market will not generate efficient results.

This is an elementary discussion of what may be considered as some of the major elements of welfare economics. Its applicability to the consideration of the role of government in housing is evident. Anyone who knows the meaning of the concept of allocative efficiency can understand that relevance. Government intervention can be rationalized on the basis of externalities—if present—that give rise to inefficiencies in the operation of housing markets. The form this intervention should take depends on the nature of the problem, i.e., the form of the externality that gives rise to it. In the case of a public good, we can rationalize government in the role of enterprise. For ownership externalities, some form of regulation and policing action may be warranted. And if the problem is created by technical externalities, regulation and perhaps some form of subsidy and/or taxation might be appropriate.

The allocative efficiency criteria of the economist clearly provide a set of unambiguous notions that can help define the role of government in the housing sector of a market-oriented economy. Attempts to "operationalize" this set of notions, however, encounter difficulty. For while it is easy to talk of externalities of the sort in a very general way, the question of what kind and how much governmental action is appropriate in specific sets of circumstances is a difficult one. The purpose of the collective action is to make the system work better. But how can we be sure that this will be the result? Obviously, there must be some evaluation, which usually takes the form of a cost-benefits analysis of the program or action being considered. Yet there are the well-known difficulties associated with the task of determining the social costs and benefits of particular programs.[24] While it may appear that the benefits (or costs) of some program exceed the costs (or benefits), whether they do or not is by no means easy to establish. Still, these difficulties should in no way detract from the potential effectiveness of allocative efficiency notions to policymakers. The achievement of allocative efficiency is a necessary condition of the great society. Whether it is a sufficient condition as well is much less certain.

Suppose we were able to diagnose correctly the allocative ills of society and prescribe the appropriate government remedies. It is by no means clear that this would be judged the best of all possible worlds. For in the discussion to this point income distribution has been taken as given. If we free ourselves from this assumption, another dimension is added to the problem, for with different income distributions there will be different patterns of resource use that fulfill the marginal conditions of allocative efficiency. Which one of these is best?

The problem here is one of evaluating the impact of income distribution on the happiness coefficient of society; in other words our concern comes with the optimal distribution of income. Unfortunately, there is little in economics analogous to the marginal conditions of allocative efficiency that can be used as a means of making statements about the optimal income distribution. General statements have to be made about the necessity of a social welfare function before this question can be addressed. Yet, the concept of social welfare is extraordinarily difficult to define. Starting with the problem of interpersonal utility comparisons and adding it to a domain, i.e., society as a whole, in which there are so many conflicting interests, the problem seems almost insurmountable. If it is not possible to compare the pain and pleasure of members of society and we consider that society as one in which considerable conflict is generated by altering the distribution of income, it is not

[24] For one statement of the costs and benefits associated with cost-benefit analysis, see A. R. Prest and R. Turvey, "Cost Benefit Analysis: A Survey," *Economic Journal*, Dec. 1965, pp. 683–731.

really clear how one can begin to make statements about which distribution will generate the highest happiness coefficient.

If no such function can be objectively determined, it may nevertheless be that it can be expressed through voting at the ballot box. If we do not have what we want through the operation of the market mechanism, collective action is possible. And indeed government as it operates through its fiscal and other policies does in fact redistribute some of the Nation's real product among individuals.[25] But do we get the kind of distribution results we want through the activities of government? Can we get the results we want? Both political scientists and economists have devoted much time in recent years researching the question of whether the decision rules of a democracy lead to a consistent transitive ranking of social alternatives.[26] If it did, the ballot box could be used as a means of dealing with the distribution question. But apparently it does not, or at least early research raises some doubts.[27] The questions raised in this research have served to clarify aspects of the political process; but they have yet to indicate how knowledge of political behavior can shed light on the question of an optimal distribution of income.

Another approach to the problem that appears to be emerging is one of fitting specific ethical propositions—value judgments—as functions into models that are representations of the system that generates income distribution in the economy.[28] Simulations with such models then generate income distributions that are compared with the actual. The simulated version is taken as the "norm" or the optimal distribution. It is "better" than the actual in that it takes into account important ethical aspects of society believed to have bearing on society's view of what an optimal distribution of income is. Questions can be raised, of course, about the criteria for the choice of the ethical propositions used as a basis of specifying the social welfare function in such models.[29]

Clearly, the concept of an optimal distribution of income is an important one to the judgments made about the role of government in the economy. What seems clear, however, is that we do not yet have sufficient knowledge on the basis of which statements can be made about the conditions for an optimum distribution of income.

Government and Low Income Housing: What Programs?

While the housing of low income families is generally considered to be a problem of long standing,[30] remedial actions through various kinds of governmental programs and policies are of fairly recent origin. All government programs that benefit housing can be considered as activity that, potentially at least, will help low income families upgrade their housing. For even if that aid is directed toward the more affluent members of society, these beneficiaries will presumably release housing that will "filter" down to those at the lower end of the income scale.[31]

There are a number of Federal Government policies and programs that have impact on housing—and hence low income housing consumption—some of whose effects are not so evident as others. Among those whose effects are "indirect" are certain of the fiscal policies of the Federal Government. While the Federal Government does not receive revenues in the form of residential real estate taxes, there have been and still are elements in the tax structure that have affected housing investments. The early stages of the recent apartment house boom, for example, were attributable to a special depreciation provision in the tax law that encouraged the flow of equity money into apartment house con-

[25] See, for example, Tax Foundation, Inc., *Tax Burdens and Benefits of Government Expenditures by Income Class, 1961 and 1965*, New York: Tax Foundation, 1967.

[26] Included among the many references that could be cited here are W. J. Baumol, *Welfare Economics and the Theory of the State*, (London: G. Ballard Sons, 1965): A. Downs, *An Economic Theory of Democracy*, (New York: Harper and Row, 1957): and J. M. Buchanan and G. Tullock, *The Calculus of Consent*, (Ann Arbor: The University of Michigan Press, 1962).

[27] See K. J. Arrow, *Social Choice and Individual Values*, (New York: John Wiley and Sons, 1963).

[28] See, for example, R. C. Fair, "The Optimal Distribution of Income," *Quarterly Journal of Economics*, Nov. 1971, pp. 551–579.

[29] The choice Fair makes comes across as eminently reasonable—all people should be given an equal opportunity in life. But the criteria that underlie the choice—and in fact my judgment of it—is by no means evident in the same way as is the criteria we could use to judge the reasonableness of statements regarding allocative efficiency.

[30] McKelvey talks of overcrowded and generally unpleasant living conditions of low income families in parts of many of our cities in the middle of the 19th century. See B. McKelvey, *The Urbanization of America, 1860–1915*, (New Brunswick: Rutgers University Press, 1962), p. 14.

[31] Many are not so optimistic about the outcome of the filtering process. See M. Edel, "Filtering in a Private Housing Market," *Readings in Urban Economics*, (Eds.) J. Rothenberg and M. Edel, (New York: Macmillan Company, 1972), pp. 204–215.

struction projects.[32] It is also the case that gains or losses from the sale of residential property are treated as capital gains and hence taxed differently from regular income, a tax treatment generally believed to bestow special advantages on investments in multifamily residences. And all homeowners know that interest costs on their home mortgages constitute a deduction for tax purposes. Homeowners are also exempt from making income tax payments on net imputed rents.[33]

There are also a number of Federal programs concerned with the financing aspect of housing, most of which, however, are not concerned with low income housing per se. Much of what is now in force goes back to legislation enacted in the 1930's when the Depression had highly disruptive effects on the Nation's residential mortgage market. Loan insurance through the Federal Housing Administration, the secondary mortgage market facilities of the Federal National Mortgage Association, and a liquidity pool for savings and loan associations in the Federal Home Loan Bank system are examples. In the 1940's housing credit received another assist when the Veterans Administration was given the authority to guarantee mortgage loans to veterans.

These institutions have been added to and modified in various ways over time in response to particular problems that have arisen. The most substantial of these changes in recent years has been the establishment of the Federal Home Loan Mortgage Corporation and the Government National Mortgage Association. What the Government has done, in effect, is to strengthen the bond between savings and housing, and by doing so has made it possible for some families to upgrade their housing circumstances both directly and indirectly.

The Federal Government has also influenced housing through a series of programs concerned with urban renewal and through the interstate highway program, both of which are generally considered to have contributed to the housing problems of the poor by removing a substantial amount of low income housing from the stock without necessarily providing new housing.

There are also Federal Government programs directly concerned with housing the poor, one of which has been in existence for some time. In 1937, the Nation's public housing program was set up with the establishment of the Public Housing Authority. The assistance provided by the Government in the public housing programs takes two major forms, one of which is in the form of financing aids in the construction of the project and the other is a rent supplement to those who are occupants in completed housing projects.

Congress has also authorized what are often called "below-market interest rate programs." These programs have as their primary purpose reducing occupancy costs by providing financial aid to reduce the mortgage interest costs of a low income housing project. The initial programs were set up so that only nonprofit institutions could sponsor such projects, which were to be occupied primarily by persons who not only had low incomes but were either elderly or handicapped as well. More recently, the programs have been expanded to permit sponsorship by profit-oriented corporations, and the beneficiaries need not be only those who are elderly or in some way handicapped.

Finally, Congress has recently authorized the establishment of several other types of programs that provide a basis for housing assistance to those with low incomes. Under the rent supplement programs, for example, tenant families pay 25 percent of their income toward rent.

The Federal Government makes up the difference between these payments and market rent levels by a direct payment to the landlord. There is also a program now designed to aid those with low incomes who wish to buy homes. Assistance is restricted to new or substantially rehabilitated housing units. Eligible buyers finance their purchases with FHA-insured market rate mortgages with private lenders. The Federal Government subsidy takes the form of paying part of the homeowner's monthly mortgage payment where the maximum subsidy allowable will reduce the homeowner's payment to that which would apply if his purchase had been financed with a mortgage having a 1-percent interest rate.

State and local governments also influence housing, although there is much less in the way of programs designed to deal with specific housing problems. As is the case with the Federal Government, the fiscal policies of State and local governments have impact on housing. The reve-

[32] Back in the middle part of the 1950's, Congress provided depreciation rules for investments in residential income property that permitted "first users" to take depreciation equal to double the straight line rate applied to a declining balance. What this provision did was to provide a tax shelter for persons with income derived from other sources.

[33] One writer estimates that because of these homeowner tax benefits, housing consumption is 20 precent greater than it otherwise would be. See Henry Aaron, "Income Taxes and Housing," *The American Economic Review,* Dec. 1970, pp. 789–806.

nue sources of such governmental units are particularly important because they depend so heavily upon real estate taxes, much of which comes from assessments made on residential properties. Obviously, the nature and magnitude of these taxes can have impact on residential investments in particular places. In some places, for example, real estate taxes are alleged to encourage homeownership and result in relatively high housing costs for those who rent. In other places, the reverse situation is said to prevail. And in most places, it is argued that real estate taxes are such that they help to perpetuate the presence of slum housing in cities.

Finally, there are the overall planning activities of cities, counties, multicounty regions and States that are also believed to influence housing investment in particular places. The nature and extent of this influence, however, is not really understood very well and in fact is alleged to contribute to the housing problems of the poor in some cases.[34]

Government Housing Assistance to Low Income Families: Why?

If the role of government in the economy is construed as one of dealing with problems of market inefficiency and the redistribution of income according to some set of ethical criteria, housing policies can be considered in light of these criteria. To consider how government housing policies have measured up to the efficiency criteria and to attempt to assess their redistribution effects is a task that falls far beyond the scope of this paper. Moreover, it would cover certain ground that has been recently worked over by Aaron and others.[35]

There are, however, certain things about these programs worth noting. One of these is the observation that until recently and, with a few notable exceptions,[36] discussions about housing policy have been primarily concerned with what has to be judged as the social welfare of the Nation. While there have been many stated purposes for the programs legislated—to create jobs, to help the poor, to save the financial markets, to improve the tax base of cities, to do away with slums—the 1949 Housing Act set the stage for what has to be considered as an emphasis on what is right and proper for the nation as a whole. The best known of its many statements is the one that establishes the goal of a "decent home and suitable living environment for every American family." The apparent concern in this statement is with those who do not live in decent homes or have suitable living environments, and these are, for the most part, families with low income. While subsequent legislation through the 1950's and much of the 1960's did not provide a great deal in the way of direct housing assistance to the poor, that statement seems to lurk in the background of most discussions of the rationale of our housing policies over this period. That is, the ultimate rationale for the particular bits and pieces of legislation promulgated, if it ever came to the need for talking in terms of ultimate causes, was indicated to be that of providing all American families with decent homes. So what if the benefits of particular programs were directed toward more affluent families in society; the filtering mechanism operated in ways to make more and better housing units available to those living in substandard dwellings. What was less than evident was the meaning to be attached to the stated housing expression of social welfare—a decent home and suitable living environment. Little is to be found in the way of carefully constructed criteria that could be used as a basis for distinguishing between decent and indecent housing.

With regard to efficiency, while the allocative aspects of the Nation's housing markets have always provided a basis for governmental intervention,[37] it was seldom included in discussions of the rationale for particular programs and policies. That it was not undoubtedly stems from the fact that not many people concerned with housing really had much knowledge of the efficiency aspects of the Nation's housing markets. It is, in fact, only recently that the tools of microeconomic analysis have been applied to the housing sector in ways that have generated information necessary to such analysis. Hence, there were rather sharp limits to what could be said about the warrant for government interven-

[34] See L. B. Sagalyn, and G. Sternlieb, *Zoning and Housing Costs*, Center for Urban Policy Research, Rutgers University, The State University of New Jersey, Jan. 1973.

[35] H. J. Aaron, *Shelter and Subsidies*, (Washington, D.C.: The Brookings Institution, 1972).

[36] See L. Grebler, "Criteria for Appraising Governmental Housing Programs," *American Economic Review*, May 1960.

[37] Certainly some of the Government's programs designed to bolster the housing finance program, e.g., the Federal Housing Administration, the Federal Home Loan Bank Board, the Federal National Mortgage Association, can be construed as an effort to deal with certain technical externalities, e.g., access to national money and capital markets and loss protection. And the housing programs that have been designed to help low income families, e.g., rent supplements, public housing, and the like, can be rationalized in terms of consumption externalities generated when these families were living in lower quality dwellings.

tion in this market on efficiency grounds. Since more can now be said about the efficiency aspects of these markets, considerations of allocative efficiency have come to occupy a more prominent role in policy deliberations and are likely to be used increasingly as a means of rationalizing the housing policies of government at all levels.

Conclusions and Recommendations

Housing has been and still remains to some extent an issue that is discussed more in terms of the heart than the head. It is not difficult to find statements by professional politicians and a considerable number of social scientists that wax eloquently about the problem of substandard housing and argue in very strong terms for the need to reduce the disparities such housing implies. And it is difficult to resist the persuasiveness of such rhetoric as it is so easy to inspect at first hand the kind of housing in which some low income families live. But my reading of most of the statements made indicates little in the way of specifics with respect to the meaning of housing standards, a matter of no small importance to the distinctions that have to be made if we are to move collectively in dealing with housing disparities.

It is also clear that both policymakers and students of housing markets and housing policies are now looking much more carefully at housing in general and the role of government in housing in particular. To say this is not to imply that dispassionate analysis has been lacking in the past. But it is clear that the caliber of the analysis of our housing markets and institutions has improved considerably, which is largely a reflection of improvements in analytical and empirical capabilities particularly among economists. We now know much more about the economic aspects of housing because of the works of Reid, Muth, Kain, Rothenberg, Downs, Aaron, and deLeeuw. This increased knowledge combined with the growing interest of economists in applying notions of allocative efficiency to the evaluation of both the private and public sectors of the economy is giving rise to much more critical and effective evaluations of all programs and policies of the Federal Government.

What this means in terms of housing is that we are beginning to look more carefully and systematically at the allocative effects of past and present programs and alternatives that have been suggested for future use. The strategies suggested are now being stated in ways that invite an analysis of both allocative and distributive effects,[38] and such analysis should begin to yield more useful results than earlier efforts because of the better understanding we now have of the way in which the housing market works. Furthermore, as the results of current research efforts unfold and are made public, e.g., the research results from the National Bureau of Economic Research and the Urban Institute, our ability to trace both the allocative and distributive effects of important housing facts will be enhanced. A foundation is being laid on the basis of which inquiries will be made that provide the basis for sound judgments about the efficiency aspects of housing. And such judgments are seen by this writer as an essential input to any effort to define the role of government in the area of low income housing.

It is also the case that we remain some distance from achieving such a goal. Certainly allocative inefficiencies in the housing market can be discussed in a general way. But to make statements about the nature and magnitude of market failures in housing in a way that will provide the warrant for asserting that X dollars will be required to correct for misallocations associated with this set of technical externalities and Y dollars will be needed to deal with misallocations associated with these ownership externalities remains a difficult task. We now have models that allow us to explore some of the allocative implications of certain important housing facts, such as Federal Government housing programs, and Aaron and others have begun to exploit this knowledge in ways that allow us to make some sensible statements about the beneficiaries of these policies and their costs. But as I read this literature, it is by no means clear that we can yet say with confidence that the marginal social benefits of particular programs are or are not equal to or greater than marginal social costs.

Nevertheless what we have before us are a set of unambiguous notions that have obvious relevance to the issue of housing policies. While problems of identifying areas of market failure and the appropriate remedies to apply once these areas are identified are not easy to deal with, we now know enough to be able to express them in ways that can provide a fairly explicit agenda for research. The findings of which should help us to define better the proper role of government in housing. My presumption is that

[38] See A. Downs, "Housing the Urban Poor: The Economics of Various Strategies," *American Economic Review*, Sept. 1969, pp. 165–175.

this is a part of what this current review by HUD of housing policies is designed to accomplish.

Suppose now that through future research we acquire the knowledge necessary to identify the externalities operative in housing markets and to propose the measures involving government that effectively deal with the allocative problems these externalities imply. We could then define or rationalize a role for government in housing in terms of a set of widely accepted criteria. But such a rationalization, while important, would neglect the distributive aspects of the economy. And it is not evident that the results of a set of policies designed to achieve allocative efficiency will generate outcomes that will satisfy someone who is concerned with the problem of a decent home for everyone.

Certainly, the achievement of allocative efficiency would improve the chances of getting all families better housing. But one can easily conceive of a housing market that is allocatively efficient, yet generates results that do not satisfy the criteria specified in some social welfare function. A highly unequal distribution of income could generate such a result as might an equal distribution of income. The point is, it is difficult to see how the matter of income distribution or equity can be ignored in deliberations about the criteria for policy.[39] The problem now is that it is probably included in these deliberations in a way that conceals more than it reveals about issues and conflicts that have bearing on housing outcomes.

But how shall we deal with the matter of equity? Were it only possible to establish the conditions for an optimal distribution of income, the problem would become manageable. For if we knew these conditions, we could take the measures necessary (if they in fact were necessary) to move the system toward such a position. Once there, issues like minimum housing standards should disappear. But the current state of knowledge of the constituents of our social welfare function is primitive and it is by no means clear how the political system can be made to generate such optimality results.

If the income distribution issue remains unresolved, housing policymakers will continue to face the question of what constitutes a decent and suitable home. While the question has been pushed somewhat into the background as the efficiency elements of housing have come to occupy more of the attention of both economists and policymakers, as we begin to make headway in dealing with this problem, I have no doubt about the reemergence of social welfare as a central issue in housing policy deliberations. There are still housing disparities of a considerable magnitude, and when there are disparities of that sort there will be questions.

If markets do not generate what is construed as equitable outcomes, the political process is likely to come into play. But how will it do so? Will it do so in a way that expresses what society believes to be the common good with respect to housing? What is the political process? What is society? What is the common good? These are illustrative of a few of the many questions that can be raised when we consider how the political process operates to modify market outcomes, questions that seem to come to the foreground when we address the matter of equity. While it may seem that the role of government in housing should be defined in terms of criteria that are specified independent of the process that determines that role, when the criteria are found to be vague, elusive, and somehow linked with the political process itself, it becomes important to have a clear understanding of that process.

Yet we cannot avoid facing the question of normative criteria against which performance or outcomes can be judged. For even if the notion of what is fair can only be fully formulated in light of a clear understanding of the political processes operative in housing, ethical criteria will be involved in that formulation.

In looking at housing, the problem comes to focus in the issue of minimum housing standards. If there is to be some determination of the meaning of equity in housing, we must first clarify the meaning of housing standards in general and minimum standards in particular. Current research by such economists as Kain and others that seeks to identify the elements of housing output or consumption, linking it to price in ways that denote weights and importance is clearly relevant to such a concern. For in a free society, standards are presumably reflected in household choices, which means that the outcome of these choices should be revealing of the elements that make up the standards. Yet, knowledge of the coefficients of hedonic indexes used as a means of investigating the component items in that bun-

[39] An increasing number of economists knowledgeable in the ways of welfare economics seem to be coming to the conclusion that if economists are to make any real contribution to the resolution of certain problems, the question of equity will have to be addressed. See E. J. Mishan, op. cit., p. 26; P. O. Steiner, "The Public Sector and the Public Interest," In *The Analysis and Evaluation of Public Expenditure; The PPB System, Volume 1,* Joint Economic Committee, 91st Congress, 1st Session, 1969.

dle will not really provide a basis for establishing minimum standards. When the focus is on minimum standards, we have to think in terms of what is necessary for the well-being of the household. But what do we mean by necessary? What is the meaning of well-being?

Ultimately, the questions of the meanings of necessary and well-being must be related to some set of ethical propositions that represent irreducible elements in what is taken as the common good—the "norms" of society. But what ethical propositions? Is it sufficient to talk in terms of a decent home and suitable living environment? It would seem that the issue of standards could be clarified somewhat with knowledge of the influence of elements of housing consumption on the household. But what does this mean?

Suppose we were able to provide a low income family with a housing allowance that permitted it to move into a dwelling with indoor plumbing and at the same time reduce the impact of housing on its budget from 35 to 25 percent. The economist could presumably make statements about the welfare effects of the allowance in terms of his view or conception of economic welfare. But would that family now be living in a decent home and suitable living environment? It is not clear that the economist could answer this question.

But suppose that psychologists provided us with statements about the impact of the move in terms of certain relevant psychological states that are a part of their conceptual framework. And suppose we gather equivalent information from sociologists, community health specialists, anthropologists, and others. All such information presumably would provide insights into the impact of a change in some housing variable on the personal well-being of households affected by the change. And if we had all of it, we would certainly have something that encompassed more of the totality of the experience of the household than economic information alone. If we knew, for example, that the housing adjustment brought about by such an allowance resulted in a significant change in the health status of the family, we might be willing to make a more affirmative statement about whether the move resulted in the achievement of a decent home and suitable living environment for that family.

It would thus appear that we could make some headway in efforts to clarify what is meant by minimum housing standards, if our approach to the task were multidisciplinary. But the results of multidisciplinary studies, while they would undoubtedly be considered as interesting, would probably be too fragmented to provide the basis for improving the programing aspects of government. While significant improvements in the psychological or physiological states of the adjusting family can be used to rationalize the choice of a particular program—assuming that we can in fact make some sensible statements about the degree of change in these states—it is by no means clear how changes in the various states of the family can be combined in ways that are needed by the policymaker. What policymakers need is information that permits them to say, with some degree of confidence, yes or no to programs under consideration. From the viewpoint of policy formation, what is required is an integrated or interdisciplinary thrust. Yet, the difficulties encountered in attempting to move from a multidisciplinary to an interdisciplinary posture are immense. What is involved is a question of basic theorizing, and it is by no means clear how the job that needs to be done can be best approached.[40]

Were we willing to disregard the question of equity, the rationalization of housing policy would become a relatively simple matter. The concern would be with allocative efficiency criteria and the role of government would be to deal with problems of market failure. But to focus on allocative efficiency alone will not suffice, for the issue of equity will not disappear. What people think about housing has and will continue to turn importantly on their views of what is fair and equitable.

In my view, it is important that HUD address the question of equity in ways that will encourage the research necessary to acquire a better understanding of what it really means. HUD should emphasize several matters to be ticketed for review and research. One matter concerns the normative or ethical criteria. It has been suggested that many social scientists are unable to make a careful distinction between a scientific and an ethical or normative proposition. As this inability could become a matter of central concern in attempting to deal with the question of equity in housing, philosophers with scientific training should be encouraged to make substantive contributions in the sense of clarifying exactly what is involved in the problem we seek to analyze, i.e., the question of minimum housing

[40] For one discussion of the difficulties associated with melding separate disciplines in modeling social experience, see A. R. Winger, "Social Modeling: Crucial Deficiencies and Critical Needs," (unpublished manuscript).

standards. Second, now is certainly the time for someone to assemble housing information and analyses from the various disciplines and in light of these materials, begin to consider how research findings from different disciplines can be brought to bear on the question of the meaning of minimum housing standards.

I believe that economists, among social scientists, are probably best qualified to put these pieces together in some kind of systematic fashion. For in the absence of an explicit conceptual framework, those who are most accustomed to dealing with facts in the context of a theory-oriented framework are mostly likely to be able to create order out of a set of disorderly and disparate facts. How much immediate payoff a review essay of that sort would have for policymakers is not completely clear. But it could show the promise of an interdisciplinary thrust as a means of clarifying the concept of housing standards in a way that provides some insights into the meaning of minimum standards.

Finally, I see a real need to encourage research that will lead to a better understanding of the political processes in housing.

Economists usually have little trouble identifying the "basic" criteria used to make judgments about the role of government in the economy. The problem arises when an effort is made to implement the criteria of the economist. Progress is being made in dealing with the question of allocative efficiency, and ongoing and future research in housing should put us in an increasingly better position to use these criteria. But implicit in the use of, for example, one of the emerging housing simulation models as an aid to investigating the efficiency and distributive aspects of alternative policy strategies is a set of targets or goals, that is, a viewpoint with respect to equity considerations in housing.

This fact creates problems because we are really unable to deal analytically with the question of equity in housing. Yet, it is something that must be dealt with by the policymaker. As I see it, the matter of equity stands as a central problem in any effort made to delineate the role of government in housing. I am not prepared to take a strong stand for more or less government in housing until our studies of this issue begin to generate results that clarify precisely what is involved in the concept of housing standards and how this links up to what is determined as the ethical criteria appropriately applied to the consideration of minimum standards.

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A Rationale for Government Intervention in Housing: The Externalities Generated By Good Housing

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In a number of disciplines dealing with human beings we often know more about what is wrong than about what is right: we know more about abnormality than about normality. Indeed, it is frequently the case that we learn about normality by being forced to face various forms of abnormality. Thus, our conception of good health—physical and mental—derives heavily from grappling with many types of illness. This paper leans on the same principle: We shall try to indicate what good externalities can be generated from good housing by examining what we know and think we know about the bad externalities generated from bad housing.

Housing as a Commodity

Knowledge of the effects of good or bad housing is complicated by the fact that the very concept of "good" or "bad" as applied to housing is subject to many important questions. The trouble stems from the fact that "housing" itself is not a simple or even clear "thing." This ambiguity stems from the fact that housing, unlike most other commodities, is overwhelmingly consumed in a single, specific location.[1] It therefore serves as a geographic base for carrying on a variety of activities, and being the recipient of services and experiences, which are local in character. Since different locations make available base opportunities that can differ markedly, these locational anchoring opportunities should be considered part of that package that a household buys when it buys "housing."

Thus, a "housing package" includes four basic components: the housing structure itself, the lot, the neighborhood in which the structure is located, and the accessibility of this site to the household's desired destinations in the rest of the urban area and elsewhere. The addition of these three nonstructure components is of real importance. If together they accounted for a trivial part of the value of "the package," the housing concept would still primarily refer to physical shelter services. But variations in the price of packages containing essentially the same structure but differing in these other dimensions account for substantial proportions of the total. So these additional dimensions are essential and coequal with structure in understanding the meaning of housing quality. Moreover, as will be discussed below, there are grounds for believing that these nonstructure dimensions are especially rich in the externalities generated by good or bad housing.

If "housing" is really a package of disparate components the goodness or badness of housing refers to configurations of these components. The question of these configurations is complex, since each of the components listed above comprises a large number of dimensions. Among the characteristics of the housing structure that influence the quality of the overall package are surely the number of rooms, the square footage, various architectural amenities and conveniences, and the condition of the structure. While the two size categories are unambiguous with regard to measurement and differences are probably perceived uniformly (at least in terms of direction) by most users, the other two categories are heavily judgmental. Architectural features are not obviously measurable in terms of a single dimension; and different configurations will often be subject to widely differing appreciation by users. The same is true of condition. Housing units having different combinations of "necessary" repairs are not obviously comparable in terms of a single "condition" dimension, and different users will typically attribute different degrees of importance to any given set of repair or renovation problems.

The lot similarly comprises a variety of characteristics: size, shape, topography, placement on street, etc. Here too judgmental factors enter, so that there is no self-evident dimension along which "lot" can be measured and for which differing degrees will be greeted with noncontroversial evaluations.

"Neighborhood" comprises a much greater variety of constituents: the physical appearance

[1] Films, plays, skiing, restaurant eating are also localized, but this localization involves each instance of consumption. In the course of a year a household may consume instances of these commodities in many different places.

of other houses, the socioeconomic, taste, and personality characteristics of other households in the neighborhood, the shopping and recreational facilities, the nonmarket institutions and amenities such as parks and the quality of public services. Again, the intrinsic noncomparability of the dimensions and the judgmental character of both evaluation within each dimension and relative importance of different dimensions, makes the problem of designating quality gradations for neighborhood an extremely difficult one.

Finally, accessibility does not mean a single distance of the site in question to the central business district, but rather the economic cost of taking desired sets of trips to all the desired destinations in the urban area and outside. While these costs are in principle convertible to a single dimension that has overall quality significance, different households will have different desired sets of trips (both with regard to destinations and relative frequency), and so will rate the accessibility of any site differently.

In sum, the dimensions of the housing package contain important judgmental aspects, and the relative desirability of different configurations of the components in these dimensions is even more judgmental; so the overall quality of the package cannot be inferred from a listing of its purely physical attributes. For any household, it will depend on the situation and tastes of the household; and hence different households will often disagree about it because of differences in situation and tastes.

There is a second major problem associated with quality. It concerns the ability to create units of different qualities or to change the quality of existing units. A builder of new units has full power (within the limitations set by zoning and code regulations) to determine the structural characteristics of a new unit. He has somewhat less power to select an existing neighborhood and moderate opportunities to select lot characteristics. But exercise of a neighborhood choice strongly restricts his choice about accessibility. Moreover, he has essentially no power to change neighborhood and accessibility characteristics once he has selected a site. The owner of an existing unit has a moderate ability to change structure characteristics of an existing unit but nothing more. Neighborhood and accessibility changes, once a site is given, are out of the power of the owner and depend on the behavior of a variety of third parties. In focusing on what should and can be done to change the quality of housing it is important to understand that while some components of the package are within the power of builders and owners to change, and can therefore be influenced to do so by public policy, others are outside that power and may have to be approached differently under public policy.

Thus, two cautions must be observed in discussing the consequences of good and bad housing and what to do about them: (1) they must be interpreted in a way that does not violate the judgmental, nonunanimous aspect of evaluation; (2) the question of public policy must recognize that the different aspects of the problem may call for a combination of different policy dimensions.

What, then, should be considered good or bad housing for the present purposes? Since housing is a composite commodity, one or a few very bad components could in principle give a particular package a low overall rating. Similarly, one or a few very good components could give the package a high overall rating. For reasons we shall give later, a more common situation is for many or most components to have the same character. In this latter situation, poor (good) housing is housing that is bad (good) in a number of dimensions at once. This is likely to be true of very bad (good) housing. But the earlier cases of highly disparate characteristics is a possibility; and for these the designation as bad (good) depends on the identity and degree of the exceptional dimensions.

What we shall consider as bad housing in the typical case is where the unit is overcrowded (very low size relative to current occupancy), and in bad condition, with few structural amenities, and on a small lot, and in a bad neighborhood. Inaccessibility is not so much typical of bad housing as it is of constrained locational opportunities (the usual situation of housing segregation). The welfare impact of bad housing will therefore be a composite of the effects of the various component deficiencies. Yet the separate impacts of the individual components have to be understood as well in order to be able to describe the welfare impact of situations where one or a few exceptionally poor components impart the overall low rating. The impact of bad housing may well be the result of deficiencies in nonstructural aspects of the package.

In categorizing housing as good or bad, consideration for the judgmental nature of the concept of housing quality requires that only extreme negative instances be included in the class of bad housing. For nonhomogeneous packages it requires that the exceptional components be significantly below mean level. Moreover, small changes in one or more components will not shift a unit to or from the bad housing category. A shift from bad to good will be identified as the removal of the several deficiencies of the package to a state of average quality. Attainment of premium quality above average is not required for the conceptual improvement from bad to good housing.

Housing Components and Welfare: A Theoretical Analysis

In this section we shall indicate the kinds of impact bad housing may be expected to have on well-being. The argument here is speculative. Later we shall indicate the kinds of empirical evidence that substantiate and/or measure the extent to which these speculations are borne out.

The question of bad housing's impact on well-being is not independent of the issues involved in defining the housing package and "bad housing." The impact of housing conditions depends on what is included in "housing." Moreover, since we propose to include structure and neighborhood components, we shall argue below that their impact is not a simple summation of independent effects, but rather a complex interactive web of influences. This complicates even the theoretical expression of how housing affects welfare. To clarify the issues, however, we shall first present the theoretical impact analysis in terms of a set of separate influences. We shall examine in succession the presumed mechanism by which each component of bad housing can influence well-being. Subsequently, we shall discuss the interactive nature of the influence of the whole complex of components.

A further preliminary must be mentioned. The present paper is concerned with the externalities generated by good housing, not with all of its consequences. The distinction is important. Bad housing is generally the type of housing consumed by poor households (indeed, it is generally referred to as "poor" housing), along with inadequate food, clothing, recreation, health care, etc. As such, it is a typical accompaniment of, and symptom of, poverty, and therefore is a contributor to the low level of well-being associated with poverty. Improvement of housing for such households is tantamount to mitigating their poverty and, on that account, increasing their welfare. This is perfectly straightforward, but it is simply an aspect of redistributing real income to decrease poverty. In this paper we are not concerned with poverty per se, but with housing externalities—of inadvertent and third-party effects that go beyond the quality-level inadequacies associated with low budgets. We are looking for respects in which housing is a strategic focus for helping the poor, because of features that make housing an unusual commodity. We are asking, in effect, in what way is housing special? Thus, in what follows we shall deal with the externality consequences of each housing component, not the simple consequences of low quality consumption.

Housing Structure

Size: What is often considered the most important component of housing quality is the size of the housing unit—its physical quantity. Size is important, and inadequacy is associated with a significant set of externalities. But size is not a self-evident dimension.

Square footage and number of rooms both measure size. Yet there is empirical evidence, both qualitative and econometric, that the two are not considered equivalent by households. More of one can substitute for less of the other with respect to household satisfaction, but the two are not perfect substitutes. For our purposes we shall avail ourselves of both. Inadequate size will be measured in terms of both square footage and number of rooms.

This treatment diverges from the common practice of measuring inadequate size in terms of density of land use—the number of residents per acre. The reason for the divergence is that a major externality arising out of inadequate size is crowding and its consequences. Crowding is a function of shelter space per person, and this is better measured by interior space actually occupied by people. Land use density is more a measure of land crowding than of people crowding. Luxury high-rise apartment buildings may exhibit extraordinary crowding of land but offer large, sumptuous interior space per inhabitant.

Overcrowding leads to psychological stress. Stress is a form of personal disequilibrium. It can be either a positive or negative stimulus for change in that it sets in motion psychological forces to overcome, bypass, or adjust to what generated it. If the individual under stress can end the overcrowding or satisfactorily adjust to it, the stress will have served a positive function. If not, the stress acts as a permanent disturbance, raising the probability of abnormal behavior—depression, apathy, aggressivenes, antisocial acts.

This potential consequence of overcrowding is an "externality" in either of two senses. Its self-destructive path toward depression and apathy hampers the well-being of the victim inadvertently well beyond the mere consumption of a low quality version of a basic commodity. The consumer is in effect the inadvertent "third-party" victim of his own consumption pattern. Its activist, aggressive path brings the more familiar spillover damage to genuine third parties.

Overcrowding is not a purely physical relationship between an individual and his per capita shelter space. Except in a one-person dwelling overcrowding is interpersonal: it is a competition for space on the part of the several inhabitants of a dwelling unit. The character and intensity of this competition depends not only on the amount of space available and the number of individuals sharing it (per capita square footage) but also on their relationship to one another, their respective activities in the shared space, the possibilities for specialized, noninterfering uses of space, their mutual expectations, the duration of their interaction, and other psychosocial factors. The richness of the situational determination is only crudely reflected in per capita space magnitudes.

A group of *n* persons sharing a small space is less likely to be overcrowded if all are familiarly related than if any are unrelated; less if some of their potentially interfering activities can be performed in space outside the shelter; less if the substance of their interaction is gratifying. Thus, doubling of households in the same unit is stressful, as is the absence of appropriate substitute space outside the home. Similarly, households subject to interpersonal tensions on other grounds are likely to have these tensions exacerbated by the feeling of overcrowdedness. In two of these cases, poor households are especially likely to be adversely affected: they double up, and their budgetary deprivation is likely to elicit frequent interpersonal tension. In respect to substitute space outside the home, the poor are largely restricted to street society. While this has its strengths, it leads to some of the neighborhood externalities we shall discuss below. One aspect of it, which has been dealt with in the literature, is the socialization and general upbringing of children. The need to seek outside space tends to decrease parental guidance of children relative to peer group guidance in such families—with a variety of attendant consequences.

Finally, a given degree of space competition may be less stressful if it is known to be temporary, especially if it is a means to a gratifying end, than if there seems no present or near future prospect of improvement, or if exposure to it seems to have no instrumental capacity to achieve desired goals. Thus, upwardly mobile households are likely better to bear a given degree of physical crowding than households who feel stalled, excluded, or hopeless. Once again, the immobile poor are the chief victims.

To summarize, inadequate space leads to crowding. But crowding is as much a social phenomenon as a physical one. Sociological features of poor households suggest that in addition to little per capita space the character of their use of space exacerbates crowdedness. Crowdedness leads to stress and in situations where the source of stress cannot be meliorated over significant durations—as with the dead-endedness of many poor families—it can lead to self-destructive behavior or to third-party damage via aggressive behavior.

A second type of externality consequence of crowdedness concerns physical health. Closeness of habitation aggravates the contagion of infectious diseases. An observable consequence should be the greater incidence of infectious disease morbidity. This is an explicitly "third-party" spillover. The mechanism of this externality is straightforward and persuasive.

A final consequence of crowdedness is the increased risk of a different kind of contagion: fire hazard. The more households are crowded into a single structure to carry on their daily activities, the more likely is a fire to begin in that structure; and the closer that structure physically is to others the more likely is a fire beginning in one structure to spread to other structures. The appropriate measure of hazard for this phenomenon is in terms of households—or persons—per acre: land use density.

A final remark should be made about policy issues. Size has been dealt with in terms of crowding. Yet is is not absolute size at all that is involved but rather relative size—the size of the unit relative to the number of individuals who want to share it. Thus a unit that is too small for its current occupants may not be too small for a different household. An important part of the policy problem of crowding may therefore involve shifting households among existing units instead of automatically attempting to build larger units for all who are crowded (although some of the latter may also be required). In this it may well differ from the problem of dilapidation.

Structure Condition: Structure condition affects the way a housing unit can be used. It is of course a direct constituent of the quality of housing and accordingly a natural influence on well-being derived from consumption at that quality. But it generates externalities as well. The first, like crowding, affects the user in an inadvertent, disproportionate way. The second involves "third-party" spillovers.

Bad condition is a user-victimizer in that it raises the risks of illness, fire, and accident. Flaking leaded paint, broken windows and faulty or inadequate heating, broken stairways and floors and faulty or inadequate wiring, filth and vermin infestations—all easily contribute to a considerably higher incidence of accidents, illness, and fires. Externality spillovers are closely related to these: a higher incidence of user-victim illness or fires increases the absolute number of third parties afflicted even under noncrowded conditions. With crowding as well, the third-party incidence is likely to increase appreciably.

Lot Characteristics

A lot serves two roles as part of the housing package. It is both an extension of the shelter into the outer world and an extension of the neighborhood into the housing package. For the former, it represents an effective substitute to interior space under some circumstances (depending on weather, time of day, physical character of the lot and its boundaries). It is differentiated from the outer world in that it possesses some of the privacy and exclusion of outsiders of interior space. For the latter it represents an opportunity to engage in neighborhood interaction (interpersonal, aesthetic) mediated by some of the controls characteristic of internal space—some degree of resident privacy and his proprietary determination of its use by others.

In addition to its direct impact on well-being as an amenity of the housing package, it generates externalities in combination with other components. Thus, since the presence of an adequate lot is a safety valve for some of the stress resulting from interior crowding, an absence of such a lot ratifies interior crowding. The only substitute available for the lack of private, proprietary space is then the open, uncontrolled—and sometimes uncontrollable—outside neighborhood space. This can have deep psychological impact on household members, and especially children, much of whose socialization thus occurs with a deficiency of both secure space and quasi-secure "halfway house" launching pads to the unfamiliar outside world. The sense of assuredness, of security in a potentially benign environment may be impaired, resulting in personality development that is dysfunctional for mainstream success.

Another combination occurs with neighborhood components. We shall argue below that the neighborhood component of the housing package may be intensely adverse to household welfare. In such cases presence of an adequate lot can exercise a moderating influence, since it may permit performance of some neighborhood interactions under more controlled and thus benign circumstances: that is, it provides a substitute—albeit imperfect—for neighborhood opportunities. As with the crowding combination, absence of an adequate lot ratifies adverse neighborhood characteristics, leaves the household exposed (unprotected) to an uncontrolled environment if any neighborhood interchange is to take place. The personality implications may well be social trauma and misanthropic orientations—both damaging to the long-run success of the household and its members.

Neighborhood

This is the aspect that carries most obvious and substantial externalities. Since the neighborhood, with its varied positive and negative features, is proprietorially separate from any particular housing unit within it, ownership of such a unit confers little or no power to affect the neighborhood configuration. Thus, the attractions—again positive and/or negative—of the neighborhood are preponderantly externalities.

Since the neighborhood is the area that, because of nearness in a general context of nontrivial costs of travel and communication, generally concentrates much or most of a household's buying and socializing activity, as well as much of its recreational and aesthetic experience, and a good part of its consumption of public services (some of which, like education, represent a crucial investment in human capital), the opportunities, threats, attractions, dangers, etc. of the neighborhood have a large impact on the household's well-being. It often forms the most palpable form of the society, with its rewards and punishments, for the household. A bad neighborhood will hurt the family's welfare, a good one will aid it.

A neighborhood can be bad or good in different ways. A bad neighborhood may be bad because of a deficiency of shopping or recreational facilities, or because of low quality public services, or aesthetic aberrations, or because of the presence of undesirable neighbors or because of actual high risk to life, health, and property through crime, fire hazard, and high disease incidence.

These different aspects often coexist. Such coexistence is not accidental, but part of a complex process of self-selected location, consistent reciprocal expectations, and group exclusion. Because the purchase of housing typically represents the largest single consumption transaction engaged in by a household during the year, poor households are not likely to buy other than poor quality housing. Moreover, since housing for the poor, shops catering to the poor, and the behavior of the poor themselves, are likely to be unattractive or irrelevant to, or actually dangerous for, nonpoor households, the latter will not willingly locate in areas inhabited by clusters of the poor. In general, nonpoor housholds will seek, and the market will supply, neighborhoods concentrating features attractive to them and lacking features unattractive to them. Neighborhoods of the nonpoor will tend to be stratified by income level, and this will be reflected in housing structures, density, shopping, and demographic composition. Through differential political influence, it will be reflected in the quality of public services also.

While poor households may be as repelled as the nonpoor from poor neighborhoods, the self-selection of good neighborhoods by the latter, and the relatively homogeneous provision of facilities by suppliers, will tend to congregate the poor together as a residual. Sometimes their absence from better neighborhoods results from their voluntary market choices, sometimes by actual exclusion. The latter is especially important in the case of racial segregation. Here, similarity by ethnic or racial characteristic is superimposed on income stratification.

The upshot of these processes is a high degree of homogeneity in each neighborhood. Good neighborhoods are likely to be good in most respects; bad neighborhoods, bad in most. Paradoxically, this extends not only to what is present, but to what is absent. One of the symptoms of a bad neighborhood, especially in recent times, is high vacancy rates and heavy abandonments of whole structures by their owners. This can occur even when the overall market for poor units is tight, and while occupied units in the neighborhood are crowded. Their effect is to make maintenance of units chaotic or nonexistent and to invite the further dynamic of neighborhood destruction through widespread vandalism that renders more and more structures unmanageable by their owners, and other neighborhood crime that, together with a collapse of maintenance, make the area repulsive to residents.

Negative neighborhood effects can be grouped into a passive and an active set. The passive set refers to what is done to a household by the neighborhood; the active set refers to how the household responds to the life chances presented to it by the neighborhood. The first is rather obvious: dense, old structures in poor condition physically increase the hazard of fires starting and spreading widely. Overcrowded units and low budgets for heating, clothing, food, and medical care encourage illness to begin, to spread, to flourish. Low political influence with the municipal government plus high per acre needs for public services together with less-than-proportional tax payments, lead to provision of public services at lower than average quality levels. Retailers and owners of housing, faced with inadequate, but often captive, effective demand in the neighborhood, supply shoddy commodities at above average prices. All of these clearly affect resident welfare adversely.

The active responses are more subtle. The relative homogeneity of neighborhood includes demographic characteristics. The bad neighborhood contains mostly people who are poor, undereducated, immobile. Their common presence is as least as much an exclusion from mainstream society as it is a voluntary cleaving together for comfort. Examples of human failure are ever-present, examples of conventional success few. The large numbers of like-minded individuals in the same economic straits create critical masses of those for whom the neighborhood represents a defeat in mainstream activities, a hopelessness of succeeding in traditional occupational trajectories. These groups exhibit frustration, despair, anger, alienation. Mutually fortifying one another, deviant attitudes and social codes develop, as well as a behavioral repertoire of antisocial, illegal acts. Crime, both organized and unorganized, becomes institutionalized as an understandable, even accepted, way of life. Even irrational, symbolic violence becomes more likely. Sometimes these propensities can spark group orgies of violence in riots.

Thus, the sense of exclusion and hopelessness engendered by the homogeneous deprivation of bad neighborhoods leads to widespread attitudes and behavior that are, in the form of apathy and depression, self-destructive of high motivation for conventional achievement, and, in the form of crime and violence, directly damaging to innocent third parties. These are exceptionally important types of negative externality.

Accessibility

Accessibility is a commodity-type component of the housing package. Different degrees can often be bought by the customer in such situations, who knows exactly what he is buying. This is not an externality. But externalities do sometimes enter this dimension as well. Households generally select appropriate neighborhoods and they seek specific housing units within them. Since neighborhoods are not trivial in size, there is rarely a very large number of neighborhoods in any urban area. So not every combination of structure-neighborhood-accessibility is available to every selecting household. There is a limited range of package types. This itself does not constitute an externality. But it does when there is definite exclusion of some groups from some neighborhoods via discrimination. This artificial and coercive process can severely limit the overall housing area alternatives for groups discriminated against. The group's ability to trade off between accessibility and other housing components can be seriously hampered. In effect, the locational choices of others and stipulation of barriers to similar choices by a household in question have adverse welfare effect on the latter. This externality can be especially damaging where inaccessibility affects the ability to find and hold desirable jobs.

The relation of this to bad housing is that the segregation that severely diminishes accessibility choice typically is applied to ethnic and racial groups with mean incomes significantly below the average for the urban area. Their resulting segregated neighborhoods are likely to be poorer than the average. Furthermore, barriers restricting their range of locational choices are likely to raise the real price of housing to them. This is a consequence of the externality that exacerbates the real income loss resulting from the externality itself.

The Structure of Causation

In the last section we treated the impact of bad housing on welfare as if it were a sum of separate factors each having a well-defined and separate impact. Passages throughout, and the whole of the subsection devoted to neighborhood effects, suggested a very different story. At the base of the problem is that, because of the processes of self-selection, exclusion, and the like, neighborhoods are relatively homogeneous. This homogeneity includes housing structures and their use, demographic features, and area locational factors. The various components of many, possibly most, housing packages will be harmonious with one another: good housing will be good in most respects; bad housing, bad in most respects.

One obvious consequence is that we shall not often be able to observe a high degree of variability of quality level in the several components of a given housing package. This means that the observed "outcome" of good or bad housing will be the result of the joint working of similar quality in all or most of the housing components. This complicates the attempt to trace specific causal links.

A further complication arises from the fact that the several causal factors are not themselves independent of one another. They are both contributory factors for the appearance of one another, and operate on the well-being of households in significantly interdependent ways —their mutual impacts are nonlinear, synergistic. It is difficult, perhaps nearly impossible, to separate some of their effects analytically or statistically.

As an example of complex interdependencies, consider space and structure condition, lot, neighborhood, and population characteristics. Take a group of poor families, also subject to racial discrimination. The mixed effects of budget inadequacy and exclusion (discrimination) will find them concentrated in the slum areas of ghettos. Here, they will occupy overcrowded housing units in poor condition, with little or no outdoor shelter space, located in a neighborhood relatively homogeneous with respect to absence of aesthetic amenities, relatively ill-served by public services, and often treated as captive customers by private retail establishments. Their internal overcrowding will be unmitigated by outdoor shelter, and the resulting combination of family improverishment (poor food, for example), very heavy internal use, poor and hazardous condition, and a lack of feeling of deep responsibility for what is typically only rented property (given the pent-up frustration and fury and sense of hoplessness about their life chances), will tend to result in heavy depreciation of the property, inadequate maintenance and other housing services, and a high incidence of accidents and fire and illness. Besides, the pervasiveness of despair and rage in the neighborhood, exacerbated by these ungratifying shelter characteristics, will move residents toward criminal careers, eruptions of casual violence, interpersonal relations that are poisoned by mutual disappointments, and a wide variety of personal and interpersonal maladjustments. The shelter and neighborhood deprivations will tend to augment one another, so that neither grants succor from the harshness of the other. There is no escape. Under these circumstances one would expect the interplay of physical and social environment to promote most serious welfare impairment on its participants.

An earlier treatment by the present writer describes some aspects of the complex of causation surrounding these phenomena:

> Slums are said to (1) increase fire hazards, (2) increase the menace to health, (3) breed crime, and (4) generate individual personality difficulties. These are all areas where quantitative measurement is difficult, but some are more tractable than others. In most cases the problem is either that it is not clear exactly what should be measured, or that even if that is known, measurement is inaccessible.
>
> Except with regard to fire hazards, the mechanism by which the existence of slums is supposed to "cause" these effects is neither well understood nor widely agreed upon. Moreover, in terms of what is understood, the causative process is broad, diffuse, and long-acting. It is not a case of a one-shot exposure to the "cause" at a specific time and place giving rise to a specific instance of the "consequence." The process at any one time is nearly invisible. It operates as a continuous setting of complicated interrelationships, an environment which slightly enhances the probability of some kinds of behavior and slightly reduces the probability of others. Thus, it is a stochastic, long-continuing process. Moreover, many of the alleged effects are also said to be influenced by a variety of other factors, which also generally operate in much the same diffuse, long-continuing way. The picture is often complicated further because these factors are often interrelated among themselves and related to the existence of slums. For example, health is influenced by income level, occupation, ethnic background, age, and physical surroundings. Moreover, these influences are themselves interrelated. The slums contain a far higher proportion of individuals who are poor and old and ill and poorly employed and members of minority groups than the national average. So causal relationships are, at best, difficult to unravel.
>
> A last difficulty on the purely qualitative level is that even where a certain effect does occur, it is often difficult to detect. Personality and family difficulties are extremely hard to discover. Even aggravations of crime and illness, apparently so observable, are not easy to become informed about, since information about them, whether quantitative or even qualitative, is notoriously imprecise. Finally, the processes are so intrinsically stochastic that it is not at all obvious when a significant and not simply chance variation has occurred. These are important limitations.
>
> To summarize so far: the measurement of social costs generated by slums is hampered because the causal process is complicated and interrelated with other causal factors; because outcomes are difficult to read; because in any serious attempt to isolate the effects of slums one must be prepared to separate out the influence of the other, strongly correlated factors; because changes in the arguments of the functional relationship are likely to have only minor, short-run effects, the important effects being truly long-run ones; and finally, because even where effects are isolated, they are likely to be discerned only qualitatively. Quantitative measurement, especially in terms of dollar values, is extremely difficult.[2]

These features hold a number of suggestions for the attempt to provide empirical evidence to verify and measure the externality effects of bad housing: (1) Many of the effects are longrun effects and are observable only as the chance outcomes of changed tendencies; (2) many of the effects are in dimensions that cannot be easily observed, and especially not in quantitative terms (for example, psychiatric personality assessment); (3) many of the intertwining causative influences cannot be easily measured and, in particular, are not often capable of being observed in a reasonable range of separate (or separable) variation; and (4) the nature of the interrelationships among the causative influences themselves, and their interactive influence on resident well-being, are extremely dificult to unravel.

These strictures apply to both statistical and experimental studies. The present context of public policy intervention requires further consideration. Since public policy means to change some aspects of these environments of bad housing, we are especially interested in what consequences flow from such potential changes. This is equivalent to being more interested in the reduced-form equations of a statistical system than in the underlying structural equations out of which the former are generated. In other words, it may not be necessary to know all of what happens within an immensely complicated system, so long as one can dependably predict what will be the outcomes of some particular intervention.

Two cautions are in order. First, the choice of intervention instruments is crucial. The critical distinction for this choice is that between variables that are determined within the system of interaction and variables that are determined outside the system (endogenous and exogenous variables). One can in principle dependably predict the consequences of changes in the second but not of the first. The first one in effect involves symptoms of the state of the system rather than genuine levers. To attack such a symptom directly in a given way will result in different outcomes, depending on the different states of the overall system when the interven-

[2] Jerome Rothenberg, *Economic Evaluation of Urban Renewal* (Washington, D.C.: The Brookings Institution), 1967, pp. 160–161, 163.

tion occurs—and the effect of those different system states will not generally be predictable without knowing the underlying structural (behavioral) relations of the system. Interest rates, rental levels, even the amount of housing units at some designated quality level, are endogenous variables. This does not mean that they should not be valid objects of policy, but only that their consequences on well-being cannot generally be predicted without knowing a great deal about the overall system of influences. Exogenous variables are genuine levers to be applied to the system in the sense that their consequences can be predicted simply by knowing the initial state of the system and without having to know more about the internal adjustment processes of the system.

The second caution concerning policy intervention is that the consequences of interest may be difficult to discern when they appear, and they may not appear for considerable periods of time. Some of the important personality consequences we have mentioned above are those that are affected by the socialization of the young generation. The consequences, while real and potentially of tremendous importance, may not emerge until the children of the present resident adults have grown up. Studies with shorter perspectives will completely miss these.

In the context of policy intervention, it is important to attempt some separation of the effects of the demographic, locational, and structure variables. This is because public programs generally have their major focus on one or two of these, but not all three. In particular, programs that lay greatest stress on individual structures will have less impact on neighborhood and demographic variables. Housing policy has especially neglected demographic variables. Overall impacts will be very different where the population is essentially unchanged than where significant population variables as well as structure and neighborhood variables have been influenced. Yet demographic variables are not easy to influence quickly and decisively. The real, disposable incomes of the population can be changed in rapid, straightforward ways, but many deeply ingrained characteristics are considerably more difficult to alter, especially in a short time.

While our emphasis on the intricate, multidirectional interrelationships among dependent and "independent" variables literally precludes the possibility of achieving perfect separability of the effects of the three types of explanatory variables, some separation can be achieved. Specific aspects of structures, or neighborhoods, or affected population, can be "held constant," either experimentally or statistically. Efforts of this sort are quite important. Without it, empirical findings are at best suggestive, not conclusive.

We now turn to a summary of some of the empirical evidence bearing on the kinds of externalities we have discussed.

Evidence of Externalities of Bad Housing[3]

In my book, *Economic Evaluation of Urban Renewal*,[4] I classed the externalities associated with slum living into four groups: (1) fire hazards, (2) illness, (3) crime, (4) personality and social adjustment difficulties. These classes are relevant here, but they will be brought in differently to accord with our treatment of externalities.

Before discussing them separately, an overview of the evidential record is in order. I reviewed this record up to 1967 in the aforementioned book:[5]

> Studies have been undertaken in search of the answers to these perplexing questions. Many of them are deficient. One type of study simply compares the incidence of disease, fire loss, crime, delinquency, etc., in slum areas with that in non-slum areas, or in the city or nation as a whole. This is clearly misleading. Since the slum population is a highly selective one, as suggested above, the method completely fails to abstract out the effects on these observed behaviors of the very pertinent characteristics of slum dwellers—such as poverty, minority race, old age, primitive rural background.
>
> Another kind of study tries to meet this objection by looking at the same population in both a slum and a non-slum situation, generally by following a group from a slum to public housing. This is misleading too, but at least in one direction. It systematically understates the effects of slum living in the categories studied. Whatever its strength in fact, the influence of slum living, compounded typically with the overall subculture of poverty, must be a deep-seated diffuse one within the individual's psyche. A move into a better environment after long immersion in the slum, other elements of poverty being unchanged, is unlikely to have important, immediate effects on his deep cast of personality or even his physical health. He will probably bring his behavior patterns and his ailments with him into the new surroundings. This is especially likely if groups of families move together from one site to the other. Each family will reinforce the other in retaining behavior traits generated in their former circumstances. New influences are likely to have an impact only very gradually over time. The strongest effect of a radical change in environmental benevolence is to be seen in the development of the new generation. This effect may be of great importance; yet it

[3] I want to thank Mr. Kenneth Rosen, MIT, for his extensive help in collecting this evidence.

[4] Ibid.

[5] Rothenberg, op. cit., pp. 161–163.

is likely to be missed in many studies, since they typically take a much shorter time perspective.

The 1951 article, "The Social Cost of Slums," by Jay Rumney,[6] who was himself an active empirical investigator in the field, summarizes many of the statistical studies produced in the period 1933–46. They cover thirteen cities, mostly northern. In city after city, the slums are shown to be the areas with the most disease, fire, crime, and social disorganization compared with the rest of the city. Slums and blighted areas are correlated with indices of social pathology, such as rate of juvenile delinquency, illiteracy, relief cases, disease, etc. These do not establish causal relationship, of course. Most of the studies simply adduce gross associations with no attempt to correct for the influence of special population and other qualifying factors. A few, however, do try to correct for some factors—roughly poverty—by comparing slum dwellers with public housing dwellers; but other selective characteristics of public housing inhabitants are not adjusted for in these more carefully controlled studies (1933–45), which show that public housing dwellers had a better record than slum dwellers. In the presence of a 1947 study, which compared the same families first in a slum and then subsequently in "decent" housing and found that transplantation resulted in substantial improvement in behavior, these better-controlled findings add persuasiveness to the hypothesis that slums themselves—not, for example, poverty alone—cause social costs.[7]

Crowding

There are many studies on the effect of crowding. The classic study establishing a biological basis is that of John B. Calhoun.[8] He investigated the impact of high population density living on rats in an experimental format. The results of his experiment were that rats in high density situations develop abnormal behavior patterns that can even lead to the extinction of the population. The finding is intended to be extrapolated to human populations: high population density can be harmful to man.

Application to the human situation has led to a number of complicating considerations. Land-use density is a poorer measure of crowdedness than is internal space per resident. And internal space is perceived heavily in terms of the privacy it offers.[9] But internal space is sought not only for privacy but as a sanctuary against physical and interpersonal danger. This role is sometimes generalized to external space —the lot and even the neighborhood. The prime concern of the lower class is to make "the home a place of security." The conclusion is strongly suggested by an interview investigation of social and community problems in large public housing projects.[10]

But internal space is not an invariant indicator of crowding nor of the ability of a household to obtain shelter services. External space can be used as a substitute for internal space, but this possibility depends on the warmth and benignity of neighborhood interactions. There may even be systematic differences in neighborhood supportiveness by ethnic or racial characteristics. An interview study of poor blacks in Detroit showed far less sentimental attachments to homes, neighborhood, and external space in low income black neighborhoods in Detroit than had been discovered in the ethnic west end of Boston.[11] Social values, perceptions, and interactions thus intervene between the purely physical reality of internal space and the condition of crowding—a psychosocial reality. This psychosocial aspect of crowding is stressed in an important interview-correlation study by Mitchell in Hong Kong. Incorporating in his sample some of the highest urban densities on earth, and attempting to control some of the other forms of deprivation and stress usually associated with poor housing, he found that internal space per capita influences satisfaction with housing but has less effect on deeper aspects of emotional strain and hostility. In addition, the availability of outside space as a substitute for internal space has a significant affect on at least one important familial function: parent-child relationships. Upper floor residents —having less access and surveillance control over outer space—have difficulties in the socializing supervision of their children relative to lower floor residents.[12] The apparent absence of serious stress consequences of such high densities very likely testifies to the fact that crowdedness is a social fact, not a physical one. In a city where all densities of the social classes studies are enormous, the social meaning of space deprivation must be quite different from that in American cities, where much lower densities are encountered, even in the worst slums. So crowdedness must refer to a relative space deprivation, defined in terms of customary social expectations.

[6] Jay Rumney, "The Social Cost of Slums," *Journal of Social Issues*, Vol. VII, Nos. 1–2, 1951.

[7] F. Stuart Chapin, *Experimental Designs in Sociological Research* (New York: Harper), 1947.

[8] John B. Calhoun, "Population Density and Social Pathology," *Scientific American*, February 1962.

[9] Florence C. Ladd, "Black Youths View Their Environments: Some Views of Housing," *Journal of the American Institute of Planning*, March 1972.

[10] Lee Rainwater, "Fear and House-as-Haven In the Lower Class," *Journal of the American Institute of Planners*, January 1966.

[11] Eleanor P. Wolf and Charles N. Lebeaux, "On the Destruction of Poor Neighborhoods by Urban Renewal," *Social Problems*, Summer 1967. This is the Detroit study. One of the West End studies is Chester W. Hartman, "Social Values and Housing Orientations," *Journal of Social Issues*, April 1963.

[12] Robert E. Mitchell, "Some Social Implications of High Density Housing," *American Sociological Review*, February 1971.

This intermediation of psychosocial factors has been systematically integrated into a theoretical formulation of crowding by the social psychologist Stokols—a formulation to which my treatment in the second section of this paper is strongly indebted.[13] The social complexity of crowding phenomena suggested by this model clarifies why empirical researches on crowding have obtained somewhat mixed results. Their specification of presumed different degrees of crowding did not attend to enough facets of the social situation to guarantee that such differences existed. Most of these studies also use quite short-term measures of stress consequences. A further examination of the nonphysical dimensions of crowding was made by Wilner and Baer.[14]

The upshot of all this is that there is suggestive but not conclusive evidence about the lively perception of, and some adverse consequences from, crowding. The definitive study or studies have not yet been done, since there has only gradually and recently been significant progress in understanding the social complexity of the phenomenon. One can expect this growing sophistication about what human crowding really is to be embedded in empirical investigations in the near future.

The rest of the empirical evidence will be introduced in terms of the four category classification presented above: fire hazard, illness, crime, and personality and social maladjustments.

Fire Hazard

The most significant study I have seen in this category is by Richard F. Syron.[15] He documented and rationalized the hypothesis that fire losses are greater in core areas than in noncore areas of a metropolitan region. He uses multiple regression analysis to "explain" statistically fire losses in different parts of the city, using an explanatory variable that expresses poor housing conditions (percentage of dilapidated housing units) but also variables that control for other aspects of poor neighborhoods that are associated with poor structural condition (percentage of nonwhite population, population per acre, percentage renter-occupied, percentage of poor households, percentage of low housing value, percentage of low educated adult population). He found a significant and large positive coefficient between size of fire loss and percentage of dilapidated housing units, and this variable had by far the greatest influence on the size of fire loss. In a different regression he found that number of vacant units also has a significant positive relationship with fire losses. This is a highly persuasive study.

These findings are consistent with those of a study by Robert K. Yin, one which does not attempt to separate neighborhood from structure variables.[16] He finds that a higher incidence of fires is to be found in neighborhoods in poor condition than those in good condition.

Illness

A large number of studies has attempted to measure the impact of bad housing on health. I reported on some of these in my book on urban renewal. I here quote relevant passages: [17]

> There are a number of studies that use an approach similar to the first [establish gross statistical association between housing characteristics and illness, supplemented by knowledge of a generally accepted mechanism of transmission]. Among the most notable are those of Daniel M. Wilner and his associates.[18] The method used most is to study the effect of housing on specific illnesses. The understanding of causative connections between housing and specific illnesses supports a net causal interpretation of its gross association with total morbidity and mortality. A summary of some of Wilner's findings, as cited in Schorr is quoted below.[19]
>
> 1. Acute respiratory infections (cold, bronchitis, grippe), related to multiple use of toilet and water facilities, inadequate and crowded sleeping arrangements.
>
> 2. Certain infectious diseases of childhood (measles, chicken pox, and whooping cough), related to similar causal factors.

[13] Daniel Stokols, "A Social-Psychological Model of Human Crowding Phenomena," *Journal of the American Institute of Planners,* March 1972.

[14] D. W. Wilner and W. G. Baer, "Sociocultural Factors in Residential Space," Environmental Control Administration, HEW, 1970.

[15] Richard F. Syron, "An Analysis of the Collapse of the Normal Market for Fire Insurance in Substandard Core Areas," Chapters VII and VIII, Federal Reserve Bank of Boston, Research Report #49, January 1972.

[16] Robert K. Yin, "The Development of Social Indicators: The Case of Fire Alarms," New York Rand Institute, WN-7565, November 18, 1971.

[17] Rothenberg, op. cit., pp. 169–170.

[18] For example, *The Housing Environment and Family Life* (Johns Hopkins Press, 1962); "Housing Environment and Mental Health," in Benjamin Pasamanick (ed.), *Epidemiology of Mental Disorder,* Pub. No. 60 (American Association for the Advancement of Science, 1949); "The Effects of Housing on Health, Social Adjustment and School Performance," Proceedings of 39th Annual Meeting of American Orthopsychiatric Association, 1962; "Housing as an Environmental Factor in Mental Health: The Johns Hopkins Longitudinal Study," *American Journal of Public Health,* Vol. 50 (January 1960).

[19] Alvin L. Schorr, *Slums and Social Insecurity* (U.S. Department of Health, Education and Welfare), 1963, p. 14. Other ailments, such as rat bite and certain filth-borne diseases, also are closely associated with slums.

3. Minor digestive diseases and enteritis (typhoid, dysentery, diarrhea), related to poor facilities for the cold storage of food and to inadequate washing and toilet facilities.

4. Injuries resulting from home accidents, related to crowded and inadequate kitchens, poor electrical connections, and poorly lighted and unstable stairs.

5. Infectious and noninfectious diseases of the skin, related to crowding and facilities for washing.

Other diseases that, one may be confident, may be caused by poor housing include lead poisoning in children from eating scaling paint, and pneumonia and tuberculosis.

This approach could separate out much of the influence of specific population. But a sizable interplay may remain. While certain housing characteristics may raise the probabilities of specific disorders in perfectly straightforward ways, the extent of the impact may well depend on population characteristics that were not allowed for (systematically controlled) in the investigations.

Such studies are, of course, not conclusive because they inadequately control for associated explanatory influences. A second approach is called for—one that establishes net statistical association by abstracting out such coordinate influences statistically. An early work of this sort establishes the connection between crowding and infant mortality rates, controlling for some aspects of demographic character.[20] Another, more recent study is that of Schmitt.[21] Eleven measures of poor health were associated by multiple and partial correlation with five measures of density and overcrowding, controlling for income and age distribution. Association was discovered between the two sets, the stronger being accounted for by the density variables. No causation is established by this kind of study, but the statistical association is suggestive.

The special phenomenon of housing abandonment has been seen as a particularly serious health menace. Following is a summary statement by Eliher Richter of his study on the subject: [22]

In New York City, from 1965 through most of 1968, 107,000 dwelling units, housing an estimated 428,000 people, were abandoned by their owners; during the same period, only 10,115 low-rent units, housing an estimated 40,500 people, were constructed. Abandonment of tenements by their owners is now occurring at the rate of 30,000 units per year, predominately in slum areas such as East Harlem.

Of the 1,750 buildings demolished by the City in 1968, 68% were structurally sound. Abandoned buildings are usually structurally sound, but poorly maintained. Rent and housing codes, lack of money, bank mortgage policies, management problems, narcotics, crime and the adjustment difficulties of newcomers to New York City are some of the reasons for this situation.

Equally alarming are the environmental conditions now prevailing in those tenement dwelling units still occupied and receiving skeletal maintenance services. Environmental deterioration in these buildings is periling the health and safety of people residing in slum sections of New York City. In East Harlem, lead poisoning, home accidents and injuries, rapid spread of infectious diseases, the winter suffering of the old and the young because of the cold, burns and deaths from tenement fires, carbon monoxide poisonings, bronchial asthma, and, probably, needless mental suffering are some of the definable and preventable health hazards of the estimated 130,000 people living in tenement buildings with inadequate maintenance services. Severe health and safety burdens are imposed on people living in buildings with malfunctioning heating and hot-water boilers, broken plumbing systems, missing window guards, broken windows, harborages for insects and rodents, stagnant water pools in cellars and yards, inadequate waste management and disposal arrangements, peeling of leaded paint, unlit and cluttered passageways, and garbage-filled courtyards. Thus, tenement building maintenance has implications beyond conservation of the existing housing stock. It can easily become the basis for efforts to reduce the major environmental health and safety burdens of slum dwellers.

Crime

I quote from my survey in the urban renewal book: [23]

Once again the question must be faced: How much of the gross association between slums and crime represents a net effect of housing proper? Many statistical studies show large gross associations between slums and crime. But they fail to control for important variables. The need for such control is illustrated by a study referred to above, that of Bernard Lander on juvenile delinquency. Lander found significant simple correlations between juvenile delinquency and both overcrowding and substandard housing. However, after extracting the effects of percentage of nonwhites and median educational level, the net relationship with the slum variables became zero. The only variables that maintained significant net associations with delinquency were racial heterogeneity and the percentage of homes rented rather than owned, which Lander rationalised as factors contributing to anomie (social rootlessness).

Characteristics of the slum population, and of their social interaction stemming from other than housing conditions, must play an important role in crime. The complex of poverty, poor education, low morale, and discrimination—and its ramifications—must be an important explanatory and predictive factor. It should be remembered too that this complex influences the housing market to produce slums. So causation is highly complicated and involuted.

An elementary statistical analysis would introduce variables like family income and median education along with slum variables like overcrowding and dilapidation (or simply percentage of substandard dwellings) as independent

[20] P. Stocks, in *Proceedings of the Royal Society of Medicine*, Vol. 27, 1934; reported in Martin, A.E., "Environment, Housing and Health," *Urban Studies*, February 1967. Martin's own work is a case study of a rehoused community, designed to isolate the impact of slum housing by a before-and-after comparison. He finds that the complex social background of the group studied makes assessment of the individual factors practically impossible.

[21] Schmitt, op. cit.

[22] Eliher Richter, *Program to Train Environmental Service Agents*, Division of Environmental Medicine, Department of Community Medicine, Mount Sinai, City University of New York, April 1970, pp. 3–4.

[23] Rothenberg, op. cit., p. 171.

variables regressed against crime incidence (in per capita terms). It is not expected that such a regression will completely untangle the strands of causation. But it is not essential that they be untangled for policy purposes. The factors do not have an independent impact on crime, but one rather that results from influencing and being influenced by the whole cluster of forces. The policy problem is to manipulate salient factors; and salience is not equivalent to net statistical significance. Housing could be a salient factor in the complex. At any rate it can be manipulated on a substantial scale. This may make it more strategically accessible than is poverty, or discrimination, or morale.

No such carefully controlled studies have been made. Instead, we have largely gross association between slum conditions and crime. Sometimes we have interview opinions and observer interpretations about such a connection. Thus, the Report of the National Advisory Commission on Civil Disorders, using a methodology of this sort, reports that inadequate housing was on the first level of intensity in grievances by populations that had rioted. In nearly every disorder city surveyed grievances related to housing were important factors in the structure of Negro discontent.[24] Byron E. Munson agrees that many nonhousing factors are involved in riots and other social problems. But he denies that housing is a causative factor at all.[25] However, no decisive counter-case is made either.

A more direct kind of connection is made on architectural grounds by Oscar Newman.[26] Here he shows how the form and design of residential areas crucially affect the rate of victimization by criminals by making criminal assaults physically more or less feasible. He argues that the design of housing can encourage or discourage crime.

Once again there is not a body of decisively persuasive evidence linking bad housing per se with crime. But this is not itself negative evidence, either. The task of showing a fully controlled linkage is extremely difficult. We should rather conclude again that some provocative and plausible relationships have been empirically suggested, but conclusive verification still awaits an appropriate study design.

Personality and Social Maladjustment

Here too it is convenient to summarize an overview statement about the evidence from my urban renewal book.

There is an imposing literature on the subject, producing a body of evidence that is perhaps nowhere definitive, but together forms a persuasive whole.[27] To indicate the flavor of the findings, a summary of Schorr's survey of the literature may be quoted:

Though the evidence is scattered, taken as a whole it is substantial. The type of housing occupied influences health, behavior and attitude, particularly if the housing is desperately inadequate [i.e., "dilapidated" or lacking a major facility] . . . . Housing, even when it is minimally adequate, appears to influence family and social relationships . . . . Those influences on behavior and attitudes that have been established bear a relationship to whether people can move out of or stay out of poverty. The following effects may spring from poor housing: a perception of one's self that leads to pessimism and passivity, stress to which the individual cannot adapt, poor health, and a state of dissatisfaction; pleasure in company but not in solitude, cynicism about people and organizations, a high degree of sexual stimulation without legitimate outlet, and difficulty in household management and child-rearing; and relationships that tend to spread out in the neighborhood rather than deeply into the family. Most of these effects, in turn, place obstacles in the path of improving one's financial circumstances.[28]

They decrease both the range of opportunities and the mobility of families in response to differential opportunities.

These findings receive more solid support from two statistical investigations that do control for some associate variables. The earlier cited study by Robert C. Schmitt did successfully link measures of density and overcrowding with 11 measures of poor health and social disorganization, controlling for income and age distribution.[29] Moreover, a directly relevant work by Stacey and Engle[30] uses a before-after comparative format of slum dwellers to lend even stronger support. Two groups of black slum dwellers were relocated to rental status in adjacent slums and ownership status in newly developed suburbs, respectively, with housing quality better in the latter than the former. Multivariate analysis showed that the move to better housing resulted in a "more positive orientation to society." The change significantly reduced feelings of powerlessness. The element being explicitly isolated was perceived as tenure status, but the complex involved seems appropriately designated as better housing.

How shall this whole record be evaluated? It is mixed—less in terms of conclusions (although

[24] Byron E. Munson, *Substandard Housing and Social Problems* (Washington, D.C.: U.S. Government Printing Office), 1968, pp. 467–482.
[25] Ibid.
[26] Oscar Newman, *Defensible Space* (New York: Macmillan Co.), 1972.

[27] A number of these works are listed in the appendix to Chapter III of Rothenberg's *Economic Evaluation of Urban Renewal.* In addition, for example, see James S. Plant, "Some Psychiatric Aspects of Crowded Living Conditions," *American Journal of Psychiatry,* Vol. 9 (March 1930). Also see the survey of the literature in Schorr, op. cit., pp. 14–31, as well as a useful bibliography.
[28] Schorr, op. cit., pp. 31–32.
[29] Ibid.
[30] William A. Stacey and Ronald C. Engle, *Multivariate Analysis of the Social Effects of Housing,* University of Texas, 1971.

there are certainly some contradictory findings) than of relevance and strength of statistical and/or experimental handling. The drift of results does more or less tend to support the general hypotheses presented above, but these are rarely conclusive. The hypotheses are not rejected however. It is primarily a situation where formidable empirical verification is extremely difficult to achieve. What is encouraging is that an appreciation of what constitutes good empirical procedures is growing. Some of the persuasive studies we seek may be shortly forthcoming.

I am including the partial bibliography of works on this subject that appeared in my book in the bibliography to this paper.

Goals of Governmental Intervention in Housing Markets

It is surely beyond the scope of the present paper to examine systematically the goals and instruments of public policy in housing. But it is appropriate very briefly to indicate what implications for public policy, if any, follow from the presumed presence of the externalities discussed above.

First, the policy implications will not represent a fully proportioned set of goals or appropriate instrumentalities, since the externalities question is not the only ground on which desirable public intervention might be based. It therefore constitutes only one part of the foundation for public policy. Second, we have discussed the question of the positive externalities obtainable from good housing via its inverse—namely, the negative externalities resulting from bad housing. This makes a difference. We have not stressed a spectrum of good things that might arise out of minute or even moderate improvements in various aspects of housing. Rather we have emphasized the situation in which there is a coherent concentration of "bads" in the various aspects of housing. We have argued that such concentrations are likely to exist and that their existence tends to create a multiplicatively negative impact on well-being. What this implies for policy goals seems to be that public intervention should focus on trying to achieve multifaceted transformations of slum-living conditions.

This has several features. First, the appropriate focus of intervention is the poor households living in slums. Second, attention should be paid to the mutually augmenting effects of structure, neighborhood, and accessibility. The proper goal is to gain improved housing units in better neighborhood environments without artificial constraints on accessibility for these households. Achievement of one part without the others may result in inefficiently small overall gains for the target population.

There are a number of ways to improve housing unit quality for this population. One involves production of new units aimed directly at this population—public housing or private subsidized supply or rent allowances to the poor. Another involves augmenting the overall supply of housing so as to accelerate the filtering of units to the poor through lowering the real costs of units at relevantly higher quality levels than are currently being consumed by the poor. A third involves increasing the scale and intensity of upgrading of existing low quality units, so that they will be available to the poor at lower real costs than at present.

Similarly, there is more than one basic route to the provision of better neighborhoods. One route involves massive upgrading of existing slum areas as totalities: in effect, to enable large scale upgrading to "internalize" the externalities inherent in slum neighborhoods. Another involves facilitating the ability of present slum dwellers simply to escape from these areas into nonslum neighborhoods. This can come about by two related routes: (1) accelerated filtering of individual housing units in nonslum areas to slum resident, (2) breakdown of artificial constraints on interneighborhood residence mobility because of discriminatory segregation. The first of these emphasizes housing supply forces operating on individual decisionmakers; the second emphasizes lumpy, many-party (all-or-nothing) constraints on market adjustability. The artificial constraint on accessibility refers primarily to the existence of such "coalitional" barriers to market mobility: groups arbitrarily restricted in choice to certain neighborhoods and hence to the resulting "coerced" pattern of inaccessibility (especially with respect to job markets).

Considering these different basic routes to the policy goal suggested here, there are a number of different kinds of policy instrumentalities available for achieving them. In particular, there are demand-side, supply-side and market-adjustment-side instrumentalities. Demand-side approaches attempt to augment the purchasing power potential of the target population through income or rental supplements. Supply-side approaches have both a direct and an indirect form. The direct form entails either public construction of new units meant for occupancy by the target population or public subsidization of private provision of new units for this population at prices lower than at present. The indirect form entails public subsidization of an augmented private flow of new units at quality levels and in amounts sufficient to accelerate substantially the filtering of better existing units to the poor by lowering their real prices and opening up hitherto unattainable better neighborhoods. The market-adjustment approach requires measures that prevent or break up existing patterns of discriminatory neighborhood exclusions (which foster involuntary segregation).

Our brief evaluation of different policy approaches to follow will make use of this typology.

Recent Federal Housing Policy and the Achievement of Intervention Goals

In this necessarily brief evaluation I shall emphasize three aspects of recent Federal policy: the urban renewal program, subsidization of the supply of single family ownership units, and subsidization of the supply of apartment buildings. While brief and informal, this study uses the conceptual framework and preliminary empirical findings of an econometric study of housing markets in which the author has been involved.

Urban Renewal

This has two branches: the area redevelopment format and the neighborhood rehabilitation format. In the first a "slum" neighborhoodwide demolition of existing structures would be undertaken, and the dislocated inhabitants would be relocated to other neighborhoods. Inasmuch as the original use represented a slum, a slum occupancy on this site was ended, along with its negative externalities. But since the relocated poor received at best minimal aid (mostly informational, as well as reimbursement for involuntary moving expenses),[31] availability of units fell for them and thus real prices of housing rose for them. Market pressures in their relocated locations tended to re-create or worsen slum conditions elsewhere. The discrepancy in quality level (and in relative numbers) between old and new units on the original site was too great to give impetus to increased filtering of existing units to the poor at lower real prices. Thus, because there was neither an emphasis on augmenting the purchasing power of the poor nor on augmenting the net supply of housing units to them, the problem of bad housing was very likely worsened—even though bad units and even bad neighborhoods were eliminated.

Partly to avoid the heavily income regressive impact of the redevelopment approach, an emphasis on large-scale rehabilitation of existing units in poor neighborhoods came to the forefront. In this type of program private rehabilitation would be encouraged by: (1) announcement of a neighborhood as an urban renewal rehabilitation area and thus as an area in which large-scale simultaneous upgrading could be expected, (2) financial subsidization of private rehabilitation actions.

This emphasis differs in at least two major respects from the previous one: (1) The discrepancy between new and old land use in the renewal site is much smaller, and thus relative housing supply dislocations are less severe; (2) in principle the original site population could continue to reside in the same neighborhood and thus the favorable aspects of neighborhood continuity would be preserved.

The observed consequences of this type of program were not determined so much by its intrinsic nature as by historically contingent circumstances. In really bad neighborhoods, the condition of many structures was so bad that only very extensive, very high-cost renovation could raise them to code-acceptable level. But the increased level of rentals required to make such upgrading profitable could not be expected to come from the original population, and higher income groups were not likely to move in unless the neighborhood as a whole were dramatically improved. So a consistent set of new incentives on the part of the presumed participants was not created by the program. Individual supply incentives depended upon either the expectation of widespread similar actions by others or the willingness to embark on single mammoth projects oneself. Few mutually enhancing expectational situations were apparently encountered to warrant the risky upgrading. For owner-occupiers an additional constraint was the modest means of the owners and the absence of a profit objective. The few large rehabilitation projects that operated were hampered by unfamiliar technology and a higher-than-expected required rent increase, thereby creating ill-will with neighborhood inhabitants. Many developers lost money. The overall private supply response has not been encouragingly large.

[31] I speak here of the type of project that was carried out in the major rising phase of the program, before rent allowances for relocatees was added.

An inherent problem in the context of this paper is that while existing units are upgraded, there is no increased supply in the relevant broader quality level and no mechanism for either reducing the real price of adequate housing to the poor or increasing their budgetary power to reach it. Extensive upgrading prices them out of the market (and neighborhood). Thus, even a more substantial private supply of upgrading would not solve the problem of their bad housing. They would very likely relocate, as under area redevelopment, with only slightly less overall regressive impact on housing conditions.

Subsidization of Private Supply

Under this head I shall briefly discuss private supply subsidization programs, regarding both single family ownership units and multiple-unit rental structures.

The intention here was to give financial incentives for an increased private supply of new single family owner-occupier units and multiple-unit structures that could conceivably be reached by low and moderate income groups. The emphasis was on the supply side, and on the supply side of structures, not necessarily of neighborhoods.

In principle, a program of this sort could ease the problem of bad housing by increasing the supply of housing enough to lower housing prices, accelerate downward filtering, and encourage dispersion of the poor out of slum neighborhoods into the filtered units. Direct augmentation of supply options for the poor is less likely.

In fact, the program did have little direct supply effect on the poor. A major part of the units were built at the upper boundaries of cost eligibility. Ownership tenure is difficult for the relevant poor to maintain at best, and at the levels offered they were outside the reach of this population. The rental units were generally too expensive for the poor. Some downward filtering is likely to have occurred, but market barriers may well have curtailed some of this. New units of both types appearing in the suburbs may have led—by the late 1960's—to a linkage of vacancies in no small part in the suburbs rather than in the core city. But the poor—especially nonwhites—could still not penetrate the suburbs easily. So the segmentation of the housing market could prevent interneighborhood mobility and thus dampen the effectiveness of any simple supply supplement program.

In addition, the earlier 221d(3) subsidy program was hampered by an inflation of building costs that pressed upon the upper limits of structure eligibility. The supply response was less than anticipated to subsidies of this magnitude. The later programs used a more powerful, but specialized set of financial incentives for construction. These were most attractive for income tax savings and generated a specialized pattern of financial layering that led to cost-inflation abuses and a minimum passing through of the benefits of subsdization to the user population. Their impetus to downward filtering was thus further diminished.

Thus, while in principle cost-side subsidy programs can mitigate the problem of bad housing, the dollar efficiency of such programs is low because: (1) It rests on downward filtering, (2) this filtering is hindered by incentives to build at too high market value (and rental) levels, (3) it is not aided by an enhanced purchasing power of the poor to lubricate the filtering process, (4) by paying little attention to barriers on interneighborhood market mobility it can dissipate the mobility potential of induced vacancies, and at the same time it fails to channel new building to neighborhoods or political jurisdictions, which would itself ugrade existing poor neighborhoods.

To summarize our brief, and most informal, evaluation of recent Federal housing policies, we argue that there was apparently a neglect to pinpoint the intended goal of policy to the significant multidimensional upgrading of the housing of slum dwellers. This resulted either in perverse real income distribution effects, so that the poor were actually hurt while simply changing some of the locations of slum occupancy; or in programs that produced a variety of substantial gains to producer-financer and nonpoor user groups, and only apparently quite small residual gains to the poor in the form of additional filtered units, because of incentives to build at too high market-value levels and an omission of attention to the neighborhood dimension of improved housing. Such programs display a low goal achievement per dollar ration—poor efficiency.

Alternative Policy Approaches to Housing Goal Achievement

The discussion of the last section already suggests what policy interventions seem warranted. Since the paper is already overlong, these suggestions will simply be made explicit and fleshed out a bit.

Two basic points have been made. Earlier policies, for the most part, do not pinpoint their maximum positive impact on the well-being of slum residents. Some programs seem to accord benefits to that level almost as an afterthought —i.e., through the complex but dampening intersectoral reverberations of the housing market. Others actually have perversely negative welfare impact on the poor. The other point is that the neighborhood dimension of the housing package has not been accorded adequate attention. The incentive problems involved in the private upgrading of existing neighborhoods have not been adequately handled, nor has the existence of real barriers to interneighborhood mobility, with respect to income and especially interracial group interaction.

One potentially effective way to achieve a refocusing onto slum dwellers is to enhance directly the housing purchasing power of this target group and so to help elicit—on its behalf—the adjustive processes of the housing market. Thus, demand-side intervention may well be called for. Two basic forms are available, general income supplementation and rent allowances. The choice between the two cannot be made within the present context, because the former is part of a broader policy of income redistribution while the latter addresses itself to what is special about housing. Of course, dollar for dollar, rent allowances will have the larger housing market impact. Whichever is used, an increase in effective market demand by this group is to be expected. This should have the further effect of attracting housing supplies competitively to these users: both as against other users, and with respect to use of additional resources to provide more housing services (either in current upkeep services or in physical upgrading or in new units). This magnetic pull suggests—but does not guarantee—a large share of the overall program gains to present slum dwellers.

One reason that it does not guarantee anything about the size of the net benefits to this group per program dollar is that the size of these benefits depends strongly on the size and character of the supply response to this additional effective demand in the market. This can vary greatly. The enhanced bargaining power of the recipients is greatest if they can spend their additional desired housing purchasing power in any part of the market they wish. If, however, they are restricted by discrimination or other mobility barriers (e.g., an intense desire to remain in a given ethnic neighborhood), their power is lessened. They may find much of the effect of their additional money demand dissipated in higher rentals and market values in that part of the market to which they are voluntarily or involuntarily attached. Such barriers and attachments do exist. A program that would maximize the effectiveness of its intervention must therefore deal with these additional aspects of the problem.

The above suggests that while demand-side supplementation has attractions, it is likely itself to require supplementation in order to be efficient. Both a supply-side impetus and an improvement of market adjustment seem wanted. This latter calls for direct attention to both interneighborhood mobility barriers and to the pattern of incentives necessary to achieve existing neighborhood upgrading. It is important both to enhance the ability of slum dwellers to move to better neighborhoods and to use their increased money demands within their original neighborhoods to induce considerable neighborhood upgrading there.

Supply-side impetus can, of course, be provided by any of a variety of supply subsidization approaches. What must be understood, however, is that the type of subsidy and especially the quality level sector in which it is applied influence the type and magnitude of supply response that is likely to result. In general, the size of subsidies closer to the ultimate target quality level must be larger to elicit each additional unit of supply, but the ultimate filtering effect of each such unit on the housing opportunities of the target population is greater than subsidies further from the target level. There is a delicate tradeoff, whose magnitudes depend on empirical knowledge about the housing market that researchers have not yet satisfactorily discovered.

The improvement of housing market adjustment is more difficult but no less important. Our constant emphasis on the neighborhood dimension has its branches in this problem. Facilitating neighborhood upgrading calls for efforts to assure that directly implemented additional supply activity in any target neighborhood be on a large enough scale to influence positively the number of individual expectations necessary to ignite the self-fulfilling escalation of private actions. Interneighborhood mobility requires additional legislation, or more vigorous enforcement of existing legislation concerning open occupancy or exclusionary zoning and the like. It may require deft use of contingent rewards and punishments to local jurisdictions in return for approval of even modest opening up of some suburban neighborhoods to poorer—not necessarily the poorest—

residents. This is a complicated subject, and its complications are well beyond the scope of the present paper. But the spirit of this discussion, that explicit attention be devoted to neighborhood aspects of housing, should be amply clear by now.

To conclude this section, what I am arguing is that the goal of public intervention can probably not be efficiently accomplished by a single type of housing policy. What seems called for is a many-sided approach, designed both to aim better on the genuine target and to facilitate those market adjustments that will help rather than—as probably too often in the past—hinder the achievement of the policy goals. Demand-side, supply-side, and market adjustment instrumentalities are needed in a synergistic union.

Summary

This paper has stressed the multidimensionality of the housing package, and how that multidimensionality affects both our understanding of good and bad housing, and the welfare consequences of those conditions. We sketched out the kinds of welfare impact each facet of housing was likely to have. We emphasized that there is an important interplay of housing structure variables like space and condition with one another, and with lot and neighborhood aspects of the housing package, in the overall welfare impact of bad housing. Concentrations of adverse circumstances among the several facets of housing are likely to occur, where population and structure and neighborhood mutually aggravate the negative externalities that impinge on well-being. These are the cases for which government intervention seem most warranted.

We then examined a variety of the empirical evidence that exists to verify and measure the types of welfare impact that we postulated. This evidential record is spotty and inadequate, yet it does seem suggestive of the reality of some of these phenomena.

We discussed the public policy implications of this emphasis on multidimensionality and its welfare impact. It influences the definition of a warranted policy goal as the upgrading of the housing package experiences of slum dwellers —an upgrading that must attend not only to the structure aspects of housing but to the neighborhood and accessibility aspects as well.

This specification of a housing policy goal was employed in briefly evaluating recent Federal housing policies. These are found to be sometimes inconsistent with the goal, sometimes inefficiently organized to achieve it.

A final section drew on the presumed inadequacy of these recent policies to propose some of the elements of an alternative policy approach. It is itself a multifaceted approach. It attempts to pinpoint more directly the ultimate beneficiaries as proposed above, and attempts as well to influence the adjustment processes of the housing market to facilitate rather than offset the achievement of its goals. In this attempt, the nonstructure aspects of housing are seen to require explicit attention.

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Effects of Housing on Mental and Physical Health

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Summary

The review brings together empirical evidence from many disciplines in order to answer the question: What is known about the effects of various physical parameters of housing and of the residential neighborhood on behavior and on mental and physical health? The evidence is discussed and evaluated under six major groupings: Satisfaction with housing and neighborhood, urban ecological analyses, parameters of housing and neighborhood, voluntary rehousing, involuntary relocation, and "proximate environment" and short term reactions.

The conclusions of this review, paradoxically, center on the importance of the social environment. The effects of housing are best documented in those studies where changes in housing precipitate changes in the social environment. Other studies, less plentiful, show the joint action (or interaction) of the housing and the social parameters on health. The least plentiful are studies which document the "pure" effects of housing variables alone on health and behavior. This general conclusion, however, has to be tempered by the realization that, given the complexity of the problem, simplistic study designs tend to yield inconclusive results, and that we need evidence from longitudinal studies in which some of the intervening processes of adaptation to the housing environment are also included and studied in situ.

Introduction and Scope of Review

The major purpose of this report is to review the empirical evidence regarding the effects of various physical parameters of housing on behavior and mental and physical health. A secondary objective is to derive conclusions regarding the probable consequences of changes or improvements in various aspects of housing.

The relevant literature on housing is widely scattered in the professional journals of many disciplines: sociology, social psychology, psychiatry, social medicine, gerontology, public health, and architecture and urban planning. Consequently, different viewpoints, approaches, and methodologies are represented by this literature, which in turn leads to a great variability in the soundness of the evidence and in the degree of relevance for this report. This review, therefore, has to be integrative, evaluative, and critical.

Certain areas of the total literature will be excluded from our consideration: a) the rather extensive animal literature [1–6], a lot of which deals with crowding; b) the so-called "psychiatric architecture" writing [7–12], which is primarily intuitive and speculative (albeit very interesting) material concerned with designing mental hospitals in a way that would mitigate some of the deleterious effects of the institutional setting; and c) the literature on public health standards and recommendations for the residential environment [13–16], where most of the standards, especially those which deal with mental health or psychological well-being, are not based on any empirical evidence, and are phrased in rather vague terminology.

There is also a fairly extensive literature on certain associations between housing and health which are considered too "obvious" to need any empirical proof. This viewpoint is expressed perfectly by the following quotation: "By deductive reasoning, a strong relationship between housing and health can be established" [17]. Some examples of these "obvious" relationships between housing and health might include: presence of rodents and increased probability of rodent bites; presence of stairs and increased probability of injuries due to falls, especially among the elderly and those with poor eyesight [18]; living in old buildings with lead paint and lead poisoning [19]; crowding and incidence of rheumatic fever [20].

While this review will not deal specifically with the validity of these claimed "obvious" relationships—it is organized around evidence, not around unsupported but plausible claims—several points are worth noting. First of all, most of the "obvious" relationships involve health problems with a very specific, and generally simple, causal mechanism, and where a specific corrective action can be taken. Secondly, the trouble with "obvious" relationships is that some are not so obvious as we once thought; for example, it is more plausible to talk of an association between tuberculosis and social isolation [21, 22] than between tuberculosis and crowding. Finally, "obvious" relationships can be strongly modified by host characteristics and various social variables and conditions. For example, in the association between diarrheal diseases and lack of proper sanitary facilities, the habits of the people can be a more important factor than the absence of a privy [23]. And even such an apparently simple parameter as noise has no straightforward effects: Performance decrement due to unpredictable noise is experienced only by those who think they cannot control it but not by those who think they can [24].

Inasmuch as a number of articles have previously reviewed some of the evidence [25–35], this report will build upon these reviews by extending the coverage of the evidence and by bringing it up to date. It must be noted, however, that there is apparently something inherently attractive in the perspective of ecological determinism, because many of the writers of such reviews are sorely tempted to stretch and overinterpret the existing evidence. For example, Schorr [33], in a generally excellent and comprehensive review, makes various undocumented assertions about the effects of slum housing on self-perception, pessimism, and passivity. Thus the reader may find that the conclusions in this report differ considerably from those offered by many of the writers of the earlier reviews.

It is possible to group the relevant studies into six major categories: a) satisfaction with housing and neighborhood, b) urban ecology, c) parameters of housing and neighborhood, d) voluntary rehousing, e) involuntary relocation, and f) "proximate environment" and short term reactions. This categorization is a very rough one and is intended primarily to simplify the presentation and evaluation of the evidence.

Satisfaction with Housing and Neighborhood

It appears to this reviewer that a strong empirical link can be established between characteristics or aspects of the residential environment and satisfaction-dissatisfaction with this environment. For example, studies of sources of satisfaction and of complaints [36–41] suggest that satisfaction with housing is clearly related to size of dwelling and amount of space available, and that crowding and lack of privacy are major sources of dissatisfaction. Complaints about meals, hygiene, sleeping, housework, child care, and leisure are all associated with crowding. The social class of the respondent is clearly an important variable that modifies users' preferences and satisfactions [42]. In general, it has been concluded [38] that higher social groups take for granted the amenities which the lower classes are aspiring to possess. Specific comparisons of residents of slums with working class individuals [43] reveal that for slum residents, satisfactions and dissatisfactions center on basic concerns with safety and space. For working class individuals, their satisfactions and dissatisfactions center on creating a pleasant, cozy, convenient home environment and on living in a "respectable" neighborhood.

There is other evidence [44, 45] which suggests that residents of high crime areas dislike their neighborhood and have a strong desire to move out, especially if they perceive crime and violence as a serious problem. Subsequent actual mobility, however, is only weakly related to concern with crime and violence or dislike for neighborhood, and many of the moves of the more dissatisfied people are made within the same neighborhood only. This inability to translate the desire to move out of a neighborhood into actual residential moves presumably reflects numerous barriers: inadequate finances, unavailability of housing elsewhere, discrimination against minority members, and the fact of having social roots (friendship networks, closeness to work, etc.) in the neighborhood, together with a fear of social isolation in the new place of residence. Removing all of these barriers presumably would allow many more people to move out and thus hasten central city abandonment. Removing only one barrier (e.g., the financial one, via housing allowance) might have only small effects or even paradoxical consequences, such as driving rents up without altering anything else.

It is difficult to assess the relative importance of housing satisfaction vs. neighborhood satisfaction, but in general it has been found that the nature of the dwelling is a more important source of satisfactions and dissatisfactions than is the neighborhood location [40], though the situation appears reversed for elderly subjects [46, 47] and those in high crime areas [45]. However, when basic housing needs are satisfied (as, for example, in the case of a middle class house buyer who can choose among a number of houses, all of which would meet his housing needs), then the quality of the neighborhood becomes the paramount consideration. And we find, interestingly enough, that the social characteristics of neighbors and the level of maintenance in the neighborhood are the chief determinants of satisfaction with neighborhood [40, 48, 49]. Beyond that, an ideal neighborhood is described as spacious, beautiful, good for children, exclusive, having country-like character and being close to nature (in that order of importance) and neighborhood facilities listed as important include a religious building, grocery, bus stop, elementary school, and shopping center [50].

The strong empirical link between housing characteristics and reported satisfaction-dissatisfaction must be carefully interpreted. Firstly, we must be aware of the limitations of the various measures of housing preferences and satisfactions [51]: a) Housing attitudes are related to the housing conditions with which the respondent is familiar and/or to the conditions to which he aspires; b) preferences are not absolute and permanent; c) as some needs are satisfied, other needs become paramount; d) housing attitudes are not based on full information; and e) housing attitudes and satisfactions are more volatile after rehousing. Secondly, we must remind ourselves that in a broader perspective on sources of personal satisfaction and happiness, satisfaction with one's residential environment does not compare in importance with such other sources as family relationship, job satisfaction, and social adjustment [52]. It thus appears that the strong link between residential characteristics and housing dissatisfaction does not take us very far, because we do not know with what it links up at the other end, i.e., we do not really know what are the consequences of differential levels of housing satisfaction. The satisfaction measures are too volatile, their behavioral significance is in question, and their association with physical and mental health is unproven or very weak, at best [45, 52].

Studies of Urban Ecology

The basic strategy of these studies is quite simple and consists of utilizing two sources of data: a) census-type data on characteristics of individuals and of their housing, aggregated or averaged over areas of city such as census tracts; and b) institution or agency data about the frequency and distribution of some disease or social pathology. The data analysis is then oriented toward isolating the differentiating characteristics of census tracts which yield high v. low rates of some disease or pathology. The design is simple and the study is fairly inexpensive, but the price in terms of interpretability of results is a steep one.

The major results of the urban ecology studies (and there is a large number of them) can be summarized as follows: areas of the city characterized by overcrowded living conditions (persons per room), poor housing or low rental value and high rates of several intercorrelated indices of "disorganization" (the percentage of people living alone, the percentage of multiple dwellings, etc.) have yielded higher rates of tuberculosis [53, 54], chronic conditions and cases of disability [55], venereal disease [56], infant mortality [56], juvenile delinquency [57, 58], and hospitalization for psychosis [59–61] (for schizophrenia in particular, but apparently not manic-depression psychosis).

In addition to these findings, many of the studies also demonstrate the importance of the social environment and show its interaction with the built environment. In general, these other studies [22, 58, 61–64] provide support for what has been called the "social fit" or "social homogeneity" hypothesis: Persons with a certain social characteristic, who are living in an area where the characteristic is less common, will have higher rates of pathology (juvenile delinquency, tuberculosis, hospitalization for mental illness) than people with a social characteristic who are living in areas where the characteristic is more common. The social characteristics investigated most often have been race and ethnic origin, but support is also found for age, occupation, and place of birth. All of this is a roundabout way of saying that people are better off among their own. As we shall see below, this has important implications for effects on rehousing and relocation.

In order to paint a fully accurate picture of the findings in these urban ecology studies, one would have to go beyond these generalizations and consider also many finer details, such as exceptions to these general relationships or secular trends. However, such detail is not necessary, since the whole ecological approach leaves one in great doubt just what it is we have learned about housing and health. The only thing we know with certainty from such studies is the geographical concentration of the visible cases of a certain pathology.

The basic problem with the ecological approach is that when one contrasts census tracts which differ on a housing variable (e.g., crowding or general housing quality), one is simultaneously also contrasting all the other variables that are part and parcel of poverty: Race, age, education, work status, family structure, housing, nutrition, medical care habits, attitudes, predispositions, and so on. There is no way to pinpoint the role of housing, and observed differences in rates of mental or physical illness and disability are not interpretable. A good illustration of this difficulty is to list some of the interpretations that have been offered to account for the ecological distribution of rates of hospitalization for schizophrenia: social isolation, mobility, cultural change or cultural conflict, diverse social stresses, psychological frustration, self-selective in- and out-migration, and various "biases" inherent in the social class and cultural correlations of differential detection, diagnosing, and treating of persons with mental health problems.

So my inclination is to dismiss these studies, because from an etiological viewpoint I do not think we can even tell whether the potentially significant etiological variables which might be involved are characteristics of the persons or characteristics of the environment, whether built or social.

It might be noted that the ecological design, while cheaper, represents false economy because it is so difficult to answer etiological questions. But the survey design approach (such as the National Health Survey [65–67] or surveys of the elderly [68]), which is more expensive, has not yielded proportionally more definite data on effects of housing on health, since the various components of poverty are still difficult to disentangle from aspects of poor housing. This whole issue of research design strategies is discussed in a more detailed way at the end of this report.

Studies of Various Parameters of Housing and of Neighborhood

The next category of studies to be considered represents a zeroing in on specific aspects of the residential environment. A good many of them are studies of social interaction and they generally deal with slums and slum residents, and with new housing developments.

The literature on slums is quite interesting because of the evolution of our perceptions of slums. The traditional description of the slum areas of the city in the earlier urban ecology literature has been in terms of a number of interrelated variables reflecting poor housing, high rates of crime-delinquency-disease, and a high proportion of broken families and individuals living alone. The label most frequently applied to this cluster of variables was "social disorganization," a concept which in turn was used to account for the high rates of some pathology.

However, later studies of slum communities [69–74] began to correct this old picture: a) Slums were shown to be well organized, with a good internal social structure; b) the typical slum dwellers were not newcomers or transients, and residential mobility was low; c) slum dwellers liked their neighborhood much better than did dwellers in public housing; and d) they had a strong sense of spatial identity based on extensive networks of interpersonal contacts and overlapping role relationships.

Of course, it is not clear how much validity and generalizability this more-or-less ethnographic description of the slum communities has. For example, is it more applicable to "ethnic slums" [69] than to black ghettos [43]? Moreover, it is clearly a sympathetic description, perhaps a bit nostalgic, and has served the good purpose of undermining some earlier preconceptions about slums. It has also been part of a useful argument against thoughtless, indiscriminate urban renewal.

In the long run, it has served to destroy the investigators' easy confidence in being able to detect and trace the consequences of the physical aspects of slum dwellings. Thus, the social disorganization hypothesis no longer can be applied uncritically; instead, one must determine the types of social controls that are actually present in the slums, and how they may lead to behavior (crime and delinquency) which is considered deviant by the dominant society. Similarly, the social isolation hypothesis as an explanation of high rates of schizophrenia in poverty areas of the city no longer can be accepted uncritically, since it is no longer self-evident either that such isolation is indeed highly prevalent in those areas, or that that form of isolation (as opposed to isolation that comes from rejection by significant others [75]) is truly of etiological significance in schizophrenia.

There are a number of studies which are concerned with social interaction and housing. The interest in this variable derives from the assumption that the quality and quantity of social interaction are central to a person's well-being and mental health. [76]. In studies of social interaction, the two variables of central interest have been physical distance-proximity and social homogeneity-heterogeneity. Now, there is no doubt that increasing physical distance is a powerful factor in reducing contact with relatives and friends [32, 77–79]; this conclusion applies to face-to-face contact as well as to telephone conversations and letters [77]. For example, Rosenberg [79] found that among a group of working class respondents, there was an average of five visits with close kin during the previous week, if they lived within the same block; if the distance was six blocks or more, the average frequency dropped to one visit during the previous week.

In addition to these general findings, there is also evidence that certain persons in particular are more dependent on proximity than others—namely, housewives with children, the old and the infirm, and those of lower social class [78, 80–82]. In one study, [83] for example, the greatest isolation from friends was experienced by older, poor men whose sociodemographic or racial characteristics were different from the dominant characteristics of the local residents of the neighborhood.

When one switches from the studies of social interaction among relatives and existing friends to studies of interaction among new friends, one finds that physical proximity is of importance for initiating contact, but for maintaining contact, one also needs social homogeneity [78, 81, 84–87]. The dimensions along which homogeneity is important are: socioeconomic status and its components, and variables related to the life cycle. Incidentally, these are also the major dimensions that influence individuals' preferences about type of housing and neighborhood. In suburban communities, other dimensions of social homogeneity—such as values about child-rearing, leisure time interests, and general cultural preferences—also may be significant in influencing social interaction [78].

Sometimes, the relevant dimensions of housing are not, strictly speaking, physical distance but "functional distance"—that is, those aspects of the physical layout of the buildings and of the facilities therein which generate passive contact between neighbors. Study of homogeneous populations, such as graduate students, shows that "functional distance" strongly influences friendship formation [88].

What happens when there is physical proximity but a lack of social homogeneity? Several studies [89–92] have looked at this in the context of interracial housing and the consequences for interaction and attitudes. In general, these studies agree that physical proximity between white and black residents leads to more contact, both casual and intimate, and tc more positive attitudes toward blacks, and fewer negative stereotypes about them, among whites. Unfortunately, in these studies it is not quite possible to rule out self-selection: That is, primarily, whites with initially favorable attitudes toward blacks were the ones who might have chosen such interracial housing. It is also interesting to note that the authors of these studies acknowledge the possibility that their findings may not be generalizable to the typical, communitywide housing—partly because of the unmeasured effects of the prestige of the housing authority which, in setting up the interracial housing, appeared to legitimize and support interracial contact. This point emphasizes the difficulty of studying the effects of purely residential dimensions without the intrusion of social variables. And, in fact, a community study of residential contact and attitudes toward blacks [93] did suggest that some forms of prejudice may be stronger the greater the proximity.

Studies of nonhomogeneous populations in other settings, such as planned retirement communities, show that propinquity alone is not sufficient to overcome the influence of socioeconomic status on social interaction and friendship formation, and that obvious stratification takes place [94–96]. One author [81] has also suggested that the combination of physical proximity and social heterogeneity leads to more hostility among neighbors, but the evidence for this is not very compelling.

There is a separate literature on elderly people, and it clearly demonstrates the great importance of physical distance to friends and to various facilities [46, 79, 80, 97]. For example, there is no doubt that distance to grocery and to some form of transportation has an influence on the frequency and type of shopping, which in turn affects the adequacy of nutrition among the aged [98]. Similarly, the decline in church attendance among the elderly—even as their religious feelings and attitudes grow stronger—is largely due to problems of accessibility of the church [99]. Overall, it would appear that among the elderly, morale and happiness are more closely linked to the amount of neighboring and visiting [100, 101] and to perceptions of convenience of location of various facilities, than they are linked for younger people.

Aside from the literature on the elderly, there are also a number of studies on children, since many investigators have been specifically concerned with effects of housing on children and child development. Some reports are clinical case histories [102] which emphasize the deleterious effects of crowding on privacy, consistency of child care, and competition between parents and grandparents. Other reports [26, 103] emphasize selected issues, such as the lack of control parents have over their children when they live in crowded conditions or in high rise apartments. The actual evidence for some of these observations, however, is quite scant. It has been shown that children of preschool age living on upper floors of high rise buildings stay in open fresh air for considerably shorter periods of time and are delayed in motor development [104]. We also find that there is a negative relationship between amount of crowding and total school achievement, but it is quite small once we control for social class and race [105]. In another study, low-rent public housing pupils were compared with controls living in slums [106]. The two groups were initially comparable on age, race, IQ, size of family, family stability, and occupation of head of family. The results revealed that the public housing sample was somewhat superior on grades in reading and arithmetic, and on teachers' ratings of antisocial behavior. Interestingly, there were no differences in performance on standardized reading and arithmetic tests, and the slum sample appeared superior on physical growth and development.

There is an additional study of children [107] which makes an important point. In this study, it was found that physical crowding and lack of privacy per se were not an important influence on school achievement. Rather, it was how the space at home was used; i.e., setting aside time when a particular room was devoted only to quiet pursuits. This study carries an important lesson: We shall keep getting weak relationships between physical aspects of housing and outcome variables, such as health and performance, unless we look at some of the intervening processes, such as how the family uses the facilities and how it has adapted to them.

There are also scattered studies which have examined a variety of other parameters of housing. Some of them have not been able to establish any kind of association, such as between: a) living in one-vs., two-vs., three-apartment tenement houses and morbidity indices as hospital admissions, visits to doctors, and doctors calling at home [108]; b) living in high vs. low rise apartments and visits to surgery or home visits for wives and children of British soldiers [109]; c) living in open-bay vs. closed-bay Air Force barracks and incidence of some common respiratory diseases [110]. The one study which did find significant differences compared families of British soldiers living in flats with those living in houses: Women and children living in flats had considerably higher rates of visits to physicians, especially for respiratory conditions and for "neurotic" complaints [111]. In general, the literature on high rise living [112, 113] cannot as yet support any firm conclusions regarding physical or mental health effects and, in fact, it is not yet clear what aspects of high rise living, if any, may prove to be the crucial operating factors.

Studies of Involuntary Rehousing

The studies examined in this section deal with rehousing which to all appearances was voluntary and sought out, and generally represented some improvement in housing conditions for the movers. None of the studies, however, actually assessed the perceived voluntariness of the residential move, and the distinction between voluntary and involuntary moves is made only by the reviewer so that he can examine the two sets of studies separately (see also the next section).

The kind of study that looks at people moving from one residential environment to another and measures the effects of such a residential change appears to bear a close resemblance to classical experimental design. The ideal here is a longitudinal investigation in which the data are secured before the move and on several occasions after the move, in which a control group is available, and where the allocation of subjects to the rehoused and the control groups is done with a minimum of self-selection bias. As we shall see below, not many studies approach this ideal. Nevertheless, in principle, we should be able to look to these rehousing studies for the best kind of evidence regarding the effects of the residential environment.

There is, however, a serious complication that involves even the best-designed rehousing studies: The rehousing is a change not only in the residential environment, but also in a possibly large number of known and unknown factors as well. Schorr [103], for example, has noted that moves to better housing for poor people frequently are accompanied by segregation, unfamiliar surroundings and unknown new requirements, inadequate schools and police service, rigid and unfriendly management, etc. Often they are also spending more money on rent. A related issue is that rehousing represents to many individuals a major life change which, as the recent developments in psychosomatic medicine suggest [114–117], can be stressful and can have definite health consequences.

The classical study of the effects of voluntary rehousing on health and behavior is that by Wilner and associates [34]. In spite of certain inevitable shortcomings in design, this study remains a model for other investigators to follow. Some 300 rehoused families and 300 control families, both obtained from the files of the Baltimore Housing Authority, were seen approximately 10 times over a period of 3 years, starting when the families to be rehoused were still living in their old residences. The two groups were young black families, and they were initially comparable on major demographic and some health characteristics. However, as the study progressed, some of the families made spontaneous moves of their own, which necessitated their removal from the study, thereby also destroying the comparability of the two groups. Specifically, those rehoused families moving back to poor slum housing and those control families moving on their own to better public housing were removed. These easily may be two processes of selective attrition, both of which favor the rehoused group over the control group in terms of some general dimension of social adjustment-efficacy. For the rehoused families, the major aspects of improved housing included less crowding, better heating and refrigeration, running hot and cold water, screens, garbage disposal, and absence of rodent infestation.

The major findings of the Wilner study may be summarized as follows: (1) On a number of morbidity and disability indices, the rehoused group proved to be somewhat healthier than the controls. But, all in all, the physical health benefits of rehousing were quite small, applied primarily to younger individuals, and were not manifested until some 16 months after the move. (2) In the area of personal and family relations, no differences were found in common family activities, in parental interest in children's activities, in family quarrels, and in assistance to the housewife. The only significant difference was that control families (those who didn't move) reported more difficulty over the children spending too much time away from home. (3) There appeared to be more neighborly activity (casual contact, helping out) among the rehoused families. However, they also complained more about being farther away from facilities and relatives. The rehoused families felt better about the neighborhood as a place to live than did the controls, but they were less likely to call it their "home." (4) Various measures reflecting the psychological state of the respondents (mood, nervousness, general morale, self-esteem, general anxiety) failed to differentiate the two groups. (5) The rehoused group was more likely to "feel better off in life than 5 years ago," but only for housing-related reasons. The rehousing had no effect on the parents' occupational and educational aspirations for the children, on the husbands' job aspirations, or on various self-promotive activities of the adults. (6) On measures of the children's school performance, no differences were found on IQ tests, or arithmetic and reading achievement tests. However, the rehoused children did show better school attendance and were more likely to be promoted at the regular pace.

This set of findings leads one to conclude that the consequences of rehousing were quite modest: Aside from some effects on housing satisfaction and on evaluative perceptions of the neighborhood, very little was found—certainly no effects on mental health or well-being or life goals or aspirations.

Among the other American studies of rehousing, the work of Chapin [118, 119], done in the late 1930's, is frequently quoted in support for all sorts of claims of beneficial effects of rehousing. In fact, when he matched the rehoused families with controls still residing in the slums (waiting-list applicants) on a number of important demographic variables, he was unable to show any differences in morale or general adjustment in a 1-year followup. However, the rehoused families did show a larger gain in social participation and in quality of home furnishings, and showed a reduction in "use overcrowding" (subjecting the living room to different uses).

In addition to the American studies, there are several British studies that deal with rehousing people onto new housing estates that were built in the early 1950's. Unlike the American studies, which showed no mental health effects, the British studies do reveal some effects. Unfortunately, these effects run in all directions and are mutually inconsistent. For example, one study reported no differences, as seen in data obtained from interviews, general practitioners' records, and hospital records [120]; another study [121] reported higher rates of mental health problems in the housing estate sample, using admissions to mental hospitals, general practitioners' consultation rates, and self-reports of complaints; and a third study [122] found the rehoused population better off by some standards (in-patient hospitalizations), no different by others (out-patient psychiatric hospital referrals, reports of nervous symptoms), and sicker by still another (psychiatric conditions treated by general practitioners).

In another area, however, these studies were in substantial agreement. Namely, the move to a housing estate represents a greater physical distance to relatives and old friends, and a sizable reduction in social interaction with them [123–127]. Some authors describe the move as a transition from a closed network of relationships (all friends and kin know each other) to an open network (not all of the contacts are interconnected). The consequences of this breaking of old social ties are many: a) reduced possibility of mutual aid among relatives; b) a more flexible division of labor at home; c) more neighboring and mutual help from new neighbors, even though some of the contact may be quite superficial; and d) spending more time at home and belonging to a greater number of (non-church-related) associations.

In these housing estate studies there was also some evidence of a higher rate of juvenile delinquency and of child guidance clinic consultations among families living on a housing estate [128]. However, this effect is distinctly temporary, and the elevation disappears within 4–5 years of the move. Interestingly, the same study also reports more outdoor play among the housing estate children [124], and conflict within families appears to be somewhat reduced [123].

In the area of satifaction and dissatisfaction, it appeared that families on housing estates were more satisfied with the new dwelling but less satisfied with the housing estate neighborhood and its lack of amenities, especially right after they made the move. Another temporary effect was the increased loneliness among the wives on the new housing estates [126].

There is also a sizable American literature on housing moves to the suburbs [84, 129–133]. The findings here are frequently based on retrospective interviews only with those who moved—which is about the weakest design which can be used. Nevertheless, it can be noted that most of the changes which take place after the move to the suburb are "intended" changes, i.e., the reasons for which the move was made in the first place—increased satisfaction with housing (especially with amount of space), increased social life, etc. There seem to be no effects on mental health, family life, or marital happiness. Some writers [129] have specifically noted that moving to the suburbs does nothing to alter the life style of working class individuals who do not adopt middle class life style. Perhaps the only "unintended" change as a result of the move to the suburb was an increased involvement in local organizations, but this appears true only when the suburban community is a new one [130].

Herbert Gans [134] has summarized the finding as follows: "In short, the community itself does not shape people's ways of life as significantly as has been proposed by ecological and planning theory. The major behavior patterns are determined, rather by the period of the life cycle, and the opportunities and aspirations associated with class position."

The above quotation represents a strong rejection of ecological determinism. Elsewhere, Gans [135] has written about the failure of physical planning, and Blumenfeld [136] has emphasized the social environment and cultural variables at the expense of the physical environment. The point to remember, however, is that such expressions of skepticism regarding the influence of the built (physical) environment are most appropriate when applied to the evidence on moves to suburbs—which is only a small part of the evidence examined in this review.

Housing moves of the elderly also have been studied. In general, we know that the elderly, as a group, are less mobile, less likely to plan or to desire to move, and are less successful in anticipating their mobility behavior [137]. The elderly who are especially unwilling to move out of their neighborhood are those who lived there a long time and who have many friends there [138].

Nevertheless, voluntary rehousing of elderly from slum conditions of poverty and isolation to a new public housing facility can be associated with some striking benefits. One study [139, 140] showed: a) greater life satisfaction, morale, and better feelings about life accomplishments; b) more positive evaluation of health; c) increased membership in social groups and greater enjoyment of activities with others; d) decrease in "lost" time and time spent sleeping; and e) decrease in services they felt they needed.

The above results of studies of rehousing suggest that one group which can experience the most beneficial effects of a substantial improvement in housing are the elderly. The benefits in mental health and well-being of the elderly are better documented than the benefits in physical health. In addition, one may note that because residential moves can have a strong social uprooting effect, the most beneficial effects can be expected among those elderly who seek out and desire such a move, and who are living in relatively isolated social circumstances. As we shall see below, the elderly can show the most disastrous effects when the housing move is forced upon them.

Studies of Involuntary Relocation

The literature on involuntary rehousing falls roughly into one of two categories: a) Institutionalization—the change from community living to institutional living, involving primarily the elderly; and b) enforced change in community residence, primarily associated with urban renewal, highway construction, or condemnation of buildings.

The interest in institutionalization stems partly from the repeated observation [141–144] of high mortality rates of aged subjects within the first year of entering a state hospital, nursing home, or an old-age home. Unfortunately, this consistent observation is difficult to interpret because of the strong possiblity of a self-selection effect, i.e., individuals who are in a seriously debilitated or incapacitated state are largely the ones who get admitted. A couple of studies [141, 145] of mortality of elderly on a waiting list—accepted into an institution but not yet admitted—reveal mortality rates close to the rates within 1 year after admission, and thus appear to support the self-selection interpretation. However, it is also possible that persons placed on a waiting list are under some stress due to anticipation of the impending move to an institution. Thus, the waiting list mortality may not be a good baseline against which to compare institutional mortality.

The clearest, most convincing data come from studies of institutional transfer—mass relocations of elderly subjects from one institution to another, where mortality data before and after the move can be compared. Here we find a definite increase in mortality associated with such an institutional transfer, especially among elderly who were labeled as "depressed" or "psychotic" [146–150]. Because these mass relocations involved comparable or improved institutional housing, the increased mortality cannot be attributed to the purely physical parameters of housing.

It is fascinating to note that in a couple of instances [149, 151], casework service and psychological support were provided for each elderly person. For example, detailed attention was paid to such issues as residents' fear of the unknown, preservation of familiar relationships, retention of familiar belongings, etc. Under such excellently managed relocation programs, the postrelocation death rate was found to be actually slightly lower than the rate at the old institution for the previous year.

In addition to the above evidence, there are also many cross-sectional studies comparing elderly people living in institutions with the elderly living in the community [152, 153]. These studies yield largely ambiguous data, because—short of using a longitudinal design—it is impossible to disentangle the effects of the institutional environment from the effects of self-selection, anticipation, and selective attrition (mortality) during the process of adaptation to the institution.

The literature on involuntary change in a community residence due to urban renewal or highway construction is clearly sufficient to mount an attack on the way Federal and local governments have managed this social problem. For example, it has become clear that slum residents who are relocated, generally pay higher rent without necessarily experiencing better housing [154, 155]. Sometimes they scatter throughout the city [156], but more often they move to adjacent areas where similar housing is available [154, 155]. Because such housing is usually substandard, the relocatees experience additional moves later.

The largest impact of relocation is due to the uprooting of existing social networks, as is well demonstrated in the study of relocation of West End Boston [157, 158]. Fried reports that even 2 years after relocation, over 40 percent of the sample gave evidence of fairly severe grief reaction. Such a grief reaction was especially likely among those who had a strong prerelocation commitment to the area, who knew a great part of the neighborhood, who had a great number of close friends in the area, and who had positive feelings about their neighbors. The grief reaction, and the associated variables, were also predictive of poor adjustment-adaptation to the new neighborhood. In addition, poor adjustment was likely if the respondents were low on educational and occupational status and first-generation American, had a poor knowledge of Boston other than West End, and had had no plans to move out of West End.

There is also extensive literature dealing specifically with relocation of the elderly [152, 159]. The relocated elderly are generally those who have been less mobile and who have lived in the old neighborhood longer than the average person. For the elderly, the move frequently represents an added financial hardship because their economic circumstances are already quite precarious. The old neighborhood which they are forced to leave has two major advantages for which the better housing conditions of the new location cannot adequately compensate—the extensive friendship ties and the convenience to many facilities (grocery, drugstore, church, transportation, etc.).

The social ties to the old neighborhood are a particularly strong impediment, and the stronger the ties, the more dissatisfied are they with the new neighborhood [138] and the more severe is their grief reaction [157]. Those who are able to maintain old contacts with friends from the old neighborhood show the least emotional distress. The loss of friends creates not only loneliness but also a certain amount of insecurity, inasmuch as the elderly depend partly upon their friends for help in case of some emergency [160]. It is also worth emphasizing that among all age groups, the elderly appear to be the most vulnerable to the adverse effects of the involuntary relocation: Kay [161], for example, found more intense depression, sadness, and negative feelings among older persons who were forced to move because of urban renewal or highway construction.

The Evidence from Environmental Psychology

The last category of evidence to be examined is based on studies of the "proximate environment and short term reactions." The hope is that in considering these types of studies we may understand better some of the intervening processes that mediate the influence of the built environment on health and behavior. The approach here is clearly more microscopic than in the previous studies: The focus is on the short range interaction of a person with some (limited) aspects of the build environment.

In spite of the fact that the field of environmental psychology (ecological psychology) is a rapidly expanding one [162–165], its contribution to the evidence relevant specifically to the concerns of this paper is disappointing and limited. For example, from these studies we learn how verbal interaction between patients on a geriatric ward or in a mental hospital can be increased by manipulating the furniture and the decor [166]. Or we learn how the seating arrangement of persons around a table affects interaction [167], and how a discussion group is affected by the presence of a designated leader and when it is leaderless [168]. And we can find out about the seating arrangements of individuals seeking privacy in a library [169]. But we are still in the dark about how different members of a family seek privacy in their home or apartment, what are the different ways (short term and long term) of coping with lack of privacy, and what are the tradeoffs and consequences of the different modes of coping. Nor do we know how the various arrangements of rooms and of furniture affect social interaction in the family and with others, and what is the quality and quantity of such interaction. In short, what is needed are studies carried out specifically in the residential setting (in situ). Studies done in the social scientist's laboratory, or in selected public places, or in institutions, have limited generalizability, because in those settings the individuals have a minimum opportunity to modify or alter the built environment, only to react to it. And the observation period in such studies is usually so brief that we can only talk about short term reactions, not long term accommodations.

Some Conclusions and Implications

Inasmuch as the present report is already a major distillation of the evidence on housing and health, any additional summarizing of this literature can be made only at the price of some oversimplification. Aside from this disclaimer, however, the following conclusions appear defensible:

First, the link between parameters of housing and satisfaction is a strong one, especially when it involves such components as amount of space, comfort and amenities in the dwelling, and facilities and safety in the neighborhood. The major issue here is how to view the housing satisfaction variable. We can see it as an important aspect of well-being, as a significant indicator of quality of life, i.e., as an outcome variable in its own right. Or we can treat it as an intermediate variable, only in its relation to the "real" outcome variables, such as physical and mental health. In this latter view, housing satisfaction has an unproven link with physical health and a weak association with mental health. In neither case must we forget that housing satisfaction indices are sensitive to the person's present living conditions as well as his housing aspirations—i.e., they reflect, partly, his state of adaptation to his housing. It is also likely that housing satisfaction has motivational properties and relates to such behaviors as residential mobility or destructiveness of public housing property.

Second, the link between parameters of housing and social interaction is also a strong one, albeit somewhat more complex. Studies of slums clearly show that substandard housing does not preclude the existence of rich social networks with plentiful social interaction, mutual help, and social control. Studies of rehousing and relocation suggest that the disruption of social networks may be the most significant effect against which the possible benefits of improved housing must be weighed. Vulnerable segments of the society, such as the elderly, may be particularly affected because they are not as able to maintain old social ties (in the face of relocation) or to form new ones. Studies of physical proximity show that the amount of social interaction is correlated with this dimension, and that in homogeneous populations propinquity and friendship formation are associated. In heterogeneous populations, housing proximity is probably not enough to overcome social class barriers, although certain attitudinal changes may take place.

The variable of social interaction may again be viewed in two ways—as an outcome variable in itself, or as a link to physical and mental health. From the latter view, social interaction and physical health probably do not have any direct linkage, but potentially have many indirect links via social support and medical care. For example, in a group of low income mothers, inadequate antepartum and postpartum care was related to various factors reflecting low social support, such as being unmarried, experiencing frequent residential moves, and having to manage a household with a newborn without help [170]. A study of men who experienced their first myocardial infarction showed that they typically are almost exclusively dependent on family, friends, and relatives for medical care [171]. And a study of response to physical rehabilitation showed that persons living alone have a considerably poorer response [172]. The link between social interaction and diverse indices of well-being and mental health is a reasonably well established one [100, 101, 173, 174], in the correlational sense. However, the direction of causality is not clear, and such correlations do not establish that social interaction contributes to mental health. But the results from longitudinal studies, relating changes in social involvement with changes in life satisfaction and morale [175–177], suggest that this may be the case and that being able to maintain stable activity patterns contributes to mental health [178].

Third, the link between parameters of housing and indices of physical health has not been well supported by the reviewed evidence, at least not in any direct sense. To be sure, certain relationships involving simple causal mechanisms—presence of rodents and probability of rodent bites, presence of lead paint in old buildings and probability of lead poisoning in young children—do exist, or are highly plausible. But the relationship between housing and chronic conditions and disability is not at present supported by any firm evidence, and it would seem that any association which may be established will be shown to operate via social variables.

Fourth, the association between housing and mental health (excluding housing satisfaction) is supported only by the weakest, most ambiguous studies using the urban area analysis approach. The best designed studies do not demonstrate any mental health benefits, and it now appears that some of our most cherished hopes—such as raising educational and occupational aspirations by moving people out of slums—never will be realized. However, since there are many studies suggesting that rehousing may be a severe social uprooting experience, accompanied by adverse mental health effects, it is thus still possible that once we can separate cleanly the adverse effects of rehousing via the social uprooting, the purely physical aspects of improved housing will be shown to have some mental health benefits after all.

Fifth, the findings on children reveal some direct effects of housing on such behavior as indoor vs. outdoor play, and some modest influence on the more "social" aspects of scholastic achievement (attendance, teachers' ratings, promotion through the grades), but no effects on achievement measured by standardized tests.

Needed Future Studies

The above summary of evidence for housing effects is very likely an underestimate of the true amount of influence of housing, for the following reason: Most of the effects of housing on health and behavior are probably complex and are mediated by various social (and perhaps physiological) processes of reaction, adaptation, and accommodation to the housing environment. Thus, in order to detect these effects, we need more comprehensive studies which not only relate the distal independent and dependent variables (housing and health), but are also concerned with the whole matrix of intervening processes. Since such studies so far have been quite rare, we may suppose that the true story of housing effects has not yet been told.

Figure 1 represents a schematic outline of the types of variables that seem relevant in the total causal chain that links the built environment to health and behavior. The presumed causal sequence progresses from left to right: The influence of the objective environment (both physical and social) is believed to operate through the subjective (perceived) environment, to short term (proximate) behavioral reactions and mediating processes, and on to long term (distal) outcome variables. Moreover, each step in this presumed causal chain can be influenced by various characteristics of the person. And even though the diagram is already cluttered, it is still only a limited representation of the complexity of the whole set of variables involved. For example, there are no feedback loops to illustrate how proximate reactions or distal outcomes can, in turn, modify the objective or the subjective environment.

In short, Figure 1 is a schema that invites the reader to view the complex problem of effects of residential environment on health and behavior from a certain perspective, which may prove useful in our attempts to answer the many questions which still must be raised: How do we conceptualize the environment and the way it operates to influence behavior? What aspects of the residential environment in particular can influence behavior? How can we understand "nonconforming" usage and the distinction between "potential" environment (the way it was built

Figure 1. Classes of Variables in a Comprehensive Study of Health and Behavioral Effects of the Built Environment

Conditioning Variables in the Person

Demographic	Cultural-Subcultural	Stable Personality
Age, sex, race Marital staus Stage of life cycle Educ-occup-income Residential mobility	Religion & religiosity Ethnic-racial Extended family kin contact Values about "deviant" behavior	Coping styles Flexibility-rigidity Behavioral habit patterns Needs & aspirations Internal-external orientation

Objective Environment	Subjective (perceived) Environment	Proximate Reactions	Mediating Processes	Distal Outcome Variable
Physical Environment Dimensions & characteristics of dwelling unit Distance to facilities Characteristics of neighborhood (spatial, circulation, ambient, visual, symbolic) Social Environment Presence of relatives & friends Sociodemographic homogeneity of neighborhood, its stability, and social similarity of residents to neighbors Crimes against people & property Indices of "disorganization"	Perceptions & evaluations of: crowding, privacy convenience to facilities pollution noise General satisfaction with housing & neighborhood Desire to move out Perception & evaluations of: closeness to kin & friends sense of social support similarity of neighbors dangers & threats in neighborhood instability & unpredictability of neighborhood	Variations in use of space Behavioral adaptations Coping behaviors Daily patterns of living Interpersonal behavior Leisure time activities	Biochemical and physiological blood pressure pulse rate lipids glucose clotting time plasma cortisol Affective anxiety-tension depression anger-irritation life satisfaction anomie symptoms & complaints	Disease states Impairment & disability Illness & sick role behavior Social deviance Role performance (effectiveness & competence) Addictions Marital adjustment

and "effective" environment (the way it is used)? How do we separate the physical factors from the social factors in the overall way the residential environment affects people? What are the goals which planners and builders are trying to achieve and how do the various aspects of the built environment promote or hinder such goals? What are the needs of individuals vis-a-vis the residential environment? What is the best way to understand the congruence or fit between characteristics of the person and of the specific environment in which he is living?

On the other hand, Figure 1 is of no help to us in setting up better research designs: It is too immense and too complex to represent the objectives of a single study, and it ignores the practical difficulties of conducting housing research in situ. These research design issues have to be addressed separately.

Better designed studies of housing should be strong in one or more of the following respects: (1) It should permit before-after comparisons and, even better, permit a distinction between short term and long term changes. (2) Permit some handle on the problem of self-selection, i.e., the lack of initial equivalence between the group of individuals who are exposed to some residential environment (which is under study) and those who are not. (3) Devote some effort to studying the intervening behavioral processes through which the effects of the residential environment can be traced, particularly the proximal reactions to the residential environment and the actual use to which it is subjected. (4) Include a consideration of selected social-psychological variables, such as those which characterize the social support system and the interactions of the individuals, or those which characterize the sociodemographic similarity between the individual and his neighbors. In addition to these design issues, there is also a great need for investigators to be sensitive to the total social milieu or setting in which the problem they are investigating is embedded. For example, moves to better housing for poor people may represent not only the intended change in residential environment, but also such unintended changes as increased social segregation, greater unfamiliarity with rules and regulations, greater social distance between tenants and management, etc.

There would seem to be three compromise research design strategies which combine feasibility with a certain amount of promise of advancing our state of knowledge. One is a cross-sectional design that compares individuals living in residential environments which differ from each other in some significant aspect, such as high rise vs. low rise. The crucial stipulation here, however, is that the individuals living in these different residential environments be unusually comparable in all important respects (e.g., socioeconomic status, racial-ethnic background, stage of life cycle, etc.) and that, moreover, the way they came to live in one kind of a residential environment or another had little to do with their own choices and preferences. Admittedly, the opportunities for carrying out such a study will not occur frequently, but they do exist. For example, two comparable communities may have built similar low cost public housing which differs in some important respect—the housing may be located in the center of one community and at the outskirts of the other. If the housing draws on similar clients and if the clients differ basically only in that they were born and raised in one community or the other, then we have a good compromise design that can yield some useful information.

The second kind of design is best conceived at the point where the planner and the builder are contemplating the introduction of some variation in design within one housing development complex. For example, the selective introduction of indoor nursery-like facilities into some but not all of the buildings in the complex can lead to a good study of the effects of such a facility on child development, mothers' life satisfaction and leisure activities (especially social interaction with other tenants), development of as sense of cohesion and community among neighbors which, in turn, may lead to group action, such as the setting up of a true daycare center. However, such a study must be planned from the start, since it requires near-random assignment of tenants to the housing and since, in general, it calls for great sensitivity in anticipating the various unexpected consequences of such a differential in facilities.

The third approach is represented by the strategy of designing longitudinal studies around "natural experiments," i.e., changes in the residential environment that are planned and predictable, especially those that involve some governmental action calling for program evaluation. These "natural experiments" could involve such events as institutional transfer of the elderly, urban renewal and rehousing of residents, introduction (or closing down) of some commercial or recreational facility in a neighborhood, and building low income housing in high income suburban neighborhoods. In these kinds of studies, self-selection may remain a problem, but they are very useful because they allow before-after comparisons and because they can provide valuable evaluation data on consequences of programs to which a governmental agency is already committed but which are subject to modification.

In the long run, the major point to emphasize is that no intervention that involves housing can ever afford to neglect the social matrix within which housing is firmly embedded. It is a safe rule of thumb to assume that the physical aspects of the residential environment always interact with social-psychological variables. Housing intervention is also a major social intervention. This emphasis on the social matrix of housing parameters leads to many questions which, ultimately, can be answered only by joining actual interventions with evaluation studies. Under what conditions is it preferable to renovate existing housing in a given community, rather than offering the residents scattered public housing elsewhere? What individual counseling and social services are needed when elderly persons are placed in public housing for the elderly, and what services must such housing offer in the immediate vicinity? Are there strong individual differences in housing needs and preferences among the underpriviledged or the elderly, so that a serious effort should be made to construct a variety of public housing and to selectively screen and place individuals within these? Can we create a sense of ownership and of community (strong social ties, mutual helping, participation in management) in large complexes of high rise public housing, and will this prevent the rapid physical degradation and destruction of the buildings and property that so often take place?

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A Rationale for Government Intervention in Housing: Housing as a "Merit Good"

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Summary

There are a number of plausible rationales for government intervention into private markets. Among these is the rationale that certain goods are so meritorious that they should be publicly provided or subsidized. Such goods are called merit goods, and housing is frequently thought to be an example.

It is seen that the idea of merit good is most fruitfully treated as a positive consumption externality, i.e., a good that confers benefits on other than those directly consuming it. The existence of such goods gives rise to the need for transfers in kind for the purpose of achieving the most efficient use of resources.

Whether or not consumption externalities exist and in what magnitude are difficult empirical questions. Although there now apparently exists a theoretically sound method for answering these questions, the method has not yet been applied to housing (or for that matter to any other specific good or service). Nevertheless, some empirical work relevant to the issue has been performed for housing. This work indicates that consumption-externality benefits must be at least as large as 10 to 15 percent of the public subsidy to ensure that certain existing housing programs are efficient uses of resources. Whether or not present housing programs produce this much in consumption externalities is unknown.

If in fact consumption-externaltity benefits are created by housing, then the case for subsidized housing programs is strengthened and the case for cash transfers is weakened.

Nevertheless, there is still the problem of the appropriate form of the inkind transfer. It is argued in the text that housing transfers should take the form of rent certificates rather than some other form such as public housing projects, interest rate subsidies, rent control, and so forth.

If in fact consumption-externality benefits are not created by housing, then the case for subsidized housing, in whatever form, is weakened and the case for cash transfers is strengthened. There are other factors favoring cash transfers as well.

Consequently, we conclude that if housing is a merit good, it should be subsidized via rent certificates. If it is not, then housing should not be specifically subsidized; rather whatever transfers are justified should be in cash. Which of these cases is appropriate in the United States today is an empirical question not yet answered.

The Rationale for Government Intervention in Private Markets: General[1]

One of the greatest achievements of economic theory has been the elucidation of the conditions under which competitive markets produce efficient resource use. Although the idea dates back at least to the time of Adam Smith, it was not until fairly recently that the conditions under which the theorem holds were satisfactorily worked out.[2]

Two propositions about competitive markets are of special importance for our purposes: (1) a competitive equilibrium is efficient, and (2) any efficient allocation of resources can be achieved by competitive markets, given a suitable reallocation of initial resources. These characteristics of competitive markets provide a rationale for decentralized decisionmaking by individuals and firms without government intervention. This is basically Adam Smith's "invisible hand." Private self-interest on the part of consumers and producers in a competitive environment results in the best use of scarce resources. Also, if we can decide on some socially desired distribution of incomes and a mechanism for attaining it, then the competitive market can be used to obtain an efficient allocation of resources consistent with the desired distribution of income. This means decisions regarding equity can be separated

[1] This section draws heavily on the author's paper, "The Economic Rationale for Transportation Planning," in J. S. DeSalvo (ed.), *Perspectives on Regional Transportation Planning* (Lexington: D. C. Heath, 1973) pp. 21–89.

[2] The most complete presentation is found in G. Debreu, *Theory of Value: An Axiomatic Analysis of Economic Equilibrium* (New York: Wiley, 1959).

from the efficient operation of an economy; the latter can be left to private competitive markets.

These propositions provide the intellectual rationale for private enterprise operating through competitive markets. Nevertheless, these powerful propositions are based on certain assumptions that may not hold for particular economies. When they do not hold, the basic propositions justifying decentralized decisionmaking no longer hold, and there is a need for some kind of collective decisionmaking designed to produce efficiency.

Competitive markets may fail to be economically efficient for a number of reasons, and, of course, there is no presumption that noncompetitive markets will be efficient. Hence, there are two broad issues with which to deal. The first concerns those factors that prevent otherwise competitive markets from achieving efficiency. The second concerns noncompetitive market structures.

Since competitive markets are so important to the efficient operation of a decentralized economy, the first question one might raise is whether or not such markets can in fact work. It turns out a competitive equilibrium depends on the absence of increasing returns to scale large relative to the market.[3] The existence of scale economies large relative to the market may not permit the operations of competitive markets, for the firm would be induced to expand its production until it was one of a few firms or the only firm occupying the market. However, if only one or a few firms operated in a single market, each would have some control over price. Such "high concentration" would violate the requirement for competition that specifies no control over price.

Thus, the absence of increasing returns large relative to the market means that a competitive equilibrium is possible. There are, however, other conditions that may not permit such a competitive equilibrium to be efficient. Perhaps the most important of these is externalities.[4]

Externalities are interdependencies among economic units for which no market exists. These interdependencies are a barrier to achieving economic efficiency because there is no market mechanism to value them. The smoke emitted by the steel manufacturer may increase the cleaning bills of neighboring households, but the producer does not perceive this cost. Hence, the social cost of steel production is greater than the private cost. If it were possible to make the producer bear the full social cost of his output, the production of steel (and consequently smoke) would be less. In fact, the amounts of these products would be optimal in the sense of efficient resource use. Where there exists no way of "internalizing" externalities, the private competitive market will result in inefficient resource use.

Aside from increasing returns, where competition may not exist, and externalities, where if competition exists it cannot be efficient, there is a special kind of commodity that the market may not produce in appropriate amounts. This kind of commodity is called a public good (also called a collective or social good). It is a good that can be consumed by more than one person at the same time at no extra expense, and it actually costs something to exclude potential consumers.[5]

When an ordinary commodity is consumed, the units consumed are thereby denied to others. For public goods, however, it may be impossible or very costly to exclude people from consumption. In those instances where the cost of exclusion exceeds the gain, private enterprise will not produce the good, even though it may be desired by consumers, because consumers cannot be made to pay their fair share for its provision. Thus, in an economy with a demand for public goods, these demands may not be satisfied by private enterprise even when competitive markets prevail. There is therefore a possible role for collective action in the provision of such goods.

Implicit in the definition of a competitive market are certainty and complete information on the parts of buyers and sellers. Uncertainty, a lack of knowledge of which state of nature will prevail in the future, is not in and of itself inconsistent with competition. People can make contracts contingent on the occurrence of certain possible outcomes. Insurance is an example of

[3] See M. J. Farrell, "The Convexity Assumption in the Theory of Competitive Markets," *Journal of Political Economy,* Vol. 67, No. 4, Aug. 1959, pp. 377–391; J. Rothenberg, "Non-Convexity, Aggregation, and Pareto Optimality," *Journal of Political Economy,* Vol. 68, No. 5, Oct. 1960, pp. 435–468; R. M. Starr, "Quasi-Equilibria in Markets with Non-Convex Preferences," *Econometrica,* Vol. 37, No. 1, Jan. 1969, pp. 25–38.

[4] The classical discussion of externalities may be found in A. C. Pigou, *The Economics of Welfare,* 4th ed. (London: Macmillan, 1932), Part 2, Ch. 9.

[5] The implications of the existence of such goods for attainment of efficiency by private markets were presented by Samuelson in three articles: P. A. Samuelson, "Aspects of Public Expenditure Theories," *Review of Economics and Statistics,* Vol. 40, No. 4, Nov. 1958, pp. 332–338; P. A. Samuelson, "Diagrammatic Exposition of a Theory of Public Expenditure," *Review of Economics and Statistics,* Vol. 37, No. 4, Nov. 1955, pp. 350–356; P. A. Samuelson, "The Pure Theory of Public Expenditure," *Review of Economics and Statistics,* Vol. 36, No. 4, Nov. 1954, pp. 387–389. The definition used here is adapted from R. N. McKean, *Public Spending* (New York: McGraw-Hill, 1968).

this kind of contract; common stocks may also be an example. It is not, therefore, uncertainty itself that is inimical to competitive markets or efficiency.[6] This is true, however, only when the events insured are not controllable by individual behavior. There are, of course, situations in which the fact of insurance affects the insured's behavior (called "moral hazard" in the insurance literature). An example is hospitalization insurance, where the insured will tend to spend more on hospital services than he would if uninsured. In such cases competitive markets result in overconsumption, since the price paid by the consumer is artificially low. Inefficiencies may therefore occur in otherwise competitive markets because of uncertainty.[7]

Apart from uncertainty about states of the world, lack of information itself leads to inefficiency. Participants in the economic system are assumed to have full knowledge of prices and availability of commodities and factor inputs. Clearly, this assumption does not hold in the real world. It is approximated in many situations (for example, commodities that are repeatedly purchased) but not in others (for example, the one-time purchase of a durable consumption item). Where there is incomplete information, there is no reason to believe the market outcome will be efficient.

The previous discussion has dealt with the assumptions underlying competitive equilibrium and with the other conditions that, although not inconsistent with competition, result in inefficiency. Now, there is no presumption that noncompetitive market structures will be efficient.

Seller concentration is the primary characteristic of imperfect markets, the extreme being monopoly but with gradations from monopolistic competition to oligopoly. The inefficiency resulting from these market forms manifests itself in higher prices and smaller outputs than would result under competitive organization.[8] Whatever the particular cause of concentration (economies of scale; product differentiation; or barriers to entry, such as patent controls, monopolistic resource ownership, pricing to discourage or prevent entry of new firms, and strong stable buyer preferences)[9] and whatever the degree of concentration, the allocation of resources through these markets will be inefficient. To the extent that market forces do not themselves tend to mitigate these noncompetitive conditions, there is a role for government in this area.

In summary, we can safely say there are a number of reasons why a market economy may not achieve efficient utilization of resources. In otherwise competitive markets, externalities, public goods, uncertainty, and incomplete information render the market solution inefficient. With these factors absent, increasing returns and noncompetitive markets in general render the competitive market solution inoperative, the resulting market solution being inefficient. Hence, the powerful forces of the invisible hand are stymied when certain conditions prevail. The case for decentralized decisionmaking is weakened, and the case for governmental intervention is strengthened. Whether and to what extent these inefficiency-producing conditions are present in particular markets is an empirical question. What to do about them if present is partly a theoretical question and partly an empirical question.

The preceding has been concerned with efficient resource use and the conditions for which there exists a rationale for government intervention into private markets for the sake of efficiency. There is, however, another major reason for government, and that is to affect the distribution of income in socially desired ways. In other words, efficiency in the use of resources does not necessarily imply equity in their distribution. It was noted earlier that, when competitive markets exist, any desired distribution of resources can be attained by such markets, given a suitable reallocation of initial resources. Consequently, even if all the requisite conditions for the operation of competition were fulfilled, there might be a rationale for government intervention to attain the socially desired distribution of income. Whether there is a socially desired distribution of income different from that produced by a competitive economy and, if there is, how to achieve it are difficult questions that are partly theoretical and partly empirical.

We shall return to the issues of efficiency and equity later in the context of housing. We now turn, however, to a rationale for government

[6] For proofs that this type of uncertainty is consistent with efficiency and decentralized competitive markets, see K. J. Arrow, "The Role of Securities In the Optimal Allocation of Risk Bearing," *Review of Economic Studies*, Vol. 31(2), No. 86, April 1964, pp. 91–96; and R. Radner, "Competitive Equilibrium under Uncertainty," *Econometrica*, Vol. 36, No. 1, Jan. 1968, pp. 31–58.

[7] See K. J. Arrow, "The Economics of Moral Hazard: Further Comment," *American Economic Review*, Vol. 38, No. 3, Part 1, June 1968, pp. 537–539.

[8] See any intermediate microtheory text, e.g., E. Mansfield, *Micro-Economics: Theory and Applications* (New York: Norton, 1970), pp. 268–270, 299–300, 329–330.

[9] For a discussion of factors facilitating concentration, see J. S. Bain, *Industrial Organization* (New York: Wiley, 1959).

intervention that has not yet been discussed here, the concept of "merit goods." This particular rationale gets separate treatment for two reasons. First, on the face of things, it appears particularly relevant to a study of transfer programs such as those for housing and has frequently been used as a justification for such programs. Second, there is some question whether it is in fact different from some of those rationales discussed earlier.

The Rationale for Government Intervention in Private Markets: The Case of "Merit Goods"

In his textbook, *The Theory of Public Finance,* Richard Musgrave introduces an additional rationale for government intervention into private markets. This rationale is based on the need to satisfy "merit wants." There are wants that are satisfied in part by the private market but not in socially appropriate amounts. According to Musgrave, these include such wants as housing and education. They are merit wants "if considered so meritorious that their satisfaction is provided through the public budget, over and above what is provided for through the market and paid for by private buyers."[10]

Merit wants should be publicly subsidized (or penalized) because some people will spend either "too much" or "too little" on them. People will not live in adequate housing or provide enough education for their children because they prefer to spend their incomes on other items. Consequently, it is in the public interest and is a government function to induce people to consume appropriate amounts of merit goods through subsidy and taxation.

This is an appealing idea and one that has been used to justify governmental intervention for many years. However, Musgrave has difficulty with the concept on two grounds. First, he cannot reconcile the analysis of merit goods with that of public goods.

> The satisfaction of merit wants cannot be explained in the same terms as the satisfaction of social wants. While both are public wants in that they are provided for through the public budget, different principles apply. Social wants constitute a special problem because the same amount must be consumed by all, with all the difficulties to which this gives rise. Otherwise, the satisfaction of social wants falls within the realm of consumer sovereignty, as does the satisfaction of private wants. The satisfaction of merit wants, by its very nature, involves interference with consumer preferences.[11]

[10] R. A. Musgrave, *The Theory of Public Finance* (New York: McGraw-Hill, 1959), p. 13.
[11] Ibid.

Second, he is concerned about the appropriateness of including merit wants "in a normative theory of public economy, based on the premise of individual preference in a democratic society."[12] In his analysis, the individual is the basic decision unit of society (he rejects an organic theory of the state); hence, he is decidedly uncomfortable with the concept of merit want that seems to require interference with individual preferences.

As a consequence of these twin concerns, Musgrave, for all practical purposes, abandons the concept of merit wants. He maintains "that the merit-want situation is not so frequent as is sometimes assumed; the case at closer inspection frequently proves to be one of social want." He also claims "that a full theory of the public household requires multiple explanation. The allocation-branch problem [i.e., those aspects of the public budget dealing with allocation of resources] posed by social (or mixed social-private) wants is more amenable to economic analysis than that posed by merit wants . . ."[13]

A decade later (1969), Musgrave was still concerned with these issues, except that now he was ready to propose a reconciliation. In fact, he proposed two possible ways to reconcile his concept of merit want with social wants (i.e., the demands giving rise to public goods) and with an individualistic normative theory of public economy.

> A possible reconciliation may be obtained by granting that rational individual choice requires acquaintance with alternatives and that experimentation (even though it may involve imposed choice on a temporary basis) may be needed to obtain the necessary information. Temporary use of imposed choice may also be justified as an aid to the learning process. Then, what appears to be imposed choice may be compatible, in the longer run, with the objective of intelligent free choice. This, however, is a somewhat uneasy position to one who may deplore the poor taste of the "public," but would rather persuade than force them to choose otherwise. Yet, it is not without some validity in the realities of the social framework.
>
> An alternative possibility of reconciliation emerges along these lines: Many of the phenomena which appear to be of the merit good type can actually be explained by interdependence of utilities. . . . In other words, A derives a utility from his own consumption of Y, but he also derives a utility (though of a different kind) from B's consumption of Y. This, in fact, is a quite widespread attitude regarding the consumption of basic commodities, e.g., minimum requirements of food, shelter, health, and so forth. The social philosophy of Western society appears to be such that the freedom to tolerate inequality in the distribution of luxury consumption and saving is purchased at the cost of earmarked (specific) subsidies which assure equality in the consumption of necessities. Looked at in terms of this double standard, subsidies in kind, especially to low income

[12] Ibid.
[13] Ibid., p. 89.

groups, make sense; and what appeared to be the wholly different phenomena of merit wants may be incorporated into a subjective preference theory.[14]

In the first paragraph quoted, Musgrave is saying that some people do not spend their money wisely. At first he seems to think this is a technical defect that can be corrected through acquaintance with alternatives, experimentation, and temporarily imposed choices. Yet toward the end of the quoted paragraph, Musgrave realizes that this view is really a value judgment: It involves one person's opinion of how another should act. But, if this is so, the first reconciliation is no different in principle from the second; they both involve utility interdependence.

There may, however, be some validity to the "technical inefficiency of expenditures" argument. In standard consumer-choice theory, there is no concept of inefficiency in a person's expenditure of his income. He is assumed to obtain maximum satisfaction from consumption subject to the constraint of his income level and given prices of the goods he buys. Efficiency in expenditure is therefore implicitly assumed. Recently, however, Kelvin Lancaster has provided a theory of consumer choice that does not implicitly require efficiency in consumer expenditure.[15] It might, therefore, be possible to interpret Musgrave's idea of inefficiency in expenditures and its relation to merit goods in terms of Lancaster's theory. This has not been done however. Lancaster's theory is still fairly new and, although applications are beginning to appear, it has not yet displaced the standard theory.

Thus, in terms of the standard theory of consumer choice, it would appear that the only meaningful way to make sense out of the merit good concept is as a consumption externality. In the next section, we present an exposition of this approach.

The Theory of Transfers

The traditional treatment of transfers in theoretical welfare economics has been through the device of a social welfare function.[16] This function, though it can be more general, is usually of the individualist variety. That is, a social welfare function indicates that society's well-being depends on the well-being of its constituent members. It is further assumed that if one person is made better off, in terms of his own preferences, and no one is made worse off, then society is made better off.

Given an initial distribution of resources among society's members, competitive markets will produce an efficient use of these resources. Such an efficient distribution of resources need not be a socially most-desired distribution of resources. It can be shown that an economy can produce an infinite number of efficient resource allocations, only one of which is the competitive market allocation. Hence if it were possible to judge society's welfare in terms of these efficient allocations, society could pick the one most preferred. This is exactly the role of a social welfare function in theoretical welfare economics.

One of the fundamental theorems of welfare economics is that given an initial reallocation of resources, competitive markets can attain the socially preferred allocation efficiently. In other words, if society can decide on a most preferred distribution of income and a mechanism for attaining it, the rest can be left to competitive markets. Given that the present distribution of resources is not socially optimal, then transfers of resources from some people to other people must take place in order to achieve that social optimum.

Theoretical welfare economists generally do not spend much time on the form or mechansims of the requisite transfers, except to say that suitable lump-sum and, where there are externalities present, ad valorem taxes could lead society to the social optimum.[17]

Perhaps the main reason for this lack of attention to transfers by theoretical welfare economists is the neatness of the dichotomy between efficiency and equity. It is extremely useful to be able to distinguish between these two concepts, for very little of a scientific nature can be said about equity, at least in the traditional welfare economics framework. To choose one efficient allocation over another will necessarily involve making at least one person better off and one worse off. Consequently, in order to evaluate such a choice involves making comparisons of the worthwhileness of individuals, comparisons that welfare economists are loath to make. If there is a social welfare function, however, then the equity problem is resolved, and the economist can worry only about efficiency.

[14] R. A. Musgrave, "Provision for Social Goods," in J. Margolis and H. Guitton (eds.), *Public Economics* (London· Macmillan, 1969), pp. 143–144.

[15] See K. J. Lancaster, "A New Approach to Consumer Theory," *Journal of Political Economy,* Vol. 74, No. 2, April 1966, pp. 132–157.

[16] For a discussion of social welfare functions in the context of traditional welfare economics, see J. de V. Graaff, *Theoretical Welfare Economics* (Cambridge: Cambridge University Press, 1967).

[17] See, for example, ibid.

The unfortunate thing about this situation, however, is the unsatisfactory nature of the concept of a social welfare function. How is such a function obtained? In a dictatorship we might simply say the welfare function reflects the individual preferences of the dictator. In a democracy, however, this is not a satisfactory answer. Without going too far afield, for this issue inevitably ends up on the border between economics and political science, we can say that principles underlying formation of social welfare functions are not at present satisfactorily worked out. Some even contend that it is impossible to obtain a satisfactory social welfare function.[18] Given this state of affairs, it is not hard to see why a normative theory of transfers was not developed in the context of traditional welfare economics theory.

In recent years, however, a normative theory of transfers has been developed. The time seemed to be ripe for such a development, and a number of people came forth at about the same time with remarkably similar ideas.[19] The general feature of these theories is the use of consumption externalities to justify transfers, instead of a social welfare function. Perhaps the main contribution of these theories is the proof that transfers are required for efficient resource use; in other words, transfers are treated along with resource allocation on the efficiency side of the welfare economics ledger. An important issue brought out by these theories is the appropriate form of the transfer, that is, whether it should be in cash or in kind.

Since the purpose of this paper is to evaluate the rationale of housing as a merit good, and since the merit good concept is, we think, most fruitfully interpreted in terms of consumption externalities, it is clear that these recently developed theories are extremely important to the issue at hand. Consequently, we shall present a version of the the theory here. The version we present is due to Edgar Olsen and is in the form of a simple numerical example, although generalizable.[20]

Assume there are two individuals in society, the grantor and the recipient. Suppose that they consume two goods, nonhousing and housing. The grantor directly consumes only nonhousing, but he also cares about the recipient's consumption of housing. The recipient directly consumes both nonhousing and housing.

The following utility functions are assumed (a utility function shows the relationship between the goods a person consumes and the satisfaction he receives from the consumption of those goods):

$$U_g(X_g, H_r) = X_g^{.9} H_r^{.1}$$
$$U_r(X_r, H_r) = X_r^{.8} H_r^{.2}$$

where

X_g = the quantity of nonhousing consumed by the grantor

X_r = the quantity of nonhousing consumed by the recipient

H_r = the quantity of housing directly consumed by the recipient.

Assume further that nonhousing and housing are produced at constant costs of \$2 and \$1 per unit respectively and that the grantor has an income of \$400 and the recipient an income of \$100 per time period.

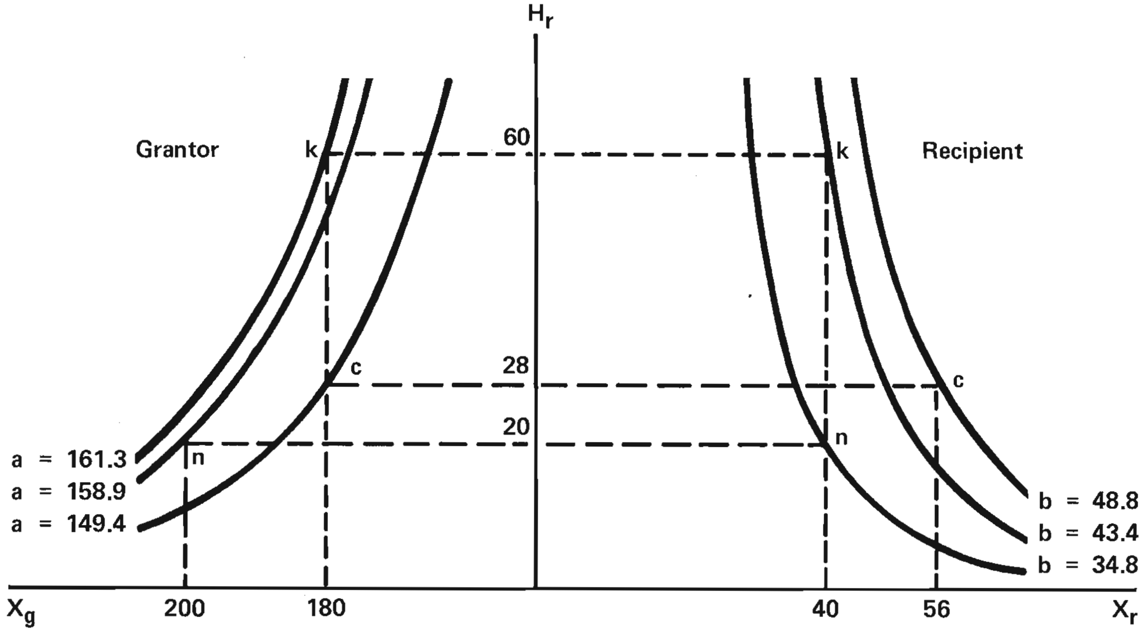
In a competitive economy without transfers, each person would attempt to obtain the most satisfaction from his expenditures by buying the appropriate quantities of the commodities he wants; the resulting allocation of resources would be $H_r = 20$, $X_r = 40$, and $X_g = 200$. These amounts are shown on the indifference-curve diagram in Figure 1 and are labelled *n*. (An indifference curve shows all the consumption combinations of two goods that will yield the same level of satisfaction for the consumer. Higher indifference curves mean greater satisfaction.) Notice that the 20 units of housing bought by the recipient affect the preference level of the donor (these levels are indicated by *b* and *a* respectively) but that the "donor" has done nothing yet to affect the level of housing consumption of the recipient.

[18] K. J. Arrow, *Social Choice and Individual Values*, 2nd ed. (New York: Wiley, 1963).

[19] See H. M. Hochman and J. D. Rogers, "Pareto Optimal Redistribution," *American Economic Review*, Vol. 59, No. 4, Part 1, Sept. 1969, pp. 542–557; B. O. Olsen, "A Normative Theory of Transfers," *Public Choice*, Vol. 6, No. 2, Spring 1969, pp. 39–58; and M. V. Pauly, "Mixed Public and Private Financing of Education," *American Economic Review*, Vol. 57, No. 1, March 1967, pp. 120–130.

[20] E. O. Olsen, "Subsidized Housing in a Competitive Market: Reply," *American Economic Review*, Vol. 61, No. 1, March 1971, pp. 220–224. For the generalization, see P. A. Samuelson, "Pure Theory of Public Expenditure and Taxation," in J. Margolis and H. Guitton (eds.), *Public Economics* (London: Macmillan, 1969), pp. 98–123. Samuelson, however, is unsympathetic to this approach, claiming it has no relevance to motivated market behavior because of the possibility for gameplaying by the individuals involved (ibid., pp. 106–107 and appendix). We do not think his remarks apply to the interpretation given here to the consumption externality model.

Figure 1



It turns out that this competitive market allocation of resources is inefficient because at least one of these people can be made better off without making the other worse off. The reason for this is that the donor has a demand for housing consumed by the recipient, and the donor would be willing to pay something to see this demand satisfied. This something he would pay is, at the margin, the dollar value of the amount he would give up of his own consumption of nonhousing to see the recipient get another unit of housing.

If this amount could be charged to the donor in partial payment for the recipient's housing, and if the rest of the cost of the recipient's housing could be charged to the recipient, the resulting allocation of resources would be $X_g = 180$, $X_r = 40$, and $H_r = 60$. The proportion of the recipient's housing paid for by the donor would be two-thirds, the recipient paying the remaining one-third. This allocation and its associated preference levels are illustrated in Figure 1 by the points labelled *k*. Notice that both the donor and the recipient are better off than they were under the nontransfer competitive market allocation; i.e., they occupy higher indifference curves.

We have not indicated the nature of the transfer mechanism in the above example, but the transfer itself is of an inkind nature. It is necessary for a social optimum that the recipient consume 60 units of housing, and the transfer is rigged so this outcome will result.

Suppose a cash transfer of $60 were given to the recipient. He could consume 60 units of housing but would not choose to do so. In fact, he would consume only 28 units of housing and 56 units of nonhousing, in effect trading off housing for nonhousing consumption. The donor would still consume 180 units of nonhousing. This allocation is denoted by the points labelled *c* in Figure 1.

Notice that in comparison with either the nontransfer competitive market allocation or the inkind transfer allocation, the donor is worse off and the recipient is better off. Moreover, this allocation is not efficient because both the recipient and the donor could be made better off, for example, at the feasible allocation $X_g = 170$, $X_r = 48.9$, and $H_r = 68.9$ (not shown on Figure 1). Therefore, to allow recipients of subsidies inkind to convert these to subsidies in cash may result in inefficient resource allocation, and a fortiori to give cash grants may result in inefficient resource use, where individuals are concerned about the quantity of goods that other people consume. Whether preferences are of this type would seem to be an empirical question of great importance.

The preceding provides a rationale for transfer between individuals for the purpose of economic efficiency. Does it, however, provide a rationale for government intervention to bring about optimal resource use where preferences for transfers exist? In the two-person example used above, it does not seem unlikely that the individuals involved would recognize their interdependence and arrive voluntarily at the optimum allocation of resources. However, as the number of people involved increases, the transfer activity takes on the characteristics of a public good. It then becomes advantageous for any person with a demand for consumption by someone else to hide his preferences, for if the good is provided, he will get to enjoy it without contributing to its provision. This is the standard problem of public-good provision pointed out by Samuelson nearly 20 years ago. If it were possible to get information on preferences for such transfer activities as housing, we could conceptually solve the problem of optimal provision. Although preferences are revealed for private goods by the actual purchase of those goods at market prices, such preferences for consumption externalities are not revealed because there are no markets in these externalities. Moreover, as already stated, there is every reason not to reveal one's preference for consumption externalities. In any event, the arrangement of transfers under these conditions appears clearly to be a governmental concern, for even with preferences known, the taxing power of the state would be required to collect sufficient revenue to support a transfer program.

Given the theoretical rationale for publicly subsidized housing as a merit good, an empirical question of some importance arises. Is there in fact a demand for the provision of publicly subsidized housing? The difficulty of answering this question has been referred to already. Despite this rather severe drawback, there has been some theoretical and empirical work relevant to the question. We turn now to an analysis of this work.

Estimating the Demand for Transfer Activities

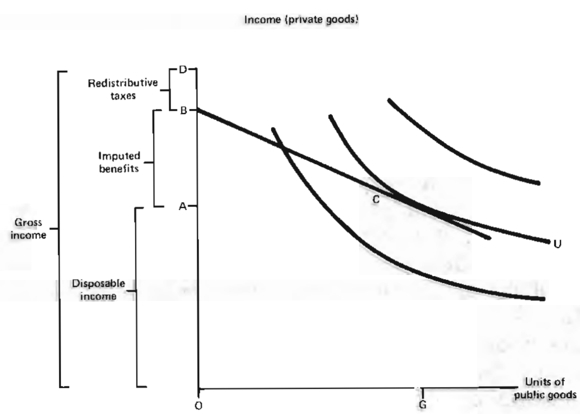
In order to establish the validity of the rationale for government intervention in private markets for the provision of goods conferring consumption externalities, we ideally should have the demand for the transfer activity. In the case of housing, for example, we should have the demands by prospective donors for the housing of prospective recipients. (As will be indicated later, we can perhaps accomplish the objective with less information than required by the ideal.)

If we had these demands, we could couple them with those of the recipients' own demands for housing to obtain the social demand for housing. This together with the cost of housing could be used to determine the socially optimal supply of housing as a consumption externality and the appropriate financing method, as was seen in the two-person world of the example in the preceding section. How, in practice, to obtain these demands?

For the private demand component, the answer is clear. A commodity such as housing is traded on the private market. Hence prices and quantities are observable, and, although there are difficulties (as there are with all empirical work) it is possible to obtain estimates of demand.[21]

For the consumption-externality demand component, the situation is considerably less clear for reasons already given. In fact, until the last three or four years, most economists would probably have said that it was impossible to estimate such demands. However, due to the recent work of Henry Aaron and Martin McGuire, there appears to be a glimmering of hope that the problem can be resolved.[22]

Figure 2



[21] For example, see the housing demand studies reviewed in F. DeLeeuw, "The Demand for Housing: A Review of Cross-Section Evidence," *The Review of Economics and Statistics,* Vol. 53, No. 1, Feb. 1971, pp. 1–10.

[22] See H. Aaron and M. C. McGuire, "Public Goods and Income Distribution," *Econometrica,* Vol. 38, No. 6, Nov. 1970, pp. 907–920; and M. C. McGuire and H. Aaron, "Efficiency and Equity in the Optimal Supply of a Public Good," *Review of Economics and Statistics,* Vol. 51, No. 1, Feb. 1969, pp. 31–39.

The contribution of Aaron and McGuire is twofold. They have cleared up some theoretical issues relating to the provision of public goods, and they have developed a method for imputing the value of public goods to households. Both are important, but the latter is directly relevant to the issue at hand. An exposition of their method for imputing the benefits of public goods follows.[23]

Suppose Figure 2 represents the indifference curves of an individual who "consumes" a public good and private goods (lumped together and valued in dollar terms). The public good in this case can be thought of as a consumption externality, such as the quantity of housing consumed directly by others (like H_r that entered the donor's utility function in the example of the previous section).

This individual earns (before-tax) income of OD, pays taxes (less transfers) equal to AD, and retains disposable income of OA. All these sums are directly observable.

OA and OG are coordinates of a point C on indifference curve U. A line tangent to U at C intersects the ordinate at B. Then AB is the value to this person of OG units of the public good measured in terms of income or private goods.

This result is obtained by noting that the slope of BC measures the individual's marginal rate of substitution of public goods for income, defined at point C; i.e., it is the subjective value or price to the individual of a unit of the public good in terms of income. Multiplying the quantity of public goods by its "price" gives the income equivalent of OG to the individual.

AB may also be interpreted as the sum of taxes the individual would be willing to pay in return for OG units of the public good, provided he could be cajoled into revealing his preferences truthfully. If OG units of the public good were financed by taxes according to the benefit principle, this individual's share would be exactly AB.

On balance, then, the individual has paid AD in taxes, for which he has received benefits of AB. The amount BD, therefore, represents that portion of his taxes going for purely redistributional purposes. This might well be considered a waste unless our individual had preferences for purely redistributive transfers. Of course, B might fall well above D, in which case the individual would receive redistributive transfers instead of paying taxes.

Assuming a utility function additively separable in public and private goods, Aaron and McGuire show that the ratio of imputed benefits for any one individual to any other individual is equal to the inverse of the ratio of these individuals' respective marginal utilities of income. Given n–1 such equations and an nth equation, say $\Sigma AB_i = OG$ as suggested by Maital, then one can solve for the *n* unknown AB's.

Aaron and McGuire have used this approach to estimate the distributive impact of taxes and government expenditures. Their results cast doubt on the findings of previous studies that suggest the combined incidence of taxes and expenditures on income distribution is highly progressive.

In order to obtain this result, they computed the AB's indicated above, but only for two broad classifications of government expenditures: (1) public goods, i.e., those goods that everyone consumes in equal amounts, and (2) "specific" goods, i.e., "goods or services produced by governments, but which otherwise are similar to private goods privately produced, i.e., not commonly shared, but consumed exclusively by their 'owner.' "[24] Following the Tax Foundation's lead, Aaron and McGuire included housing in the public goods category. Although their analysis can accommodate merit goods like housing that may not enter everyone's utility functions, they do not present a separate category for this type of good in their empirical work. Maital also presents aggregate estimates of imputed benefits from public and "specific" goods, but not merit goods.

It appears, therefore, that a method exists for estimating the consumption-externality benefits of goods like housing. Such benefits have not, however, been measured. Since, as indicated at length previously, the justification for government intervention in private markets for goods like housing depends importantly on the existence of transfer benefits, the empirical estimation of such benefits ought to be a high priority research item.

It is conceptually possible, although Aaron and McGuire do not stress it, to use the preceding analysis in obtaining the individual consumption-externality demands for merit goods. Knowing these would permit the a priori determination

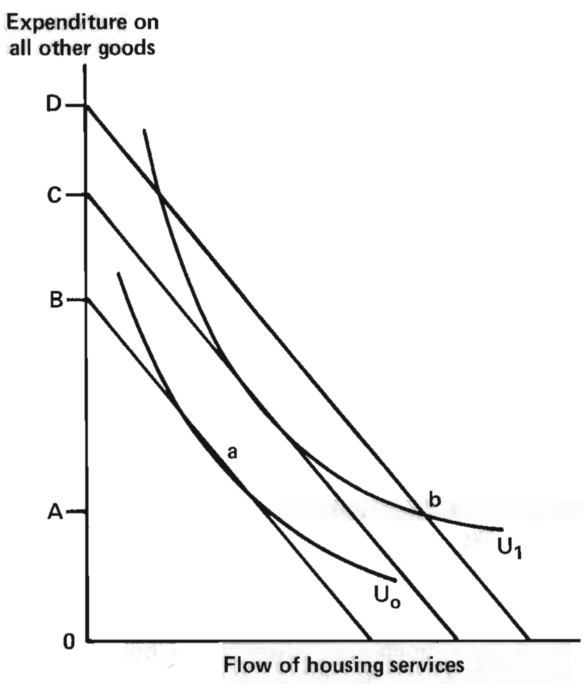
[23] The exposition in the text follows closely that of S. Maital, "Public Goods and Income Distribution: Some Further Results," *Econometrica*, Vol. 41, May 1973, pp. 561–568.

[24] A. Aaron and M. C. McGuire, "Public Goods and Income Distribution," *Econometrica*, Vol. 38, No. 6, Nov. 1970, p. 908, n.3.

of the optimal level of the good and of the optimal tax charges. However, such an enterprise would be a major undertaking, involving massive data collection and strong assumptions to render the analysis empirically tractable. Nor would such an undertaking seem necessary if that described in the previous paragraph could be done, at least for merit goods provided in ongoing government programs such as federally subsidized housing.

Although there do not exist estimates of the benefits of consumption externalities for specific goods, including housing, there have been two studies that shed some light on the magnitude of such externality benefits for housing.[25] Instead of measuring the quantity earlier called "imputed benefits," a quantity is estimated representing the minimum amount of such benefits necessary to ensure that a housing program is an efficient use of resources.

Figure 3



To see how such a concept is obtained, refer to Figure 3, which represents the preference map of a prospective (or actual) recipient of subsidized housing.[26] The preference map shows this person's choices between housing on the horizontal axis and all other expenditures on the vertical axis. As a nonparticipant, the household is at point *a* where indifference curve U_0 is tangent to his budget constraint. As a participant, the household is at point *b* on indifference curve U_1. (We assume he is better off as a participant or he would not participate in the program, but the location of *b* on U_1 is arbitrary.) Since the household's money income is the same whether or not he participates in the program, *OB* represents this magnitude which is divided between housing expenditures (subsidized) of AB and expenditures on everything else, OA. The direct net benefits to the participant are BC, that is, how much money he would have to be given to be as well off without subsidized housing as he is with it. The market value of the subsidized unit is given by AD, which under certain circumstances is the same as the total resource cost of providing the subsidized housing unit. This quantity can be divided into two parts: the tenant's contribution, AB, and his subsidy, BD. Notice that the subsidy exceeds the direct benefit by the amount CD.

If housing created no consumption externalities, the amount CD would be a deadweight loss to society, for the cost of providing the subsidized housing would exceed the benefits of doing so. It is a well-known theorem of economics that, for indifference curves shaped as in Figure 3, the direct benefits will always fall short of the resources necessary for the subsidy. On the other hand, if housing does confer consumption externalities (i.e., if housing is a merit good as we use the term), then those consumption-externality benefits must be at least as large as CD for the housing subsidy to be justified as an efficient use of resources. If the consumption-externality benefits fall short of CD, then it may be better to give the subsidy in cash than in kind.

It is possible to estimate these minimum required benefits since the subsidy is observable and, with a specific utility function, direct benefits can be estimated. The magnitude resulting from their difference can give some guidance as to the likely efficiency of the program. For exam-

[25] Namely H. J. Aaron and G. M. von Furstenberg, "The Inefficiency of Transfers in Kind: The Case of Housing Assistance," *Western Economic Journal*, Vol. 9, No. 2, June 1971, pp. 184–191; and J. S. DeSalvo, *An Economic Analysis of New York City's Mitchell-Lama Housing Program* (New York: The New York City Rand Institute, R-610-NYC, June 1971).

[26] The analysis on which the exposition in the text is based is presented in J. S. DeSalvo, "A Methodology for Evaluating Housing Programs," *Journal of Regional Science*, Vol. 11, No. 2, Aug. 1971, pp. 173–185.

ple, if minimum required benefits are small, either absolutely or relative to the size of the public subsidy, then the program would require little in the way of consumption externalities to justify its existence.

The author used this approach to evaluate a New York City housing program for middle income families.[27] As of June 1968, the 123 housing projects containing 57,000 units were producing $109.6 million a year in direct benefits to their occupants. This amounted to $1,926 per unit. Of this total the tenants themselves provided $84 million through payment of their subsidized rentals. The remainder was $25.6 million or $450 per unit. On average, then, each tenant would have had to be given $450 per year in cash to be made as well off without the program as he was with it. This was a real income increase amounting to about 5 percent of the average tenant's actual money income. It required $130.9 million annually to operate these projects, of which $47 million or $824 per unit was the public subsidy. Consequently the minimum required consumption-externality benefits were $21.3 million or about $374 per unit per year. This comes to about 16 percent of the total annual cost of the projects. Whether or not the projects created this much in consumption externalities is unknown, but at least this much must have been created if the subsidized housing was a worthwhile public investment. Given this kind of information, one would hope citizens and public officials could better evaluate whether such a program was worth its price.

Aaron and von Furstenberg use exactly the same conceptual framework to calculate the inefficiency of housing subsidies. Their inefficiency percentage is our minimum required consumption-externality benefits expressed as a percentage of the public subsidy. In terms of Figure 3, it is 100 $(\frac{BD-BC}{BD})$ percent or 100 $(\frac{CD}{BD})$ percent. For the program discussed above, the inefficiency percentage as defined by Aaron and von Furstenberg would be 100 $(\frac{\$374}{\$824})$ percent = 45 percent. In other words, a cash subsidy equal to an amount 16 percent smaller than the inkind subsidy would have produced the same level of benefits to subsidized households. Aaron and von Furstenberg also calculate the income effect of housing subsidies, defined in terms of Figure 3 as 100 $(\frac{BC}{OC})$ percent. This is the percentage increase in real income accruing to the occupant of subsidized housing, given above as 5 percent for the New York City program.

Aaron and von Furstenberg do not present a detailed analysis of any subsidized housing program. Rather, they calculate values of the two percentage figures discussed above for various values of variables representing (1) the degree of substitutability between housing and other goods in consumption (called the elasticity of substitution) and (2) the percentage size of the subsidy, i.e., the percentage reduction in the price of housing for a subsidized household. (See Table 1.) They find that the greater the degree of substitutability, the greater is the inefficiency of subsidized housing, no matter what is the percentage size of the subsidy. This just says that the more housing a person would be willing to give up for a unit of other goods, the less cash he would have to be given to be made as well off as with any given value of subsidized housing. Aaron and von Furstenberg also find that the inefficiency of housing subsidies increases as the percentage size of the subsidy increases. That is, the more of a person's housing budget is subsidized, the better off he would be with a cash transfer of equal dollar amount. Finally, the income effect of subsidized housing is found to increase with the elasticity of substitution, given the size of the subsidy, and to increase with the size of the subsidy, given the elasticity of substitution.

Table 1. Inefficiency and Income Effects of Subsidized Housing

Elasticity of Substitution	Percentage Size of Housing Subsidy 10	20	30	40	50	60	70	80
	The Inefficiency Percentage of Housing Subsidies							
2.0	7.5	15.0	22.5	30.0	37.5	45.0	52.5	60.0
1.5	5.7	11.8	18.1	24.8	32.0	39.8	48.4	58.2
1.0	3.9	8.2	13.0	18.3	24.3	31.4	39.8	50.5
0.75	2.9	6.3	10.1	14.4	19.5	25.6	33.2	43.3
0.5	2.0	4.3	7.0	10.1	13.9	18.6	24.3	33.2
	The Income Effect of Housing Subsidies							
2.0	2.8	6.2	10.7	16.7	25.0	37.5	58.3	100.0
1.5	2.7	6.0	10.0	15.1	21.8	31.2	45.5	71.4
1.0	2.7	5.7	9.3	13.6	18.9	25.7	35.1	49.5
0.75	2.6	5.6	9.0	12.9	17.6	23.4	30.8	41.3
0.5	2.6	5.5	8.7	12.3	16.4	21.3	27.1	34.6

Source: H. J. Aaron and G. M. von Furstenberg, "The Inefficiency of Transfers in Kind: The Case of Housing Assistance," *Western Economic Journal*, Vol. 9, No. 2, June 1971, p. 188.

[27] See J. S. DeSalvo, *An Economic Analysis of New York City's Mitchell-Lama Housing Program* (New York: The New York City Rand Institute, R-610-NYC, June 1971). The figures in the text differ from those reported in the Rand study due to the correction of a specification error in the latter.

With rough calculations, Aaron and von Furstenberg figure that the inefficiency of public housing ranges from 3.4 to about 10 percent. For Sections 235 and 236 housing, they estimate the inefficiency at about 18 percent. For Section 243 of the Emergency Home Financing Act of 1970, Aaron and von Furstenberg estimate inefficiency of at most 5 percent. Unfortunately, dollar magnitudes are not presented. They conclude as follows:

> In sum, if all housing programs operated with maximum consumption efficiency, the same increase in the welfare of recipients could be purchased for about 10 to 15 percent less, depending on program mix. In fact, because of quantity constraints, the inefficiencies may be lower even if no external benefits are attached specifically to the increased consumption of better housing.[28] If there are large inefficiencies in federally assisted housing, they will have to be found empirically, on the cost side, to the extent the administration of particular programs involves detailed federal regulations of the conditions of supply.[29]

This is an optimistic conclusion. If Aaron and von Furstenberg are correct, then the empirical relevance of consumption-externality benefits is slight, for federally subsidized housing programs achieve virtually the same results as cash grants, at least as regards the benefits created. Nevertheless, cash grants may well be a less costly way of achieving the desired results. It is this writer's view that the optimistic position of Aaron and von Furstenberg is not well founded. Even if they are correct that the inefficiency of subsidized housing programs is only 10–15 percent, this is surely a large amount of money. For the New York City program discussed above, the inefficiency percentage was even higher, amounting to over $21 million in 1968 alone. Unfortunately, there are no other empirical studies of subsidized housing that provide a dollar estimate of the minimum required consumption-externality benefit.

In summary, we have shown that to justify inkind transfers requires the existence of consumption-externality benefits. Such benefits are difficult but not necessarily impossible to estimate. However, no such estimates exist, at least for housing. Nevertheless, existing studies have shown the relative and absolute size that such benefits must attain for certain housing programs to be justified in terms of efficient resource use. It turns out that these minimum required benefits are on the order of at least 10–15 percent of the public subsidy. In the absence of definite estimates of consumption-externality benefits, the main issue would appear to be the relative costs of subsidized housing versus cash grants. In the following section we discuss this issue further.

Housing Subsidies or Cash Transfers?

Suppose empiricial evidence supported the view that housing confers consumption externalities that are of sufficient magnitude to justify transfers whose purpose would be to increase the housing consumption of certain people. An unanswered question would be how best to effect such transfers.

Needless to say, there are a number of ways in which housing subsidies can be conferred. We do not intend to discuss these. Instead we present briefly a method that is superior in several respects to the standard methods. Specifically, we recommend a rent certificate scheme designed to increase the quantity of housing consumed by low income families.[30]

A rent certificate plan is a method that permits a set of families to purchase rent certificates for an amount less than the face value of the certificate. Sellers of housing services may redeem these certificates at their face value from the subsidizing government. The difference between the face value of the certificate and the amount paid for it by the eligible family is the public subsidy. It must be illegal to use the rent certificate for other than the purchase of housing service. Consequently, a penalty must be imposed on the illegal use of rent certificates, since, as implied by the discussion in the last section, recipients of the rent certificate would prefer an equal dollar cash amount. (In fact they would be willing to take less, up to a point.)

In order to implement such a scheme, several issues must be settled in advance by the

[28] In their analysis, Aaron and von Furstenberg assume households receive a price subsidy and can choose whatever quantity of housing they wish. Of course, many programs are not like this but instead require a participant to take a particular unit at the subsidized price. The analysis can be generalized to include this type of program; however, we believe Aaron and von Furstenberg are incorrect in saying inefficiencies will be lower under such programs. See J. S. DeSalvo, "A Methodology for Evaluating Housing Programs," *Journal of Regional Science*, Vol. 11, No. 2, Aug. 1971, pp. 173–185.

[29] H. J. Aaron, and G. M. von Furstenberg, "The Inefficiency of Transfers in Kind: The Case of Housing Assistance," *Western Economic Journal*, Vol. 9, No. 2, June 1971, p. 190.

[30] The analysis draws primarily on E. O. Olson, *An Efficient Method of Improving the Housing of Low Income Families* (Santa Monica: The Rand Corp., P-4258, Dec. 1969). See also I. S. Lowry, J. S. DeSalvo, and B. M. Woodfill, *Rental Housing in New York City*, Vol. II: "The Demand for Shelter" (New York: The New York City Rand Institute, R-649-NYC, June 1971).

subsidizing government. It must be decided who is eligible to receive rent certificates, what is to be the face value of the certificate received by each person, and what is to be the amount that each person must pay to receive his certificate.

Given answers to these questions and an adequate administrative set-up, it can be shown that such a rent certificate plan will have desirable features not shared by other methods of conferring housing subsidies. Specifically, the housing service consumed by participating families will be provided at least cost. This is so because the program uses the private competitive housing market to provide housing instead of some other mechanism, e.g., public housing projects. Competition forces housing producers to operate efficiently, whereas there is no comparable force at work in many subsidized housing programs. Also, the rent certificate plan is considerably more flexible than others. Namely, any distribution of consumption of housing service can be achieved by varying the face value of the certificate and/or the amount required to purchase it.

Suppose, however, that empirical evidence did not support the view that housing confers consumption externalities. Then, to the extent income or preference levels of others created consumption externalities, there would be justification for transfers in cash rather than in kind. Efficient methods for transferring cash have been discussed for some time and will not be analyzed here. Suffice it to say that something like the Family Assistance Plan originally proposed by the Nixon Administration would seem to fill the bill.

In the absence of empirical information on the existence and magnitude of motives for transfers, whether in cash or kind, one must fall back on plausible reasons for supporting specific transfer schemes. In a recent unpublished paper Edgar Browning provides a list of advantages of cash transfers, where the comparison is with consumption subsidies of equal cost:

1. Recipients will be better off if the assistance is given in the form of cash. (This familiar reason is still as good as ever, and deserves to be listed first.)

2. Recipients will learn to make wiser consumption decisions as a result of having the responsibility of making their own choices. (The strength of this argument probably depends, however, on the form of the consumption subsidies. Some forms of consumption subsidies, such as public housing, are more clearly than others an instance of the government making choices *for* recipients and thereby depriving them of the knowledge and experience to be gained by making their own choices.)

3. Consumption subsidies would have to be changed frequently with the introduction of new goods and technology, and with changes in preferences, incomes, other government policies, etc. (This must be true if the programs are presented as being "optimal" since what is optimal in a consumption subsidy depends on all these, and other, factors.) Frequent, and unpredictable, shifts in government policy will compound the difficulty of recipients wisely planning their own affairs. With cash transfers, this type of uncertainty can be reduced.

4. The administrative cost of a cash transfer program will be smaller.

5. Problems created by special interests in the government bureaucracy and in producer groups are less severe.

6. Making one decision—how to distribute money among the poor—will put less strain on the legislative process than having to make a multitude of decisions concerning each commodity subsidized.

7. The consequences of cash transfers are easier to understand so voters will be better informed.

8. Cash transfers will increase understanding of, and respect for, the ability of markets to cater to the needs of the poor.[31]

Browning realizes that these points will not all attract wide agreement. He claims, however, that they are positive propositions capable of refutation and that disagreement about them indicates that there are plenty of issues that need settling in addition to the basic issue of existence and magnitude of consumption externalities.

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[31] E. K. Browning, "Consumption Subsidies and Cash Transfers: The Controversy Revisited," unpublished paper [n.d.], pp. 30–31.

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Housing Subsidies as Redistributive Instruments

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Introduction

This paper sets out and evaluates the logic of housing subsidies as instruments of income redistribution from rich to poor. This objective of government intervention in housing markets is, of course, difficult to separate from other objectives like the reduction of neighborhood or community segregation, the internalization of external effects associated with poverty and blight, and the counterbalancing of imperfections in markets for housing and housing finance. These objectives interface, in the joint product sense, with the redistributive objective. The narrow focus of this paper, however, is on the legitimacy—other justifications aside—of housing subsidies as means of redistributing income, where redistribution is desired for its own sake, and for its effects on recipients and the communities in which they live. Desirable effects of housing subsidies which might occur whether or not they redistribute income, such as reduction of urban externalities, are neither considered nor denied.

To assess housing subsidies as means of redistribution, where equalization is itself the program objective, requires an examination of their incidence. This must be examined in light of what might have happened had such programs not been adopted, as well as what might have happened if other redistributive programs such as cash transfer had been used instead. Henry Aaron's recent volume contains a careful study of such effects.[1]

Where the stated objective of a housing program is to reduce the extent to which individuals, by choice or economic necessity, are ill-housed, as judged by a majority within one or more of the political communities (local, State, or Federal) in which they reside, its logic need not necessarily be redistributive. The political majority that sanctions the program might, for instance, care only about appearances or esthetics, and not at all with the income or the welfare of the poor. This cynical view, however, which calls only for hiding poor housing from public view (analogous to the annual parade of a military dictatorship) seems very much at odds with the current level of concern with housing and the community characteristics with which it is associated. Far more likely, housing subsidies indicate a concern with both the particular-commodity external effects felt to be associated with substandard housing, and with the long term distributional implications of these effects. In this perspective, alleviation of external diseconomies due to health, crime, and neighborhood decay, and the redistribution of income, are joint products of housing subsidy programs. The implicit premise, so far as income redistribution is concerned, is that an upgrading of housing quality will set in motion a dynamic process in which recipients become more likely to escape their impoverished state than they would be under simple income transfers. Implicit in this justification of income transfers through housing subsidies is a set of hypotheses about social dynamics and an equity judgment that involves intergenerational as well as interpersonal considerations.

Viewed within a public choice frame of reference, the suggestion that housing subsidies are preferable to cash transfers as means of redistribution requires the presence of some sort of external effect. Simple taxpayer-donor concern for the current well-being of the ill-housed, as opposed to their consumption of housing, is insufficient. Unless a conflict exists between shortrun and longrun distributional effects, well-to-do members of the community, if concerned only with the self-perceived welfare of the poor and ill-housed, can do better by making a given amount of income transfers in cash rather than in kind. The reason is the traditional one.[2] Cash transfers afford recipients a wider range of expenditure options and, therefore, permit greater increases in self-evaluated welfare per dollar

[1] Henry Aaron, *Shelter and Subsidies: Who Benefits From Federal Housing Policies?* (Washington, D.C.: The Brookings Institution), 1973.

[2] See e.g., Milton Friedman, "The 'Welfare' Effects of an Income Tax and Excise Tax," in *Essays in Positive Economics* (Chicago: The University of Chicago Press), 1953, pp. 100–117. For the restatement of this argument in public-choice terms, Harold M. Hochman, "Individual Preferences and Distributional Adjustments," *American Economic Review*, May, 1972, pp. 353–360; and James W. Rodgers, "Distributional Externalities and the Optimal Form of Income Transfers," (Washington, D.C.: The Urban Institute), April 1971. See as well, James W. Rodgers, "Explaining Income Redistribution," in Harold M. Hochman and George Peterson, eds., *Redistribution Through Public Choice* (New York: Columbia University Press), forthcoming.

transferred, at least in the short run, in which tastes are constant. This same argument holds if redistribution is considered strictly from the perspective of recipients, rather than within a perspective that treats them as derived from the preferences of the taxpayers who finance them.

In contrast to public choice arguments in support of income transfers through housing subsidies, transfers through housing programs are sometimes justified as a second-best means of redistribution, on grounds of political failure. This justification, however, has nothing to do with the value of housing for its own sake, at least so far as redistribution itself is the marginally relevant objective. It derives, rather, from the judger's view that the political process will not generate what he feels to be a desired amount of redistribution, and that housing subsidies are the appropriate instrument for attaining the overriding redistributive end. How much credence this argument is to be granted depends, in essence, either on evidence of political failure, in the sense that the process through which constituent preferences are translated into public programs is imperfect and does not reflect what taxpayers really want, or on one's willingness to accept an elitist interpretation of the role of government, in which the desired amount of redistribution can somehow be determined independently of the political process. The thrust of this latter argument is that the political majority, if it could so so, would enact redistributive income transfer programs in their simplest and most straightforward form, but that it is thwarted in so doing by imperfections in the political system. Evidence on this question is, to say the least, scanty.[3] Moreover, in using this argument to justify in-kind subsidies, the policymakers cannot avoid the implication that participatory democracy is defective.

Even aside from this, no matter how forcefully the "political failure" argument is put (and I am not convinced of its merit), it cannot, in itself, establish that housing subsidies are the appropriate second-best means through which to bring about the desired income transfers, or how important they should be in the mix of such second-best means. The "political failure" argument, possible differences in excess burdens (implicit inefficiencies in allocative effects of governmental interventions) aside, is just as consistent with the use of transportation subsidies, food stamps, or, for that matter, subsidies to the leisure activities of the recipients, as it is with housing subsidies. If monetary transfers are ruled out, the justification of housing subsidies, rather than other types of in-kind transfers, reverts to allocative grounds, and, therefore, to external effect considerations. Housing subsidies must be demonstrated to be better than their in-kind alternatives on such grounds.

The choice between housing subsidies and other types of in-kind transfers depends on the excess burdens (the welfare loss attributable to the effect of government intervention on the output quantities concerned) generated by each alternative. In turn, these excess burdens decline as the price elasticities of demand and supply of the services involved decline, as lower elasticities imply that output levels deviate less from what they would be without government intervention. Whether housing subsidies are desirable—assuming the political process inhibits monetary transfers—depends, then, on the relative values of such elasticities.

The desirability of housing subsidies also depends on the nature and magnitude of the implied collateral transfers to factors of production that specialize in the supply of the activities, subject to subsidization. That is, abstracting from external effects, whether subsidization of activities such as housing is desirable depends on how one views the transfer of income to persons who own factors of production that specialize in the production of housing, as opposed to factors that are specialized to other uses that might be subsidized. In the housing case, the specialized factors are urban land and subsidy building trades employees. In neither case is the beneficiary considered to be a primary candidate type for redistribution, even in the minds of those who feel that "political failure" renders redistribution insufficient.

Indeed, when one considers transfers-in-kind, it seems difficult to reject the hypothesis that housing subsidies are politically more palatable than income transfers, precisely because they permit consumer demands to be supplemented by the self-interested demands of both producers of housing services and government officials, both of which are classes with a vested interest in augmenting the market demand for housing services. Such special interests, certainly in the private sector, are inherently weaker in the monetary transfer case.[4]

[3] See Otto A. Davis and John Jackson, "Representative Assemblies and Demands for Redistribution: The Case of Senate Voting in the Family Assistance Plan," in Hochman and Peterson.

[4] Hirofumi Shibata, "Income Redistribution Through Production of Public Goods: A Two-Sector General Equilibrium Model with Public Goods," an Urban Institute Working Paper, 1972.

Except when housing subsidies are a pure substitute for monetary transfers, it is important to focus on the "effective" degree to which their receipts are earmarked in evaluating arguments for housing subsidies as a vehicle for income transfers.[5] Where the subsidies are intramarginal and not tied to increments in housing consumption, recipients can, in practice, use them to finance continued consumption of initial levels of housing and housing services. In this case, unless donor-taxpayers are irrational and derive utility from the illusion rather than the reality of controlling recipient consumption bundles, housing subsidies are indistinguishable in impact from cash transfers.[6] Only when subsidies affect the marginal price of housing can they be expected to affect housing choice. But even in this case, the increased housing expenditures resulting from housing subsidies will generally be considerably less than the total amount of the subsidies. The fact that such fungibility offsets most of the impact of housing subsidies will obviously disturb those who support such subsidies as a means of income transfers less than those who support them as a means of alleviating external effects due to substandard housing. There is, in other words, a policy tradeoff between effects on housing and redistributive effects.

External Effects and Housing Subsidies

Let us now consider the kinds of external effects that might justify housing subsidies, as opposed to cash transfers and other types of in-kind transfers, as a vehicle for transferring income. There are basically two such justifications: Either taxpayer-donors are distressed by poor housing conditions, or, previous reservations aside, "political failure" prevents them from transferring income directly and they find that housing is the second-best form of transfer.

Taxpayer-donors may prefer housing subsidies to cash (and other forms) of income transfers on both shortrun and longrun grounds. The shortrun consideration is that taxpayer-donors may attach some importance to the way in which recipients live, and feel that the private decisions of recipients will not satisfy these feelings.[7] Specifically, donors may believe that poor housing conditions promote the high incidence of crime, disease, or drug addiction, which diminish their own feelings of well-being. The longrun consideration is that they believe the social dynamics associated with improvements in housing quality will somehow reduce the future dependence of present recipients on transfers, or somehow transform these recipients so that they will no longer behave in ways that they, the donors, consider undesirable.

The basic thrust of the longrun argument for housing subsidies is that they will change the tastes, and thus the behavior, of the transfer recipients in ways that will make them better citizens in the future, both because they will be more productive members of the labor force and because their consumption and behavior patterns will generate fewer external diseconomies. This possibility, in turn, entails certain expectations about the process of acculturation. For instance, it would seem predictable that such programs as public housing would contribute little, if anything, to the acquisition of such characteristics. While public housing moves residents of substandard housing to more attractive facilities, it is unlikely to foster the fundamental personality changes—i.e., preference changes—on which the program depends, because it does not alter preexisting patterns of social relationships.

What is essential is that housing subsidy programs alter the environment in a manner conducive to generating what one might call "Coleman-type" externalities through demonstration effects on preferences and behavior.[8] In this respect, public housing, by perpetuating ghetto homogeneity, may be ineffectual, although it does spare the parties involved the discomfort of disruption of their normal social relationships. By contrast, diffusion of the recipient population, by bringing recipients into contact with other segments of the community, may reduce conflict and alienation and may provide an environment that

[5] See Frank de Leeuw, Sam H. Leeman and Helen Blank, "The Design of a Housing Allowance," an Urban Institute Working Paper, 1970, for a discussion of the earmarking question in the context of alternative housing allowance proposals.

[6] One difference, however, is that costs of administration may be higher.

[7] I rule out, as uninteresting, aberrant cases, like that of the millionaire hermit housed in a hovel, in which the redistribution implicit in a housing subsidy would be perverse, though subsidization in such cases is appropriate if external appearances are all that matter to taxpayer-donors.

[8] See James S. Coleman, et al., *Equality of Educational Opportunity*, (Washington D.C.: U.S. Department of Health, Education and Welfare, U.S. Office of Education, OE–38001) otherwise known as the Coleman Report, p. 22. Reference here is made to their finding that the socioeconomic endowments of his/her classmates are the most important factors in a poor child's educational attainment. Some discussion of the effects of social change on behavior and attitudes is contained in the paper prepared for this task force by Stanislav V. Kasl, "Effects of Housing on Mental and Physical Health."

nurtures as well as permits Coleman-type effects.[9]

If housing subsidies do not foster some such dynamic process of preference and behavioral change as suggested above, housing programs, interpreted strictly as means of income transfers, are difficult to reconcile with taxpayer-donor concern for recipient well-being. This, of course, does not mean that other arguments that can be used to justify such programs do not apply. In this particular case, it becomes necessary to recast the external effect argument in terms of the narrow self-interest of taxpayer-donors, and to demonstrate that housing subsidies promote their well-being, quite aside from whether they make the recipients feel better off. Such a rationalization for housing subsidies is obviously weaker than one that subsumes taxpayer-donor concern for recipients, attributable to utility interdependencies, as well as self-interest. Without utility interdependence, housing subsidies become, for taxpayers, only second-best alternatives. Taxpayers, Forrester-like, would prefer that the poor go away, moving not merely to another jurisdiction, but preferably to a jurisdiction far enough away so that their very presence cannot produce undesirable external effects.[10] They choose to redistribute to the poor only if this preference cannot be satisfied, and prefer housing to cash as the vehicle of redistribution, because it acts more directly on the manifestations of poverty that offend them.

Program Constituencies

One would expect that each of the different rationales for using housing subsidies as a vehicle for income transfer would attract a different constituency among potential taxpayer-donors. Those who would prefer cash transfers, and who see housing subsidies only as a second-best vehicle for redistribution, may accept housing subsidies as a more feasible though less preferable alternative. If monetary transfers should suddenly become practicable, their support for housing programs is likely to wane—unless feasible levels of monetary transfer are insufficient to satisfy their demands for income redistribution. Given the zeal of many egalitarians for redistribution, this is not at all unlikely.

By contrast, support for housing subsidies based on taxpayer dislike of the manifestations of poor housing conditions—as distinct from a benevolent concern for individuals who are badly housed—is likely to come from a very different part of the political spectrum. To sustain such support for housing subsidies, substantial evidence of effectiveness is essential. Overall, Coleman-type social dynamics or producer self-interest are the primary considerations to justify housing subsidy programs as the preferred instrument of income redistribution. Recipients, other things being equal, are likely to prefer as much redistribution as the political system will provide. Cash is, in general, the preferred vehicle from their viewpoint. If, however, recipients feel that cash transfers are in some sense more demeaning than the in-kind subsidies (more likely to attach an undesirable social label), they may prefer the in-kind transfers. They may also prefer in-kind to cash transfers if they feel that the underlying particular-commodity externalities, from the donors' perspectives, are strong enough to give rise to in-kind transfer programs that are sufficiently larger than the cash transfer programs donors would support to offset the fact that they afford recipients less expenditure flexibility.

Program Alternatives

There are numerous housing programs, some of which operate on the demand side of the market and others which operate on the supply side. In this section, some of these alternative housing programs are examined briefly in terms of their performance in promoting income redistribution and in generating desired changes in preferences and behavior.

The most interesting possibility is that the improvement in substandard housing, by inducing changes in the behavior of recipients, can benefit both recipients and donors, thus generating support for housing programs among both sets of parties. For such social change to occur, housing subsidies must first stimulate expenditures on housing, which, as was explored above, is not an automatic consequence of housing subsidy programs. Even if housing subsidies do stimulate housing expenditures, moreover, the increased housing expenditures must also exert the desired changes in tastes, behavior, and the socioeconomic characteristics of recipients. At present, this impact of housing subsidies is merely a logical possibility. No definitive evidence exists to suggest that it does happen, and

[9] On this score, one finds support for the notion of scattered-site low income housing and Section 23 leased housing, and for evaluating programs, among other things, in terms of whether they reduce segregation based on income and race. One also finds support in this rationale for rehabilitation and maintenance subsidies, as means of setting up demonstration effects.
[10] Urban renewal seems best rationalized by this kind of argument.

it is also logically possible that the result will be "leveling-down" rather than "leveling-up." [11]

The implications of using housing subsidies as a means of income maintenance, justified by "political failure," are more complicated. Here the issue is not the effects of housing subsidies on housing markets, but simply whether the subsidies find their way to intended recipients, for whom poor housing is a proxy for more general conditions of poverty. On this account, programs that operate on the demand side of the housing market are likely to be more effective than programs that operate on the supply side. Demand-side programs put real income, albeit in restricted form, directly into the hands of the intended recipients, whereas supply-side programs place the income initially into the hands of owners of factors of production in the housing industry. Among demand-side programs, moreover, such alternatives as housing allowances, which offer recipients considerable expenditure flexibility, are likely to be more effective than such programs as rent supplements that restrict the use of transfer receipts. Thus it is clear that different types of housing subsidy programs are suggested by the "income maintenance" rationale than are suggested by the "social dynamics" rationale.[12]

The next step is to examine, though briefly, some major housing programs in terms of their consistency with these alternative objectives of housing subsidies. A definitive examination of this point, of course, would require much more analysis than the kind of discursive presentation a paper such as this one can offer. But even without data and empirical tests of the specific hypotheses involved, some tentative views are justified.

In evaluating the redistributive impact of housing programs, two distinctions as to types of programs must be addressed. One such distinction is between such programs as public housing, which concentrate on a particular (low income) segment of the housing market, and such programs as general subsidies to homeowners—including the tax deductibility of mortgage interest—which operate across a wider spectrum of the housing market. In these latter cases, redistributive effects come about primarily through filtering. The second distinction is between those programs that exert their initial impact on tenants and those that initially affect owners.

I have chosen not to consider whether one's relative evaluation of alternative housing programs might be altered once differences in administrative cost among programs are brought into consideration. As a general principle, of course, introduction of administrative costs into the evaluation can change one's rankings of alternative programs. These issues of administration—which include the piggybacking of effective marginal tax rates, problems of policing and privacy, and the costs of operating a bureaucracy—are common to all discussions of the desirability of programs of in-kind transfers, so they do not seem to call for separate conceptual discussion in a paper on housing subsidies.

Programs that rely more heavily on market processes would seem more likely to diminish housing segregation, along both income and racial lines. Therefore, such programs will be more effective in generating the aforementioned changes in tastes and behavior, to the extent that housing is able to generate such effects. Within this perspective, a reliance on filtering seems preferable to ghetto displacement. Moreover, programs like the leasing of privately owned housing by public authorities for rental to the lower income families may be necessary to set up the Coleman-effects discussed earlier. Leasing, as de Leeuw and his colleagues have shown,[13] is also less expensive than the alternative of building new housing expressly for low income families, and would appear to be a preferable program on grounds of cost as well.

Where one focuses on changes in the quality of existing housing, rather than on the supply of new housing, marginal improvement in quality seems to offer an opportunity for the creation of significant external benefits. For example, subsidization of maintenance and rehabilitation within neighborhoods that have not deteriorated beyond the point of no return may both promote desirable demonstration effects and stimulate civic pride and community orientation. With demand-related programs, by contrast, one is less assured that the transfers will be used in ways that generate the changes in tastes and behavior that are required to justify the use of housing as a transfer vehicle in the first place.

[11] Since we can safely assume that unsatisfactory housing, implying problems of sanitation, health, crime, etc., provides disutility to those who live in it as well as to those who observe it, the degree to which taxpayer-donors are concerned with housing only because of selfish motives (as opposed to concern for the residents) need not be discussed separately here.

[12] The de Leeuw, Leeman, and Blank paper is a good discussion of how well different housing allowance programs perform in terms of different program objectives.

[13] Frank de Leeuw and Sam H. Leeman, "The Section 23 Leasing Program," (Washington, D.C.: The Urban Institute), March 1973.

On the other hand, demand-related transfers through housing subsidies will generally be more effective in promoting redistribution per se, for they put the funds directly into the hands of the recipients. But the more flexibility such programs give recipients, the closer they approach monetary transfers, and the smaller their housing effects are likely to be. Compared with cash transfers, such programs as housing allowances and rent supplements are inefficient means of income maintenance per se—although they may be efficient in the broader frame of reference. And the more effective housing allowances become as instruments of a given amount of redistribution, the less effectively they perform in alleviating external diseconomies, which was the justification for adopting them rather than some other instruments of redistribution in the first place.

Whether programs that subsidize landlords, with the intention that they be passed on to tenants, are as efficacious in accomplishing redistribution as are allowances paid directly to tenants is a moot question. With homeowners or landlords, the expenditures are more certain to be directed toward housing. After allowing for shifting of initial expenditures, however, it is uncertain whether the subsidies are distributed as intended, and careful study would be required to resolve this issue. If tenants are subsidized, however, earmarking may be more difficult, unless the subsidy is given some sort of supplement linked to marginal housing expenditure.

Conclusion

The primary conclusion yielded by this evaluation is that the specific case for using housing subsidies—rather than cash transfers or in-kind transfers of other types—as instruments of income redistribution hinges on their long term environmental effect, on whether population diffusion and demonstration effects would indeed bring about the kinds of changes in the behavior of the low income population that taxpayer-donors desire. Such behavioral evidence, being long term, is inherently difficult to obtain. Because the issue is fundamental to the justification of housing subsidies, however, it would seem valuable to invest research resources in trying to ascertain probable answers to such noneconomic questions. This might entail long term experiments and pilot projects.

Exclusionary Zoning: State of the Art, Strategies for the Future

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Introduction

Perhaps few contemporary issues have been subject to as much vitriolic debate [1] as zoning, especially exclusionary zoning. The latter has been defended as necessary for fiscal,[2] ecological, and esthetic considerations [3] and condemned as exacerbating racial and social polarization.[4] In this emotional atmosphere, detached analysis—though sorely needed—has often been lacking.

This study, in an attempt to respond to that need, examines the issue of local zoning and evaluates strategies that have been and could be taken to modify local land use controls. Initially it describes zoning's current state of the art by analyzing the following topics: The development of local zoning; the definition of exclusionary zoning; types of growth-limiting land use controls employed by municipalities; the justifications given by these municipalities for their exclusionary policies; the allegedly harmful effects of such policies; and the changing attitudes of the courts toward exclusionary zoning.

* The section of this paper on fair-share housing plans, pages 341–350, has been published as a separate article: David Listokin, "Fair-Share Housing Distribution: Will It Open the Suburbs to Apartment Development?" *Real Estate Law Journal,* Spring 1974, pp. 739–59.

This study's second section focuses on policies that have been taken to counteract exclusionary zoning's allegedly harmful effects. Specifically, it focuses on a number of fair-share plans that have been either effected or proposed by States, county planning boards, and others. We then consider whether Federal intervention is necessary given these State actions and, if necessary, what exactly should be done.

Zoning Exclusionary Zoning—State of the Art

Development of Local Zoning

Origins of Local Zoning: American local municipalities, up until the late 19th century, enacted practically no formal land use controls. A survey of planning during this period concluded that "apart from building regulations designed to prevent conflagrations in the densely settled areas of the city, governments had almost no inclination or capacity to regulate the use of land or to take steps to correct abuses." [5] The rapid expansion of cities following the Civil War, however, made this laissez-faire approach increasingly unrealistic and untenable. So New York City, Washington, D.C., Boston, and other cities, in the period between 1867 and 1908, enacted statutes regulating such conditions as the maximum tenement lot coverage and the maximum heights of buildings.[6]

These statutes, although welcomed by numerous city officials and planners, were seen by some as needing supplementary comprehensive zoning ordinances that would rationally segregate the city's land area into residential, industrial, and commercial sectors. Influential municipal merchants felt that the uncontrolled mixing of land uses threatened the success of their retail establishments and, consequently, devalued their parcels' worth. To prevent such downgrading, businessmen lobbied for the passage of zoning ordinances.[7] Their efforts met with considerable success, most notably in New

[1] *New York Times,* Jan. 18, 1970, Mar. 1, 1970, July 29, 1970; *Newark Sunday News,* Apr. 25, 1971.

[2] Norman Williams, Jr. and Edward Wacks, "Segregation of Residential Areas Along Economic Lines: Lionshead Lake Revisited," *Wisconsin Law Review,* Vol. 1969, pp. 838–839.

[3] David Becker, "The Police Power and Minimum Lot Size Zoning, Part I: A Method of Analysis," *Washington University Law Quarterly,* Vol. 1969, pp. 283–284; Norman Marcus, "Exclusionary Zoning: The Need for a Regional Planning Context," *New York Law Forum,* Vol. 16, No. 4, 1970, pp. 732–733.

[4] "The New Jersey Judiciary's Response to Exclusionary Zoning," *Rutgers University Law Review,* Vol. 25, No. 1, Fall 1970, pp. 172–173.

[5] William Goodman and Eric Freund, *Principles and Practice of Urban Planning* (Washington, D.C.: International City Managers Association, 1968), p. 15.

[6] Ibid., p. 17.

[7] For excellent analyses of both early and more current zoning lobbying efforts; see Stanislaw Makielski, *The Politics of Zoning: The New York Experience* (New York: Columbia University Press, 1966); Stanislaw Makielski, "Zoning: Legal Theory and Political Practice," *Journal of Urban Law,* Vol. 45, 1967; Seymour Toll, *Zoned America* (New York: Grossman Publishers, 1969); Richard Babcock, *The Zoning Game: Municipal Practices and Policies* (Madison, Wis.: University of Wisconsin Press, 1966); Sidney Wilhelm, *Urban Zoning and Land Use Theory* (New York: Press of Glencoe, 1962).

York City, where the Fifth Avenue Association spearheaded a campaign that resulted in the passage in 1916 of the Nation's first comprehensive zoning provisions.[8]

Growth of Local Zoning: In the 1920's, numerous States passed statutes authorizing municipalities and other local units of government to enact zoning ordinances. Most of these enabling statutes were modeled after the Standard State Zoning Act, which had been published in 1924 (later revised in 1926) by the U.S. Department of Commerce.[9] This model enabling act, often adopted verbatim as State law, broadly granted municipalities the right to zone so long as such zoning promoted the "health, safety, morals or the general welfare of the community."

The passage of these State zoning enabling statutes, combined with the increasing thrust by municipalities to control their physical environment, swelled the initial trickle of cities enacting zoning ordinances into a flood; by 1925, 368 municipalities had zoning ordinances.[10] The United States Supreme Court decision in 1926, *Village of Euclid* v. *Ambler Realty Co.*,[11] which ruled that zoning was a justifiable police power, led still more municipalities to turn to zoning; by the end of 1930, over 1,000 municipalities had enacted zoning ordinances.[12] Today local zoning has become almost a universal municipal practice.[13] A 1968 survey revealed that 76 percent of the Nation's municipalities and over 80 percent of the Nation's townships had zoning ordinances.[14] And in addition to enacting zoning regulations, many local units of government, in order to regulate their growth and physical appearance, also have adopted subdivision regulations and other controls (see Exhibits 1–1 and 1–2).

The growing number of municipalities enacting land use control has been especially evident in States experiencing rapid growth. In New Jersey, for example, only 13 percent of the state's municipalities had zoning ordinances in 1925; by 1971, 96 percent had enacted zoning statutes. And there was a similar upsurge in the percent of municipalities enacting subdivision regulations (see Exhibit 1–3).

What is Exclusionary Zoning?

Exclusionary Zoning Defined: Exclusionary zoning has been defined largely in terms of effect. Lawrence Sager of New York University Law School, for example, defines it as "zoning that raises the price of residential access to a particular area and thereby denies that access to members of low income groups." [15] Similarly, Norman Williams of Rutgers University describes exclusionary zoning as those land use controls "which appear to interfere seriously with the availability of low and moderate cost housing where it is needed." [16] And Robert Hirshen of the University of Michigan defines it as that "practice which results in closing the suburban housing market to low and moderate income housing." [17]

For the purposes of this study, exclusionary zoning will be defined as those land use controls aimed at restricting the entry or construction of low and moderate income housing which have been or most probably would be ruled unlawful because of their failure to satisfy the judicially approved objectives of such land use.[18]

Our definition assumes that it is both erroneous and misleading to define exclusionary

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[8] While New York City is credited with passing the Nation's first comprehensive zoning statute in 1916, Los Angeles in 1915 had already, in fact, zoned its entire area in one way or another. See the National Commission on Urban Problems, *Building the American City* (Washington, D.C.: U.S. Government Printing Office, 1968), p. 220.

[9] U.S. Department of Commerce, A Standard State Zoning Enabling Act Under Which Municipalities May Adopt Zoning Regulations Σ1 (1926).

[10] National Commission on Urban Problems, *Building the American City*, p. 200.

[11] 272 U.S. 365 (1926).

[12] National Commission on Urban Problems, *Building the American City*, p. 200.

[13] In Hawaii zoning is a State activity. The State land use commission assigns different land areas to one of four land use districts (urban, rural, agricultural, and conservation). See Robert Walsh, "Are Local Zoning Bodies Required by the Constitution to Consider Regional Needs?" *Connecticut Law Review*, Vol. 3, No. 2, Winter 1970–71, p. 256; Jay Sandak, "Exclusionary Zoning: A Legislative Approach," *Syracuse Law Review*, Vol. 23, 1971, pp. 590–591; James Coke and John Gargan, *Fragmentation in Land Use Planning and Control* prepared for the National Commission on Urban Problems, Research Report No. 18 (Washington, D.C.: U.S. Government Printing Office, 1969), pp. 57–58; National Commission on Urban Problems, *Building the American City*, p. 209.

[14] Allen Manvel, *Local Land and Building Regulations* prepared for the National Commission on Urban Problems, Research Report No. 6, (Washngton, D.C.: U.S. Government Printing Office, 1968), p. 23.

[15] Lawrence Sager, "Tight Little Islands: Exclusionary Zoning, Equal Protection and the Indigent," *Stanford Law Review*, Vol. 21, No. 4, April 1970, p. 767.

[16] Norman Williams and Thomas Norman, "Exclusionary Land Use Control: The Case of North Eastern New Jersey," *Syracuse Law Review*, Vol. 22, No. 2, 1970–71, p. 478.

[17] Robert Hirschen, "The Interrelationship Between Exclusionary Zoning and Subdivision Control," *University of Michigan Journal of Law Reform*, Vol. 5, No. 2, Winter 1972, p. 354.

[18] It could be objected that our definition of illegal zoning, which includes those controls that most probably would be invalidated by the courts as well as those that have already been invalidated is a very vague definition. The authors agree that there very well may be debate over what controls most probably would be invalidated by the courts. But, we feel that almost any definition of exclusionary zoning will contain judgmental factors.

Exhibit 1–1. Numbers and Percent Distribution of Local Governments with Planning, Zoning, and Building Regulation Activities, 1968

Coverage Group	Governments with— Planning Board		Zoning Ordinance		Subdivision Regulation		Building Code		Housing Code		Any Building Regulation [1]	
Number of governments: Total [2] and Percent (Percents are in parentheses)	10,717	(100.0)	9,595	(100.0)	8,086	(100.0)	8,344	(100.0)	4,904	(100.0)	14,088	(100.0)
Within SMSA's	4,923	(46.3)	5,199	(54.2)	4,509	(55.8)	4,527	(54.3)	2,780	(56.7)	6,264	(44.5)
Outside SMSA's	5,754	(53.7)	4,396	(45.8)	3,577	(44.2)	3,817	(45.2)	2,124	(43.3)	7,834	(55.5)
County Governments	1,596	(14.9)	711	(7.4)	886	(11.0)	415	(4.9)	211	(4.3)	1,796	(12.2)
Municipalities	6,673	(63.3)	6,880	(71.7)	5,297	(65.5)	6,484	(77.7)	3,976	(81.1)	8,985	(63.2)
1960 population of 1,000 or more	6,167	(57.5)	6,140	(64.0)	4,894	(60.5)	5,770	(69.2)	3,470	(70.8)	7,827	(55.6)
Under 1,000 (in SMSA's)	506	(4.7)	740	(7.7)	403	(5.0)	714	(8.6)	506	(10.3)	1,078	(7.7)
New England-type townships	2,448	(22.8)	2,004	(19.8)	1,903	(23.5)	1,445	(17.3)	717	(14.6)	3,387	(24.0)
1960 population of 1,000 or more	2,359	(22.0)	1,815	(18.9)	1,827	(22.6)	1,356	(16.3)	666	(13.6)	3,273	(23.2)
Under 1,000 (in SMSA's)	89	(.8)	89	(.9)	76	(.9)	89	(1.1)	51	(1.0)	114	(8.0)

[1] These figures cover units reporting any of the other specified types of activity or a local building-permit system.
[2] The "Total" relates to governments subject to sample survey representation, and thus omits (a) all municipalities and townships of less than 1,000 population located outside of SMSA's; and (b) township governments located in States where these governments lack municipal type powers.

Source: Allen D. Manvel, National Commission on Urban Problems, Research Report No. 6, *Local Land and Building Regulations.*

zoning solely as a suburban practice, in the manner of Hirshen. While suburbs have been the most visible practitioners, nonsuburban municipalities have also, on occasion, promulgated exclusionary zoning ordinances and are likely to continue to do so. But more importantly, our definition includes the notion of illegality, for it is insufficient to say that exclusionary zoning is characterized by its restrictive effect, since all zoning has some restrictive affect on land use.[19] And our definition, by noting the objective of exclusionary zoning—restricting the entry or construction of low and moderate income zoning—illuminates the distinction between exclusionary zoning and other illegal land use practices, such as spot zoning.

Exclusionary Zoning: Specific Devices: There is a wide repertoire of exclusionary land use controls.[20] A recent law review article [21] listed the following exclusionary zoning devices: Minimum lot size requirements, minimum building size requirements, prohibition of multiple-family dwellings, and various provisions in building codes. Other sources have cited floating or "non-Euclidean" zoning as an exclusionary zon-

[19] Bernard Siegan, *Land Use Without Zoning* (Lexington, Ky.: D. C. Heath and Co., 1972).

[20] See Notes, "Exclusionary Zoning and Equal Protection," *Harvard Law Review*, Vol. 84, No. 7, May 1971, pp. 1645–1646; Richard Babcock and Fred Bosselman, "Suburban Zoning and the Apartment Boom," *University of Pennsylvania Law Review*, Vol. III, 1963, pp. 1060–1061; Wiley Mayne, Jr., "The Responsibility of Local Zoning Authorities to Nonresidence Indigents," *Stanford Law Review*, Vol. 23, April 1971, p. 776; Bartke, Richard, and Gage, Hilda, "Mobile Homes: Zoning and Taxation," *Cornell Law Review*, Vol. 55, 1970; Notes, "Suburban Zoning Ordinance and Building Codes: Their Effort on Low and Moderate Income Housing," *Notre Dame Lawyer*, Vol. 45, 1969, pp. 123+; Williams and Norman, "Exclusionary Land Use Controls," pp. 481–484, Norman Williams, Jr., "The Three Systems of Land Use Control," *Rutgers Law Review*, Vol. 25, No. 1, 1970, pp. 92–95; National Commission on Urban Problems, *Building the American City*, pp. 211–217. For an early study on exclusionary zoning see Norman Williams, "Planning Law and Democratic Living," *Law and Contemporary Problems*, Vol. 20, 1955, pp. 317+.

[21] Frank Aloi and Arthur Abba Goldberg, "Racial and Economic Exclusionary Zoning: The Beginning of the End?" *Urban Law Annual*, Vol. 1971, pp. 3+.

Exhibit 1–2. Proportion of Governments with Planning, Zoning, and Building Regulation Activities, by SMSA Location and Type and Size of Government, 1968

		Percent of governments with—					
Coverage Group	Number of Governments	Planning Board	Zoning Ordinance	Subdivision Regulation	Building Code	Housing Code	and Building Regulation [1]
Total [2]	17,998	59.6	53.3	44.9	46.4	27.3	78.3
Within SMSA's	7,609	65.2	68.3	59.3	50.5	36.5	82.3
Outside SMSA's	10,384	55.4	42.3	34.4	36.8	20.5	75.3
County Governments	3,049	52.3	23.3	29.1	13.6	6.9	58.9
Within SMSA's	404	80.0	49.3	62.9	39.4	18.6	89.2
Outside SMSA's	2,645	28.1	19.4	23.9	9.7	5.1	54.7
Municipalities	9,984	66.8	68.9	53.1	64.9	39.8	89.2
Within SMSA's	4,977	67.7	74.8	61.2	69.0	44.8	86.2
1960 population							
50,000 or more	314	98.4	98.7	92.7	98.7	85.3	100.0
5,000 to 49,999	1,303	92.9	97.0	90.0	91.8	53.3	99.9
Under 5,000	3,360	54.9	54.0	47.7	57.4	37.8	79.5
Outside SMSA's	5,007	66.0	63.0	45.0	60.9	34.8	92.2
1960 population							
5,000 to 49,999	1,352	91.8	90.5	81.9	73.5	54.4	98.4
1,000 to 4,999	3,675	56.5	52.9	31.3	51.3	27.6	89.3
New England-type twp	4,960	49.4	40.4	38.4	29.1	14.5	68.3
Within SMSA's	2,228	57.1	57.3	54.3	41.0	21.2	73.0
1960 population							
5,000 or more	765	79.1	81.0	74.0	58.7	22.7	91.5
Under 5,000	1,463	45.7	44.8	44.0	33.5	20.4	63.3
Outside SMSA's	2,732	43.0	26.6	25.4	18.7	8.9	64.4

[1] These figures cover units reporting any of the other specified types of activity or a local building-permit system.

[2] The "total" relates to governments subject to sample survey representation and thus omits (a) all municipalities and townships of less than 1,000 population located outside of SMSA's; and (b) township governments located in States where these governments lack municipal-type powers.

Source: Allen D. Manvel, National Commission on Urban Problems, Research Report No. 6, *Local Land and Building Regulations*.

ing strategy.[22] The following discussion will focus on the most significant of the allegedly exclusionary devices.[23]

Minimum Building Requirements: Many municipalities require that new buildings be constructed with a minimum amount of floor space. A 1968 national survey, for example, concluded that almost half of the bodies of government that had zoning ordinances required a minimum floor area for single-family houses[24] (see Exhibit 1–4). Municipalities in rapidly growing States almost universally zone for minimum building floor area. A 1970 New Jersey survey, for example, revealed that over 90 percent of the State's developable land was zoned for a minimum floor area.

Minimum floor requirements are not, per se, exclusionary zoning; as researched by the American Public Health Association[25] and others, minimum floor areas are frequently dictated by standards of health. The exclusionary label is often applied to minimum floor requirements because they needlessly raise the cost of new housing so that it can be afforded only by middle and higher income families.[26] In many instances, the zoned minimum floor area requirements far exceed the minimum required for health reasons. In New Jersey, for example, in 1970, almost one-fifth of the State's developable

[22] Non-Euclidean or floating zoning is zoning that makes a provision for a particular land use, e.g., multifamily zoning, but does not specify the exact location of that land use. See Notes, "Exclusionary Zoning and Equal Protection," p. 1646, and Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1060.

[23] See Williams and Norman, "Exclusionary Land Use Controls." For an empirical study of the impact of numerous land use controls on housing cost see George Sternlieb and Lynn Sagalyn, *Zoning and Housing Costs: The Impact of Land Use Controls on Housing Price* (New Brunswick, N.J.: Rutgers University, Center for Urban Policy Research, 1972).

[24] National Commission on Urban Problems, *Building the American City*, p. 215.

[25] American Public Health Association, Committee on the Hygiene of Housing, *Planning the Home for Occupancy* (Washington, D.C.: American Public Health Association, 1950).

[26] National Commission on Urban Problems, *Building the American City*, p. 215.

Exhibit 1–3. Zoning and Subdivision Control in New Jersey*

Year	Percent Having Zoning Ordinance	Percent Having Subdivision Controls
1925	12.5 [1]	NA
1939	35.0 [2]	12.1 [2]
1946	NA	23.2 [3]
1947	45.3 [4]	NA
1960	75.3 [5]	NA
1964	NA	80.0 [3]
1971	96.0 [6]	85.0 [6]

* All municipalities sampled.

NA = information not available.

Sources: (1) *State of New Jersey Department of Commerce Report*, 1925. (2) *Municipal and County Planning Legislation and Procedures in New Jersey*, 1939. (3) *Administrative Guide to Subdivision Regulation* (New Jersey Department of Community Affairs) p. 2, 3. (4) *Zoning In New Jersey—1960* (New Jersey Department of Community Affairs). (5) *Zoning In New Jersey—1967* (New Jersey Department of Community Affairs), p. 37. (6) Rutgers CUPR: *Municipality Survey—1971*. Cited from George Sternlieb and Lynne Sagalyn, *Zoning and Housing Costs: The Impact of Land Use Controls on Housing Price* (New Brunswick, N.J., Rutgers University, Center for Urban Policy Research, 1972).

land had a minimum floor size zoning requirement of 1,400 or more square feet, an amount that, according to the American Public Health Association, was needed only by families of five or more people. It is charged that these excessive minimum floor area requirements are often imposed to raise the cost of housing, making it inaccessible to low and moderate income families.

Minimum Lot Size Requirements: Many communities specify the minimum lot size on which housing can be constructed. These minimum lot sizes are frequently quite large. The Regional Plan Association's 1962 study of the 17-county New York Metropolitan regions, for example, revealed that one-fourth of the metropolitan residential areas was zoned for lots of 1 acre or larger, and almost one-fifth was zoned for lot sizes of 2 acres or larger.[27]

Other studies have revealed similar findings. A Connecticut survey revealed that 92 percent of the State's land was zoned for lot sizes of an acre or more.[28] With few exceptions, Philadelphia's suburbs have zoned all of their undeveloped land for single units in one-half acre or larger lots.[29] And a 1968 national survey showed the following: [30]

> 25 percent of metropolitan area municipalities of 5,000 plus permit *no* single family houses on lots of less than one-half acre. Of these same governments, 11 percent have some 2-acre zoning; 20 percent have some 1- to 2-acre zoning; 33 percent have some one-half to 1-acre zoning; and more than 50 percent have some one-fourth to one-half acre zoning.

Large lot zoning has often been condemned as an exclusionary zoning practice [31] in that required lot size is not justifiable from the standpoint of health, ecology, or aesthetics. Critics charge that large lot sizes are mandated in order to raise the price of housing to a level affordable only by middle or higher income families. Large lot size raises housing cost for the following reasons: [32] By decreasing the number of houses that can be built in a community, large lot zoning raises the demand and hence the price of land, which in turn will increase the cost of housing because it often increases the average frontage per lot and hence improvement costs; [33] large lot requirements therefore increase the total housing cost, and builders understandably avoid building comparatively cheap housing on large, expensive lots.

Subdivision and Frontage Regulations: Subdivision regulations are those that determine the number of linear feet of various improvement, e.g., street paving and sewers, which are required to serve a given house as well as the

[27] Regional Plan Association, *Spread City* (New York, N.Y.: Regional Plan Association, 1962), p. 40. See also Linda and Paul Davidoff, "The Suburbs Have to Open Their Doors," *The New York Times Magazine*, Nov. 7, 1971, p. 41; and Curtis Berger, *Land Ownership and Use Cases, Statutes and Other Materials* (Boston, Mass.: Little, Brown and Co., 1968), pp. 686–690; "Availability of Land for Housing for Low and Moderate Income Families," in President's Committee on Urban Housing, *Technical Studies Vol. II*, pp. 287–409; Santa Clara County Planning Department, *Zoning and Housing* (Santa Clara, Calif.: December 1970); Plainfield, N.J., Planning Division, *Suburban Zoning Practices Surrounding Plainfield* (Jan. 5, 1971).

[28] "Battle to Open the Suburbs: New Attack on Zoning Laws," *U.S. News and World Report*, Vol. 68, June 22, 1970, p. 39.

[29] "The Subsidized Noose—Priced Out, Zoned Out, How the State Subsidizes Exclusionary Suburbs," *Infill*, Spring 1973, p. 13. A recent New Jersey zoning survey reached similar results. See New Jersey Department of Community Affairs, *Zoning Survey 1970*.

[30] U.S. National Commission on Urban Problems, *Building the American City*, p. 214.

[31] Norman Williams and Thomas Norman have argued that the actual impact of large lot size requirements on driving up housing costs is questionable. See Williams and Norman, "Exclusionary Land Use Controls," pp. 3+.

[32] U.S. National Commission on Urban Problems, *Building the American City*, p. 214.

[33] Ibid. See Table 7, p. 214. Williams and Norman believe that larger lots are usually, though not necessarily, wide and hence they believe that lot size may sometimes increase housing costs by increasing the average frontage per lot. See Williams and Norman, "Exclusionary Land Use Controls," footnote 17.

Exhibit 1–4. Percent of Zoning Municipalities and New England-Type Townships of 5,000-Plus having Selected Minimum Floor Area Requirements in their Zoning for 1-Story, Single-Family Houses, by Size, Type, and Location of Government: 1967

Minimum Floor Area	All zoning govern-ments	Within SMSA's Total	Within SMSA's Municipalities 50,000 plus	Within SMSA's Municipalities 5,000 to 49,999	Within SMSA's Town-ships	Outside SMSA's Total	Outside SMSA's Munici-palities	Outside SMSA's Town-ships
1,000 sq. ft. or more	7.6	8.8	6.5	11.4	4.8	5.8	4.5	12.2
800 to 999 sq. ft.	13.5	17.5	5.5	17.7	23.1	7.4	5.1	18.7
600 to 799 sq. ft	15.8	17.6	9.7	12.3	32.4	13.0	13.4	11.0
Under 600 sq. ft.	3.9	3.6	5.8	2.9	3.9	4.4	4.0	6.5
Applicable, but areas not reported [1]	4.4	4.6	1.0	6.0	3.7	3.9	3.8	4.9

[1] These governments had a minimum floor area requirement but did not specify its size in response to the survey.

Source: Allen D. Manvel, National Commission on Urban Problems, Research Report No. 6, *Local Land and Building Regulations.*

amount of land within a subdivision that can actually be devoted to housing.

Many municipalities also control lot width by imposing frontage requirements. The impact of frontage regulations on housing costs largely depends on the municipality's subdivision requirements; if the latter are severe, then a large frontage requirement will have a fairly significant impact on housing costs. These differences in municipal subdivision regulations notwithstanding, however, a recent New Jersey study concluded [34] that lot front requirements had one of the most significant impacts on housing costs.

Subdivision and frontage regulations can and do insure that new houses are adequately served by roads, streets, and sewers; and they can reduce suburban sprawl as well. But detractors deplore their frequent use in order to raise housing costs primarily to exclude families of limited means.[35]

Exclusion of Multiple Dwellings: Multiple dwellings are generally the most readily affordable housing to low and moderate income families. Because many communities impose severe restrictions on the number of multiple-family units that can be constructed—while others completely zone out multifamily construction—there is a dearth of sites for such construction, especially in suburban areas. In New Jersey, for example, in 1970, less than 4 percent of the available zoned land was earmarked for multifamily construction. And a New York metropolitan survey similarly revealed that of the undeveloped land zoned for residential purposes, 99 percent was restricted to single family dwellings.[36]

Despite the protestations of the practioners that multiple-family housing restrictions are based on sound fiscal, esthetic, and ecological considerations, critics have charged that multiple dwellings have been restricted precisely because they are the only kind of housing accessible to low and moderate income families.[37]

Exclusion of Mobile Homes: Mobile homes, an increasingly important segment of the housing market, are probably the major important source of new housing for comparatively low income families.[38] Yet, as with multifamily housing, many communities either zone out mobile homes or severely restrict the number of mobile units allowed. A New York State survey, for example,

[34] Sternlieb and Sagalyn, *Zoning and Housing Costs.*

[35] U.S. National Commission on Urban Problems, *Building the American City,* p. 216; Williams and Norman, "Exclusionary Land Use Controls."

[36] U.S. National Commission on Urban Problems, *Building the American City,* p. 215.

[37] See U.S. National Commission on Urban Problems, *Building the American City,* p. 215; Williams and Norman, "Exclusionary Land Use Controls"; Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," *Symposium.* "Apartments In Suburbia: Local Responsibility and Judicial Restraint," *Northwestern University Law Review,* Vol. 59, No. 3, July-August 1964, pp. 344–367; John A. Parkins, Jr., "Judicial Attitudes Toward Multiple-Family Dwellings: A Reappraisal," *Washington and Lee Law Review,* Vol. 28, No. 1, April 1971, pp. 220–230; "Zoning—Need for Low Income Housing Held to be a Special Reason to Support a Use Variance Within the Meaning of N.J. Rev. Stat. § 40:55–39 (d)," *Rutgers Camden Law Journal,* Vol. 2, No. 3, Fall 1970, pp. 400–412.

[38] See Frederick Bair, "Mobile Homes and the General Housing Supply; Past, Present and Outlook," (Chicago Mobile Homes Manufacturers' Association, 1970); Margaret Drury, *Mobile Homes: The Unrecognized Revolution in American Housing* (Ithaca, N.Y.: Cornell University Press, 1967); Constance Gibson, *Policy Alternatives for Mobile Homes* (New Brunswick, N.J.: Rutgers University, Center for Urban Policy Research, 1971); Earl Morris and Margaret Woods (editors), "Housing Crisis and Response—The Place of Mobile Homes In American Life" (Ithaca, N.Y.: New York State College of Human Ecology at Cornell University, 1971).

revealed that of the 237 zoning ordinances studied, more than half either explicitly or implicitly excluded mobile homes.[39] Such restriction has often been criticized as exclusionary in both intent and effect.[40]

Other Exclusionary Devices: Antiquated building codes that incorporate inefficient and costly housing codes often exclude moderate income families by elevating the cost of housing.[41] Floating zones for multiple-family and similar needed housing often serve to exclude such housing. And lengthy, complicated zoning administrative procedures have been accused of indirectly inflating housing costs by increasing the cost and time needed to make zoning amendments and obtain variances.[42]

Exclusionary Zoning: Municipal Justifications

The previous description of the prevalance of exclusionary land use controls begs the question of why such controls have been enacted. This section analyzes the municipal justifications for exclusionary zoning.

Explicit Justifications: Following are some explicit justifications.

Budgetary Considerations: On the average, local governments derive a considerable amount —87 percent[43]—of their revenue from local property taxes. In recent years, as governmental expenditures have mushroomed, local property taxes have skyrocketed. In New Jersey, for example, between 1960 and 1970, the total property taxes collected doubled and there was a large increase in the equalized local tax rate.[44] And New Jersey is not atypical—the Nation's $40 billion current total property taxes collected are double that of a decade ago.[45] To stem even larger increases in property taxes, communities have often enacted larger lot and other exclusionary zoning controls in the belief that such controls would restrain municipal expenditures and would insure that projected housing units would yield property taxes at least equal to the municipal expenditures they would incur.

Restrain Municipal Expenditures: Many municipalities believe that houses built on large lots require fewer and cheaper municipal services than multifamily and other comparatively high density residential developments.[46] Large lot houses, for example, often relying on septic tanks, preclude the need for municipal construction of costly sewer plants. Considerations such as these have impelled municipalities to enact exclusionary land use controls, e.g., large lot requirements and restrictions on multifamily housing.

Yield High Property Taxes: Many local officials are persuaded that expensive, single family houses built on large lots are good ratables[47]—yielding more property tax revenue than the municipal expenditures they incur. Conversely, they assume that inexpensive single-family homes on small lots and 3–4 bedroom multifamily units at increased densities are poor ratables—incurring greater municipal services than the property taxes they yield. Hence, to stem local property tax increases, municipal officials often have enacted exclusionary controls restricting or prohibiting the construction of these less desirable ratables while encouraging or permitting the construction of only the more preferred ratables.

Aesthetic Justifications: Communities practicing exclusionary zoning often defend their actions on the grounds of esthetic considerations. Municipal officials in such communities, for example, frequently assert that their major concern is to preserve the rural character of the area by retaining large open space and by reducing traffic.[48] Their exclusion of multifamily housing is almost universally justified on esthetic (as well as for fiscal) reasons; they maintain that

[39] U.S. National Commission on Urban Problems, *Building the American City*, p. 216.

[40] Ibid. and Williams, "The Three Systems of Land Use Control," p. 93; Williams and Norman, "Exclusionary Land Use Controls," pp. 3+.

[41] Richard Cutler, "Legal and Illegal Methods for Controling Community Growth on the Urban Fringe," *Wisconsin Law Review*, Vol. 1961, May 1961, pp. 370+; "Suburban Zoning Ordinances and Building Codes," *Notre Dame Lawyer*. See also Advisory Commission on Intergovernmental Relations, *Building Codes: A Program for Intergovernmental Reform* (Washington, D.C.: U.S. Government Printing Office, 1966).

[42] U.S. National Commission on Urban Problems, *Building the American City*, p. 216.

[43] "The Coming Change in the Property Tax," *Business Week*, Feb. 12, 1972, p. 50.

[44] New Jersey Education Association, *Basic Structural Data of New Jersey School Districts* (Trenton, N.J.: New Jersey Education Association, 1972), p. 15.

[45] "The Coming Change in the Property Tax," p. 50.

[46] Mary Brooks, "Exclusionary Zoning," *ASPO* Report No. 254, February 1970, p. 6.

[47] Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1062; "Exclusionary Zoning and Equal Protection," p. 1667; Williams and Wacks, "Segregation of Residential Areas Along Economic Lines," pp. 838–839; Arthur Lazerow, "Discriminatory Zoning: Legal Battleground of the Seventies," *American University Law Review*, Vol. 21, No. 1, September 1971, p. 167; "Large Lot Zoning," p. 1421; "Danger Zoning," *The Record*, Aug. 3, 1970.

[48] Brooks, *Exclusionary Zoning*, p. 7; Schoenbrod, "Large Lot Zoning," p. 1420; "Snob Zoning," p. 252; "Exclusionary Zoning and Equal Protection," p. 1667; Babcock and Bosselman, "Exclusionary Zoning and the Apartment Boom," p. 1067.

such high-rise housing will cut off light and air and will increase traffic congestion.[49]

Ecological Justifications: [50] The topography of some communities necessitates their strict limitation on the density of development in order to prevent dangerous flooding and sewer conditions. Municipal officials in such communities often have enacted zoning statutes which in effect may be exclusionary but which are defended on the grounds of environmental protection.[51]

Property Value Consideration: Community officials often believe that land zoned for moderate income housing—e.g., multifamily housing—depresses the value of adjacent properties. Conversely, they believe that exclusionary zoning, by limiting housing construction to high-priced dwellings raises the value of both the property and its adjacent land. Consequently, in an attempt to insure property value stability and to appreciate local property values, many communities enacted large lot and comparable zoning ordinances.[52]

Other Explicit Justifications: Among the other justifications communities offer for their exclusionary zoning practices are the following: Such controls are needed for public health and fire prevention reasons; [53] in excluding high density suburban these controls eliminate tomorrow's slums; [54] and that by preserving space and privacy,[55] these controls forestall the anomie and antisocial conduct that accompany the lack of such amenities in many cities.

Implicit Reasons: [56] One of the implicit objectives of exclusionary zoning is the preservation of a racially, socially, and economically homogeneous community by zoning out racial minorities and the poor.[57] Another is the exclusion of multifamily housing that would attract transient families with no firm interest in their neighborhood.[58] These and other implicit objectives [59]—as well as the aforementioned explicit justifications—often dictate the pattern of suburban land use controls as one article concluded:

> By the simple device of large lot zoning, suburbanites believe that a municipality can achieve its developmental goals in a single stroke. The community will be beautiful, its taxes will be low, and "undesirables" will be kept out. Minimum lot-size zoning requirements become the keystone for the arch, the focus of strong pressures for larger and larger lots, an extraordinarily salient feature of the suburban political process.[60]

But as we shall soon see, exclusionary zoning has many vocal critics. Before examining the latter's specific charges, we shall first overview national demographic and social trends accompanying the growth of restrictive land use controls.

The Context: Outmigration to the Suburbs: A discussion of outmigration to the suburbs follows.

Urban-Surburban Population Shift: Since 1910, cities have been growing at a much slower rate than have the suburbs; sometimes they have actually experienced a drop in population. Only in the first decade of this century, between 1900 and 1910, did the central cities outpace the suburbs.[61] Between 1940 and 1960, suburban growth rates far outstripped those of central cities; between 1950 and 1960, the central city rate, for example, was less than one-fourth the growth rate of suburban areas. Some cities not only grew slower than their suburban neighbors, but in fact declined in population. In the 1950's, population losses were recorded in eight of the 10 largest American cities,[62] including New York,[63] Chicago, Philadelphia, and Detroit.

The 1970 census demonstrates that the trend continues unabated. In the Nation's standard metropolitan statistical areas, between 1960 and 1970 the central cities' populations increased by 6 percent while the population of areas outside central cities increased 27 percent.[64] And as in previous decades, many central cities experienced an absolute decline in population;

[49] Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1065.

[50] Brooks, *Exclusionary Zoning,* p. 7.

[51] Large lot and similar zoning has also been defended for another ecological reason—historic preservation. See Marcús, "Exclusionary Zoning," pp. 732+.

[52] Coke and Gargan, *Fragmentation in Land Use Planning and Control,* pp. 13–14; Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1067; Schoenbrod, "Large Lot Zoning," p. 1421; Williams and Wacks, "Segregation of Residential Areas Along Economic Lines," p. 838.

[53] See the arguments in *Simon* v. *Needham,* 311 Mass. 560, 42 N.E. 2d 516 (1942).

[54] Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1065.

[55] Brooks, "Exclusionary Zoning," p. 7.

[56] See Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1065.

[57] Schoenbrod, "Large Lot Zoning," p. 1420; Norman Williams, "Planning Law and Democratic Living," *Law and Contemporary Problems,* Vol. 20, 1955, p. 330. Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," p. 1071. George Sternlieb has called the explicit justification of exclusionary zoning the "dance of the seven veils," i.e., attempts to obsecure the fact that the true reason for such zoning is racial and economic segregation. See the *New York Times,* Apr. 19, 1971.

[58] Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," pp. 1069–1070.

[59] Ibid., p. 1072.

[60] James Coke and Charles Liebman, "Political Values and Population Density Control," *Land Economics,* Vol. 37, November 1961, p. 355.

[61] U.S. National Commission on Urban Problems, *Building the American City,* p. 42.

[62] U.S. President's Committee on Urban Housing, *A Decent Home* (Washington, D.C.: U.S. Government Printing Office, 1968), p. 136.

[63] Ibid.

[64] U.S. Department of Commerce, Bureau of the Census, *Number of Inhabitants United States, Summary* (Washington, D.C.: U.S. Government Printing Office, 1971), p. 1–180 (Census Publication PC (1)–A1).

Rochester, N.Y., St. Louis, and Savannah, for example, declined 7, 17, and 21 percent, respectively.[65] That the United States has become a predominantly suburban Nation is borne out by the 1970 census figures, which report 76 million suburbanites as compared to 64 million city dwellers.[66]

Urban-Suburban Racial Shift: Concomitant to the urban growth lag has been the exodus of whites from central cities. In 1950, 12 percent of the central cities' populations was nonwhite; this increased to 17 percent in 1960, 20 percent in 1966, and 21 percent in 1970.[67] And projections to 1985 indicate that the percent of nonwhite population will increase to almost 31 percent.[68]

Urban-Suburban Job Shift: As whites have fled the cities, so have industries. The result has been a large increase in the number of jobs in suburban areas while the number of city jobs has either remained stable or declined. A 1967 study concluded that between 1959 to 1965, industrial employment in 12 central cities grew by 12 percent; in contrast, employment in adjacent suburbs increased by 36 percent.[69] And the 1970 census shows that during the 1960's, suburbs of the Nation's 15 largest metropolitan areas gained more than 3 million jobs—an increase of 44 percent. In contrast, central cities lost 835,000 jobs—a 7 percent decline.[70]

Alleged Effects of Exclusionary Zoning in a Period of Urban-Suburban Shift: Many of the exclusionary controls previously discussed were imposed between 1950 and 1970, a period when the urban-suburban shifts were most prominent. The spread of such exclusionary zoning during this particular period has been blamed for exacerbating the following problems:

National Housing Problem: [71] Exclusionary zoning, by raising the cost of housing, makes it more difficult for minority groups, who often have only moderate incomes, to obtain housing. Some observers have charged that even middle class groups in some areas of the country have been adversely affected by exclusionary land use controls. One law review article, for example, concluded that "exclusionary zoning is a major factor in New Jersey's current housing crisis which affects not only the lower classes . . . but also the greater part of the middle class." [72]

Residential Segregation and Polarization: By creating enclaves of higher priced housing inaccessible to minority group, moderate income families,[73] exclusionary land use controls in the suburbs have been cited as a major contributor to the widening urban-suburban racial schism. According to one law review article:

> [A] closed suburb (through exclusionary zoning) has and will continue to have a serious effect upon life in our Nation. This condition is largely responsible for the continuation of a pattern of inner city racial ghettos and slums.[74]

Central City Educational Problems: The Coleman Report concluded that a major determinant of education quality is the socioeconomic background of the student body.[75] Inner city schools, whose enrollments preponderantly comprise minority group and lower income families, face a Herculean task in instructing such pupils. Because the central city's increasing racial and social homogenization can be at least partially attributed to exclusionary zoning, it has been charged that such zoning has multiplied the

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[65] Ibid., pp. 1–184, 1–185.

[66] *The New York Times*, Oct. 15, 1972.

[67] National Advisory Commission on Civil Disorders, *Report of the National Advisory Commission on Civil Disorders* (New York, N.Y.: Bantam Books, 1968), p. 250. See also U.S. National Commission on Urban Problems, *Building the American City*, p. 43 and U.S. President's Committee on Urban Housing, *A Decent Home*, p. 137.

[68] Patricia Hodge and Philip Hauser, *The Challenge of America's Metropolitan Housing Outlook* (Washington, D.C.: U.S. Government Printing Office, 1968), p. 31 (Research Report No. 3, National Commission on Urban Problems).

[69] U.S. Department of Labor, Bureau of Labor Statstics, "The Decentralization of Jobs," *Metropolis 1985* (Garden City, N.Y.: Doubleday and Co., 1963); Edgar Hoover and Raymond Vernon, *Anatomy of a Metropolis* (Garden City, N.Y.: Doubleday and Co., 1962); National Industrial Conference Board, Inc., *Manufacturing Employment by Type of Location, An Examination of Recent Trends* (New York, N.Y.: National Industrial Conference Board, 1969). For a review of the literature on employment decentralization see Franklin James, *Employment Decentralization, Urban Change and Job Opportunity: A Review of the Literature* (New Brunswick, N.J.: Rutgers University, Center for Urban Policy Research, 1972) (mimeo).

[70] *The New York Times*, Oct. 15, 1972.

[71] See Sager, "Tight Little Islands," p. 781; "Segregation and the Suburbs: Low Income Housing, Zoning and the Fourteenth Amendment," *Iowa Law Review*, Vol. 56, June 1971, pp. 1300, 1303; Mary Brooks, *Exclusionary Zoning*, ASPO (Planning Advisory Service) No. 254, February 1970, p. 24. For a discussion of the locational consideration (urban vs. vacant land) in housing the urban poor, see Anthony Downs, "Housing the Urban Poor: The Economics of Various Strategies," *American Economic Review*, Vol. 56, September 1969, p. 648.

[72] "The New Jersey Judiciary's Response to Exclusionary Zoning," *Rutgers University Law Review*, Vol. 25, No. 1, Fall 1970, p. 172.

[73] "The New Jersey Judiciary's Response to Exclusionary Zoning," p. 172; Sager, "Tight Little Islands," p. 781; Robert Freilich and G. Allen Bass, "Exclusionary Zoning: Suggested Litigation Approaches," *The Urban Lawyer*, Vol. 3, No. 1, 1971, p. 245; Arthur Lazerow, "Discriminatory Zoning: Legal Battleground of the Seventies," *American University Law Review*, Vol. 21, No. 1, September 1971, p. 157.

[74] Frank Aloi, Arthur Goldberg, and James White, "Racial and Economic Segregation by Zoning: Death Knell for Home Rule?" *University of Toledo Law Review*, No. 1, 1969, p. 74.

[75] U.S. Office of Education, *Equality of Educational Opportunity* (Washington, D.C.: U.S. Government Printing Office, 1966), pp. 21–22.

problems implicit in educating inner city youths.[76]

Minority Group Job Opportunities: Many individuals, ranging from former Vice President Spiro Agnew [77] to NAACP head Percy Sutton,[78] have labeled exclusionary zoning a major stumbling block to minority group employment. Their criticism is based on the assumption that many minority group members could be employed if they could only live where there are jobs. Exclusionary zoning, by keeping blacks and other minorities in the cities at the same time that cities have been losing jobs, is thus seen as a strategy exacerbating the minority group employment problem.[79] One law review article,[80] for example, charged that:

> Because low cost housing is not widely available in the suburbs, (as a result of exclusionary zoning) many inner city workers are confronted with the choice of commuting to work—the expense and inconvenience of which may be prohibitive—or doing without work altogether. This contributes to the severe problem of unemployment in the central cities.

Exclusionary Zoning: Other Alleged Effects: The prevalence of suburban sprawl, almost universally criticized as an aesthetic blight and as a spur to the spiraling costs for providing municipal services, has often been attribūted to large lot and other exclusionary zoning devices.[81] Exclusionary zoning has also been blamed for exacerbating the cities' fiscal woes by contributing to the problem of growing urban concentrations of lower income residents requiring high municipal expenditures.[82]

[76] Sager, "Tight Little Islands," p. 790; Notes, "Exclusionary Zoning and Equal Protection," p. 1664; Brooks, *Exclusionary Zoning,* p 17; Harold Schulz, "Exclusivism in the Suburbs: Restrictive Zoning Must Go," *Christianity and Crisis,* Mar. 30, 1970, p. 56. See also Alfred Lee, "The Impact of Segregated Housing on Public Schools," *Schools and Society,* Apr. 23, 1969 and the *New York Times,* Sept. 9, 1971.

[77] "Battle to Open the Suburbs: New Attack on Zoning Laws," p. 39.

[78] *The New York Times,* Dec. 7, 1969.

[79] Notes, "Constitutional Law—Equal Protection Zoning—Snob Zoning: Must a Man's Home Be a Castle?" *Michigan Law Review,* Vol. 69, No. 2, December 1970, p. 340; Aloi and Goldberg, "Racial and Economic Exclusionary Zoning," pp. 3+; Schulz, "Exclusivism in the Suburbs," p. 56; Brooks, *Exclusionary Zoning,* p. 17; Linda and Paul Davidoff and Neil Gold, "The Suburbs Have to Open Their Gates," pp. 43, 44, 46; Hirshin, "Exclusionary Subdivision Control," p. 352; Linda and Paul Davidoff, "Opening the Suburbs: Toward Inclusionary Land Use Controls," *Syracuse Law Review,* Vol. 22, No. 2, 1971, p. 513; U.S. President's Committee on Urban Housing, Technical Studies, *Jobs and Housing* (New York, N.Y.: NCDH, 1970). For a discussion of the relationship between metropolitan housing segregation and the distribution and level of nonwhite employment see John Kain, "Housing Segregation, Negro Employment and Metropolitan Decentralization: An Alternative Perspective," *Quarterly Journal of Economics,* Vol. 82, May 1968, pp. 299–311.

[80] Notes, "Exclusionary Zoning and Equal Protection," pp. 1663–1664.

[81] U.S. National Commission on Urban Problems, *Problems of Zoning and Land Use Regulation,* p. 10.

[82] Lazerow, "Discriminatory Zoning: Legal Battleground of the Seventies," p. 165.

Exclusionary Zoning: Legal Arguments, Evolving Courts' Response, and Reactions to the Current Courts' Position

The clash between proponents and critics of exclusionary zoning has often resulted in litigation—in fact, its opponents have relied during the last decade almost exclusively on such legal action as a strategy for change.[83]

This section briefly examines the legal arguments pro and con; the evolving attitude of the courts toward exclusionary land use controls and the reactions to the current position of the courts.

Legal Arguments Supporting Exclusionary Zoning: In a landmark decision, *Village of Euclid* v. *Ambler Realty Co.,*[84] the U.S. Supreme Court declared municipal zoning to be a valid exercise of the State's police power when such zoning was necessary for the community's general welfare. Communities have argued that large lot and comparable zoning is necessary for their general welfare, i.e., for their fiscal integrity, for stabilizing property values, and for aesthetic and ecological reasons. Communities practicing exclusionary zoning thus have argued for a broad definition of the general welfare criterion established by *Euclid.* Such a broad interpretation has been accepted by many courts for years.

Legal Arguments Against Exclusionary Zoning: Critics of exclusionary zoning have countered this general welfare justification by stating that it violates certain constitutional guarantees.

Violation of Equal Protection: The Constitution's Fourteenth Amendment guarantees equal protection under the law. Within the past 20 years the Supreme Court has expanded the scope of protection,[85] especially in areas affecting voting,[86] the criminal process,[87] and education.[88] Today legislative action is subject to two levels of review vis-a-vis equal protection: a rationality test and a close scrutiny test.[89]

[83] Geoffrey Shields and L. Sanford Spector, "Opening Up the Suburbs: Notes on a Movement for Social Change," *Yale Review of Law and Social Actions,* Vol. 2, Summer 1972, p. 309.

[84] 272 U.S. 365 (1926).

[85] Sager, "Tight Little Islands," pp. 767–780.

[86] See *Reynolds* v. *Sims,* 377 U.S. 533 (1964); *Harper* v. *Virginia Board of Elections,* 383 U.S. 663 (1966).

[87] See *Douglass* v. *California,* 372 U.S. 353 (1963); *Griffin* v. *Illinois,* 351 U.S. 12 (1956); *Anders* v. *California,* 386 U.S. 738 (1967).

[88] See *Griffin* v. *County School Board,* 377 U.S. 218 (1964); *Brown* v. *Board of Education,* 374 U.S. 483 (1954).

[89] Freilich and Bass, "Exclusionary Zoning: Suggested Litigation Approaches," pp. 347–348; "Constitutional Law—Equal Protection Zoning—Snob Zoning," pp. 342–344.

The rationality standard, typically applied when economic regulations are under attack,[90] requires that the classification drawn by the legislation bear a reasonable relation to the permissible State objective. The close scrutiny standard, applied when legislative classifications are drawn along constitutionally suspect lines—e.g., race, or, when they jeopardize a particularly favored right, e.g., education—requires that there be a compelling need for the legislative classification.[91] Many critics of exclusionary zoning have alleged that such zoning, when subjected to the close scrutiny test, falls short on all of this test's criteria. Hence, they argue, such zoning allegedly violates the equal protection clause.[92]

Violation of Right to Travel: Although there is no explicit constitutional guarantee of the right to travel,[93] recent decisions[94] have considered such a right to be implicit in certain explicit constitutional guarantees and clauses, e.g., the commerce clause. It is alleged that exclusionary zoning, by restricting low and moderate income housing, violates the freedom to reside freely within a desired State—a right that is implicit in the constitutional guarantee of the right to travel.[95]

Violation of the Supremacy Clause: Recent Federal programs, e.g., Section 236 of the 1968 Housing Act, have been enacted to encourage the construction of low and moderate income housing. The construction of such housing, however, has been thwarted by communities enacting exclusionary zoning statutes. Observers have alleged, then, that to the extent that these Federal programs are impeded by exclusionary zoning, there has been an encroachment upon the Federal Government's power by localities; such encroachment is unlawful under the Constitution's supremacy clause.[96]

Violation of the Due Process Clause: Exclusionary zoning may depress the value of a property. A plot of land zoned for single family house, for example, may be worth less than if it were zoned for multifamily construction. Because of its depressive effect, such zoning has been attacked as unconstitutional, like taking property without due process.[97]

Violation of the "General Welfare" Requirement: Zoning, from both a statutory and constitutional perspective, is lawful only if it serves the "general welfare." Critics of exclusionary zoning have charged that it is unlawful in that it serves only the community's parochial interest at the expense of the general welfare. One recent article stated this argument as follows:[98]

> The "general welfare" is thus both a statutory and constitutional concept in zoning . . . . If the notion of promoting the general welfare is to have any meaning in the context of contemporary metropolitan development, the pro-

[90] "Constitutional Law—Equal Protection Zoning—Snob Zoning," pp. 342–343.

[91] Ibid., p. 344.

[92] The specifics of how exclusionary zoning violates the due process clause has been interpreted in numerous ways. And there have also been differences in opinion concerning the likelihood that the courts will overturn exclusionary zoning on the grounds that such land use controls do not afford equal protection. See Sager, "Tight Little Island"; "Exclusionary Zoning and Equal Protection," pp. 1649–1670; Freilich and Bass, "Exclusionary Zoning: Suggested Litigation Approaches," pp. 347–361; Williams and Norman, "Exclusionary Land Use Control," pp. 732+; Comments, "A Survey of the Judicial Response to Exclusionary Zoning," *Syracuse Law Review*, Vol. 22, No. 2, 1971, pp. 577; Brooks, *Exclusionary Zoning*, p. 14; "State Police Power—Zoning—Validity of Local Ordinances Depends on Consideration of Regional Not Merely Local General Welfare," *Vanderbilt Law Review*, Vol. 25, No. 2, March 1972, pp. 468–469; "The Constitutionality of Local Zoning," *Yale Law Journal*, Vol. 79, No. 5, April 1970, pp. 896–917; Norman Williams, Jr., Tatyana Doughty, R. William Potter, "The Strategy of Exclusionary Zoning: Towards What Rationale and What Remedy?" *Land Use Controls Annual*, 1972, pp. 77+; Richard Cutler, "Legality of Zoning to Exclude the Poor: A Preliminary Analysis of Evolving Law," *Brooklyn Law Review*, Vol. 37, No. 3, Spring 1971, pp. 496–499.

[93] See Aloi and Goldberg, "Racial and Economic Exclusionary Zoning," pp. 3+; and Freilich and Bass, "Exclusionary Zoning: Suggested Litigation Approaches," p. 361.

[94] *Schapiro* v. *Thompson*, 394 U.S. 618 (1969); *Edwards* v. *California*, 314 U.S. 160 (1941).

[95] See sources cited in footnote 93 and "Exclusionary Zoning and the Problem in Black Jack: A Denial of Housing to Whom," *St. Louis University Law Journal*, Vol. 16, 1971, p. 307. For a discussion of the possible serious consequences of exclusionary zoning being ruled unconstitutional as violating the right to travel see Williams, Doughty, and Potter, "The Strategy of Exclusionary Zoning" (mimeo), p. 30.

[96] Local exclusionary zoning's encroachment upon the Federal Government power has been described by the National Committee Against Discrimination in Housing as follows:
The power of suburban governments to block residency by low and moderate income families effectively reduces Federal guarantees of open housing to an empty right for the bulk of America's minority families. This suburban power, likewise, largely frustrates the Housing and Urban Development Act of 1968, since its goals of building an average of 2.6 million homes annually for the next ten years can be achieved only through massive construction on open land in outlying localities. Land-locked central cities, especially their overcrowded ghetto areas, can accommodate only a relatively small portion of this annual volume of urgently needed housing. In addition to space limitations, building progress in central cities is tortuously slow because of relocation problems, clearance of buildings, high-rise construction, and other conditions which impede rebuilding.
See National Committee on Discrimination in Housing, "NCDH Program Identification and Research to End Exclusionary Land-Use Controls and Other Regulatory Devices which Block Housing for Low and Moderate Income Families in the Suburbs," April 1969, p. 3. Cited in Brooks, *Exclusionary Zoning*, p. 15. See also Marcus, "Exclusionary Zoning: The Need for a Regional Planning Context," p. 736.

[97] Brooks, *Exclusionary Zoning*, p. 15; "State Police Power Zoning—Validity of Local Ordinance," p. 468; Marcus, "Exclusionary Zoning: The Need for a Regional Planning Context," p. 736.

[98] Williams, Doughty, and Potter, "The Strategy on Exclusionary Zoning," (mimeo), p. 30.

vision of substantial new housing (especially inexpensive housing) is clearly one of its most important aspects. In this context, it does not involve a major step—assuming appropriate plaintiffs are present who can raise the issue—to expand the notion of municipal responsibility to include a share of regional housing need. Under this theory then (exclusionary) restrictions may be held not to conform to the general welfare requirement as set forth in the enabling law or in general constitutional law.

Violation of the Civil Rights Act: It also has sometimes been alleged that because exclusionary zoning severely restricts the housing choices open to black Americans, it violates the 1968 Civil Rights Act as well as earlier Civil Rights Acts, e.g., the 1964 Act.[99] Suits against exclusionary zoning on the grounds of Civil Rights Act violations [100] have been brought, but various commentators have questioned the viability of such a strategy.[101]

Exclusionary Zoning: Evolution of the Court's Attitude

For many years, the legal arguments of communities practicing exclusionary zoning were upheld by the courts. Recently, however, the courts' attitude has been much more sympathetic to the critics of such zoning. The courts' position toward zoning in general, and exclusionary zoning in particular, has gone through four stages which can be labeled as pre-Euclid, Euclid, and two stages of post-Euclid decisions.

Pre-Euclid: In the early 1900's, a laissez-faire attitude toward land use prevailed.[102] Courts, adhering to the belief that the private property owner's rights had to be protected, often declared zoning ordinances unconstitutional.[103] When courts did allow zoning statutes to stand, they did so only when such ordinances were clearly necessary to protect the public's health, safety, morals, or material welfare.

During the 1920's, as previously noted, the number of cities enacting zoning ordinances mushroomed. During this period, many State courts, reversing their previous stand, declared these zoning statutes constitutional.[104] They frequently held that zoning was justified by the State's police power—a power that they felt could and should be construed as a positive and affirmative force to promote the general welfare, and not merely as a suppressor of offensive or harmful property uses.[105] But despite the growing acceptance of zoning by State courts, a legal cloud hovered over local zoning ordinances until 1926,[106] when the United States Supreme Court declared zoning constitutional.

Euclid: The Decision and Its Impact: The *Euclid* v. *Ambler* case involved a challenge of Euclid's (Ohio) zoning ordinance, which restricted the use of land, and established minimum lot sizes and maximum building heights in designated zones. The district court ruled that Euclid's zoning statute was unconstitutional because it had the effect of taking property without due process. In language remarkably similar to current decisions condemning exclusionary zoning, the court held that "the true object" of the (zoning) ordinance in question was to place all property in a strait jacket and that it would segregate Euclid's population according to their income or situation in life.[107] The Supreme Court, however, overruled this decision; it declared Euclid's zoning ordinance constitutional, stating that it was justifiable under the State's police power as a necessary measure for the public's general welfare.

However, the *Euclid* decision did not give local zoning advocates carte blanche; it specifically stated that:

> [I]t is not meant by this (decision), however, to exclude the possibility of cases where the general public interest would so far outweigh the interest of the municipality that the municipality would not be allowed to stand in the way.[108]

[99] See U.S. President's Committee on Urban Housing, Technical Studies, p. 390; Aloi and Goldberg, "Racial and Economic Exclusionary Zoning," pp. 3+; Chester Johnson, "Exclusionary Zoning: Damage Actions Under the Civil Rights Act," *Law and the Social Order—Arizona State University Law Journal*, No. 3, 1971, pp. 578–587; "Exclusionary Zoning and the Problem in Black Jack," p. 312.

[100] Some zoning suits brought under the Civil Rights Act have included *Urban Developers* v. *City of Tempe*, Cor. No. 70–373 (D. Ariz. filed June 29, 1970); *Dailey* v. *City of Lawton*, 296 F. Supp 266 (W. D. Ok'l. 1969), off'd., 425 F. 2d 1037 (10th Cir. 1970) and other suits. See Johnson, "Exclusionary Zoning: Damages Under the Civil Rights Act," pp. 538–543.

[101] See supra footnote 99.

[102] "Suburban Apartment Zoning: Legality and Technique," *Boston College Industrial and Commercial Law Review*, Vol. 12, 1971, p. 956.

[103] *Calvo* v. *City of New Orleans*, 136 La. 480, 67 So. 338 (1915); *People ex rel Frient* v. *City of Chicago*, 261 Ill. 16, 103 N.E. 609 (1913).

[104] *Miller* v. *Board of Pub. Works*, 195 Cal. 477, 485, 234, p. 381, 384 (1925); In re: *Wolfsohn* v. *Burden*, 214 N.Y. 288, 150 N.E. 120 120 (1925).

[105] "Suburban Apartment Zoning." pp. 957–958.

[106] The Supreme Court in *Buchanan* v. *Warley*, 245 U.S. 60 (1917) declared racially tinged zoning to be unconstitutional, but it could only indirectly be inferred from this decision that zoning that was not racially motivated was constitutional.

[107] *Ambler Realty Co.* v. *Village of Euclid*, 297 F. 307 (N.D. Ohio 1924).

[108] 272 U.S. 365 (1926) at 390. See Comment, "The Equal Protection Clause: A Single-Edged Sword for the Gordian Knot of Exclusionary Zoning," *University of Missouri—Kansas City Law Review*, Vol. 40, No. 1, Autumn 1971, p. 20; "The Battle for Apartments in Benign Suburbia: A Case of Judicial Lethargy," p. 301; Michael Holmes, "Removing the Bar of Exclusionary Zoning to a Decent Home," *Ohio State Law Journal*, Vol. 32, 1971, pp. 383–384; Lyon, "Exclusionary Zoning from a Regional Prospective," p. 240.

But Euclid's guarded affirmation of zoning was almost totally ignored; instead, the decision was viewed as removing any legal question regarding local zoning's constitutionality. Specifically, *Euclid* and a similar 1928 Supreme Court decision, *Nectow* v. *City of Cambridge,*[109] were interpreted as a virtually absolute upholding of zoning ordinances as a valid exercise of the State's police power. Both decisions were also interpreted as giving zoning statutes a presumption of validity [110] so that such ordinances could be challenged only if they were shown to be clearly arbitrary and unreasonable.

Post-Euclid I: Strong Affirmation of Zoning: Following *Euclid,* many municipalities enacted exclusionary zoning statutes. Although many of these ordinances were challenged by owners and developers of the restrictively zoned land, the controls were almost universally upheld by the courts.[111]

Minimum Lot Area Regulations Upheld: In *Simon* v. *Town of Needham,*[112] the Massachusetts Supreme Court, in upholding a zoning statute establishing a 1-acre minimum lot size, reasoned that a large lot size requirement was needed for the public's health and safety and thus was a reasonable exercise of the State police power. The court described the advantages of large minimum lots in glowing terms, stating that: [113]

> . . . The advantages enjoyed by those living in one-family dwellings located upon an acre lot might be thought to exceed those possessed by persons living upon a lot of ten thousand square feet. More freedom from noise and traffic might result. The danger from fire from outside sources might be reduced. A better opportunity for rest and relaxation might be afforded. Greater facilities for children to play on the premises and not in the street would be available.

The *Needham* decision was not unique; scores of other courts similarly upheld large minimum lot sizes.[114] The court in *Bilbar Construction Company* v. *Board of Adjustment* [115] upheld a one-half acre minimum lot size. A Connecticut decision, *Senior* v. *Zoning Commission of the Town of New Canaan,*[116] upheld a zoning statute that established a 2-acre minimum lot size. Many courts have even upheld extremely large minimum lot sizes; both an Illinois [117] and a New Jersey [118] court, for example, have upheld the legality of zoning ordinances requiring a 5-acre minimum lot size.

Minimum Floor Area Regulations Upheld: For years many courts declared that minimum floor area ordinances were an unreasonable [119] exercise of the police power. But their position began to change in the post-World War II period, when they almost uniformly started accepting such local requirements.

The New Jersey Supreme Court landmark decision, *Lionshead Lake, Inc.* v. *Wayne Township,*[120] for example, declared that Wayne Township's minimum floor area requirements (ranging from over 700 to 1,200 square feet) were constitutional. The court reasoned that these requirements were needed to protect the public's general welfare.[121]

The *Lionshead Lake* case was not unique.[122] As suburban development acceler-

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[109] 277 U.S. 183 (1928).

[110] "Exclusionary Zoning and Equal Protection," p. 1674–1648; Holman, "Removing the Bar of Exclusionary Zoning to a Decent Home," p. 381; "Segregation and the Suburbs," pp. 1304–1305; Gerald Fisher, "The General Public Interest vs. The Presumption of Zoning Ordinance Validity: A Debatable Question," *Journal of Urban Law,* Vol. 50, No. 1, August 1972, p. 132; "State Police Power—Zoning—Validity of Local Ordinance Depends on Consideration of Regional, Not Merely Local, General Welfare," *Vanderbilt Law Review,* Vol. 25, 1972, pp. 466+; "State Police Power—Zoning—Validity of Local Ordinance Depends on Consideration of Regional Not Merely Local General Welfare," p. 467; Mayse, "The Responsibility of Local Zoning Authorities to Nonresident Indigents," p. 779.

[111] It is difficult to pinpoint why courts for so many years upheld exclusionary zoning controls. Many commentators, though, have attributed this wide acceptance to the fact that zoning was and is considered one of the most powerful local powers and hence courts were extremely hesitant to restrict a power considered essential for local home rule. See Brooks, *Exclusionary Zoning,* p. 6; Cutler, "Legality of Zoning to Exclude the Poor," p. 487.

[112] 311 Mass. 560, 42 N.E. 2d 516 (1942).

[113] 311 Mass. at 565–566, N.E. 2nd at 519.

[114] *Appeal of Blackstone,* 38 Del. 230, 190 A. 597 (1937); *R. B. Construction Co.* v. *Jackson,* 152 Md. 671, 137 A. 278 (1927); *Demars* v. *Zoning Commission,* 142 Conn. 580, 115 A. 2nd 653 (1955); *Dillard* v. *Village of No. Hills,* 276 App. Div. 969, 94 N.Y.S. 2nd 715 (1950). See also Comments, "A Survey of the Judicial Responses to Exclusionary Zoning," *Syracuse Law Review,* Vol. 22, No. 2, 1971, pp. 538–548; "Zoning Law in Michigan and New Jersey: A Comparative Study," *Michigan Law Review,* Vol. 63, No. 7, May 1965, pp. 1191–1192; William Bowe, "Regional Planning versus Decentralized Land Use Controls: Planning for the Megalopolis," *DePaul Law Review,* Vol. 18, 1968–1969, pp. 150–154.

[115] 393 Pa. 62, 141 A. 2d 851 (1950).

[116] 146 Conn. 531, 153 A. 2d 415 (1959), *cert. denied,* 363 U.S. 143 (1968).

[117] *Honeck* v. *County of Cook,* 12 Ill. 2d 257, 146 N.W. 2d 35 (1957).

[118] *Fisher* v. *Bedminster Township,* 11 N.J. 194, 93 A. 2d 378 (1952).

[119] *Frischkorn Const. Co.* v. *Lambert,* 315 Mich. 556, 24 N.W. 2d 209 (1946); *Senefsky* v. *City of Huntington Woods,* 307 Mich. 738, 12 N.W. 2d 387 (1943); *Brookdale Homes Inc.* v. *Johnson,* 123 N.J.L. 602, 10 A. 2d 473 (1940), *affd* 126 N.J.L. 516, 19 A. 2d 868 (1941). See Lazerow, "Discriminatory Zoning: Legal Battleground of the Seventies," pp. 162–163.

[120] 10 N.J. 165, 89 A. 2d 693 (1952).

[121] For discussions of the decision see Charles Haar, "Zoning for Minimum Standards: The Wayne Township Case," *Harvard Law Review,* Vol. 67, 1954, pp. 986+; Charles Haar, "Wayne Township: Zoning for Whom? In Brief Reply," *Harvard Law Review,* Vol. 67, 1954, pp. 986+; Williams and Wacks, "Segregation of Residential Areas Along Economic Lines," pp. 827-847.

[122] *DeMars* v. *Zoning Comm'n.,* 142, Comm. 580, 115 A. 2d 653 (1955); *Konvitz* v. *Board of County Commr's.,* 180 Kan. 230, 303 P. 2d 180 (1956). Also see cases cited in footnotes 123 to 125 supra and Comments, "A Survey of the Judicial Responses to Exclusionary Zoning," pp. 551–553.

ated in the post-World War II period,[123] many other courts upheld the constitutionality of minimum floor area ordinances. The Nebraska Supreme Court in *Dundee Realty Co.* v. *Omaha,*[124] for example, declared that a 1,200-square foot minimum floor area was constitutional because it was needed for the public's safety, for maintaining local property values, and because of esthetic consideration. Similarly, a Texas decision, *Thompson* v. *Carrollton,*[125] upheld an ordinance requiring a 900-square foot minimum floor area, and a New York decision, *Flower Hill Building Corp.* v. *Village of Flower Hill,*[126] declared that an 1,800-square foot minimum floor area requirement was constitutional.

Exclusion or Restriction of Multiple Dwellings Upheld: A judicial hostility to multiple-family housing can be traced to the *Euclid* decision, wherein Justice Sutherland, writing for the majority, stated that multiple dwellings were often a "mere parasite" [127] and that with the construction of such housing "the residential character of the neighborhood and its desirability as a place of detached residence are utterly destroyed." [128] Scores of decisions [129] have since upheld local communities' exclusion and restriction of multiple-family housing, contending that such housing was "productive of disease, dirt, noise, fire and congestion." [130]

Other Exclusionary Devices Upheld: In the years following the *Euclid* decision, many courts have upheld the constitutionality of exclusionary zoning controls other than those discussed above. The New Jersey Supreme Court in *Vikers* v. *Township of Gloucester,* for example, upheld a local ordinance prohibiting trailer camps.[131] And courts have frequently allowed local communities to adopt secondary exclusionary devices,[132] e.g., setback requirements,[133] height regulations,[134] and architectural controls. The court in *State ex. rel Saveland Park Holding Company* v. *Willand,*[135] for example, uphe'd the legality of an ordinance providing that new structures could not be at variance with the exterior architectural appearance of existing houses.

Post-Euclid II: Exclusionary Zoning Challenged As Judicial Approach Modifies: During the 1960's, many courts began to modify their strong defense of exclusionary zoning. Numerous courts placed restrictions on when and where exclusionary controls could be applied; some even declared that certain controls could not be applied at all. The changing judicial attitude, however, did not constitute a new line of legal thinking, because even among the strong pro-exclusionary rulings cited above, there were often articulate and vigorous dissents.

Judge Hall in the *Vickers* v. *Gloucester Township* decision, for example, dissented from the majority, stating:

> In my opinion, legitimate use of the zoning power by such municipalities does not encompass the right to erect barricades on their boundaries through exclusion or too tight restriction of uses where the real purpose is to prevent feared disruption with a so-called chosen way of life. Nor does it encompass provisions designed to let in as new residents only certain kinds of people, or those who can afford to live in favored kinds of housing, or to keep down tax bills of present property owners. When one of the above is a true situation, deeper considerations intrinsic in a free society gain the ascendancy and courts must not be hesitant to strike down purely selfish and undemocratic zoning enactments.[136]

Similarly, the minority opinion in the *Lionshead Lake* decision declared that a zoning amendment that can produce this effect (precluding individuals in the $8,600 to $12,000 income bracket

[123] Even in the post World War II period courts did not unanimously uphold minimum floor area zoning. See *Elizabeth Lake Estates* v. *Township of Waterford,* 317 Mich. 359, 26 N.W. 2d 788 (1947); *Senefsky* v. *Lawler,* 307 Mich. 728, 12 N.W. 387 (1943).

[124] 144 Neb. 448, 13 N.W. 2d 634 (1944).

[125] 211 S.W. 2d 970 (Tex. Cir. App. 1948).

[126] 199 Misc. 344, 100 N.Y.S. 2d 903 (Sup. Ct., Sp. Term. Nassau Co. 1950).

[127] 272 U.S. 365 (1926) at 394. Cited in "The Battle for Apartments in Benign Suburbia," p. 346.

[128] Ibid.

[129] *Miller* v. *Board of Public Works,* 195 Cal. 477, 234 P. 381 (1925); *Minkus* v. *Pond,* 236 Ill. 467, 158 N.E. 121 (1927); *Wolfsohn* v. *Burden,* 241 N.Y. 288, 150 N.E. 120 (1925); *Sullivan* v. *Anglo-American Investment Trust Inc.,* 89 N.H. 112, 116, 193 Atl. 225, 227 (1937); *City of Bismark* v. *Hughes,* 53 N.D. 838, 208 N.W. 711 (1926).

[130] See Comments, "A Survey of Judicial Responses to Exclusionary Zoning," p. 555; Babcock and Bosselman, "Suburban Zoning and the Apartment Boom," pp. 1073–1074; for dissenting opinions against the restriction on exclusion of multi-family housing. See *City of Youngstown* v. *Kahn Brothers Bldg. Co.,* 112 Ohio St. 654, 662–663 148 N.E. 842, 844–845 (1925); *Bjork* v. *Safford,* 333 Ill. 255, 164 N.E. 699 (1928); cited in Comments, "A Survey of the Judicial Responses to Exclusionary Zoning," p. 556.

[131] 37 N.J. 232, 181 A. 2d 129 (1962); *cert. denied,* 371, U.S. 233 (1963).

[132] See Comments, "A Survey of the Judicial Responses to Exclusionary Zoning," pp. 557–562.

[133] See *Goreib* v. *Fox,* 274 U.S. 603 (1927); *Preotz* v. *Messer,* 112 Ohio St. 628, 149 N.E. 30 (1925); *Thille* v. *Board of Pub. Works,* 82 Cal. App. 187, 255 P. 294 (1927); *Richard* v. *Zoning Bd. of Appea!s,* 285 App. Div. 287, 137 N.Y.S. 2d 603 (2d Dep't. 1955). See supra footnote 131, pp. 558–560.

[134] *Welch* v. *Swassey,* 193 Mass. 364, 79 N.E. 745 (1907) *aff'd,* 214 U.S. 91 (1909); *Toliaferro* v. *Solzer,* 162 Cal. App. 2d 685, 328 P. 2d 799 (1958); *Michigan Lake Building Corp.* v. *Hamilton,* 340 Ill. 284, 172 N.E. 70 (1930); *Bay Harbor Islands* v. *Burk,* 114 So. 2d 225 (Fla. 1959). See supra footnote 131, pp. 560–561.

[135] 269 Wis. 262, 69 N.W. 2d 219, *cert. denied,* 350 U.S. 841 (1955).

[136] See supra footnote 131.

from affording a house) certainly runs afoul of the fundamental principles of our form of government.[137]

Pre-1970 Decisions Challenging Exclusionary Zoning: A 1959 decision, *Board of County Supervisors of Fairfax County* v. *Carper,*[138] was one of the earliest modern decisions to overturn an exclusionary zoning strategy. Fairfax County, (Va.), had for fiscal reasons enacted an ordinance requiring a minimum of 2-acre lots in its western section. Subsequent litigation contended that the 2-acre zoning would in effect exclude low income people from living in the rezoned area and hence was unconstitutional. The court in *Fairfax County* v. *Carper* agreed, ruling that the county rezoning served only private rather than justifiable public interests and therefore was unconstitutional.[139]

Six years later, the Pennsylvania Supreme Court [140] declared as unconstitutional a zoning ordinance establishing a 1-acre minimum lot size,[141] declaring that:

> The question posed is whether the township can stand in the way of the natural forces which send our growing population into undeveloped areas in search of a comfortable place to live. We have concluded not. A zoning ordinance whose primary purpose is to prevent the entrance of newcomers in order to avoid future burdens, economic and otherwise, upon the administration of public services and facilities cannot be held valid.

A 1969 Illinois decision, *Lakeland Bluffs Inc.* v. *County of Will,*[142] struck at the core of the rationale used by municipalities to defend exclusionary zoning. The court in *Lakeland* declared that where certain land uses—e.g., zoning—are concerned, the term "general welfare" cannot be interpreted solely as the local municipality's general welfare but must be defined more broadly to meet the exigencies of urbanized society.

Post-1970 Decisions Challenging Exclusionary Zoning: Since 1970, there has been a veritable deluge of court decisions overturning exclusionary zoning. State courts, especially in Pennsylvania and New Jersey, have repeatedly questioned the constitutionality of exclusionary land use controls. The Pennsylvania Supreme Court, striking down minimum lot size in a 1970 decision, *Appeal of Kit-Mar Builders,*[143] reaffirmed its 1965 contention that municipalities had an obligation to deal with the problem of population growth. In another decision in the same year,[144] the Pennsylvania Supreme Court ruled that municipalities did not have the right totally to exclude multifamily housing. The court argued that: [145]

> Apartment living is a fact of life that communities like Nether Providence must learn to accept. If Nether Providence is located so that it is a place where apartment living is in demand, it must provide for apartments in its plan for future growth; it cannot be allowed to close its doors to others seeking a "comfortable place to live."

A number of New Jersey decisions have also strongly challenged exclusionary zoning. The New Jersey Supreme Court in 1970, for example, upheld a zoning variance in Englewood [146] that was effected to allow the construction of multifamily housing for low and moderate income housing. The court argued that the need for such housing justified the granting of the zoning variance under New Jersey law.

In 1971, a New Jersey lower court in *Oakwood at Madison* v. *Tp. of Madison* [147] overturned a local exclusionary zoning plan. Madison, in an effort to curb population growth and reduce its expenditures, had rezoned its land area to exclude multifamily housing almost completely; it also had stipulated minimum lot sizes of 1 and 2 acres. The *Madison* decision declared that this zoning change was invalid. The court argued that: [148]

> [I]n pursuing the valid zoning purpose of a balanced community a municipality must not ignore housing needs, that is its fair proportion of the obligation to meet the housing needs of its own population and of the region . . . . Large areas of vacant and developable land should not be zoned as Madison Township has into such minimum lot sizes and with such other restrictions that regional as well as local housing needs are shunted aside.

In the same year, the New Jersey Superior Court [149] ruled as unconstitutional a local Glassboro ordinance restricting the number of two or more bedroom apartments that could be built and requiring that certain expensive amenities be included in apartment house developments. The court found that the ordinance would severely restrict the ability of low and moderate income families and families with children to ob-

[137] 89 A. 2d at 701.
[138] 200 Va. 653, 107 S.E. 2d 390 (1959).
[139] See 107 S.E. 2d at 390 and 396.
[140] *National Land and Investment Co.* v. *Kohn,* 419 Pa. 504 (1965).
[141] Ibid., 215 A. 2d at 597, 215 A. 2d at 610–616.
[142] 114 Ill. App. 2d 267, 252 N.E. 2d 765 (1969).
[143] 439 Pa. 466, 268 A. 2d 765 (1970).
[144] In Re: Appeal of Joseph Girsh, 437 Pa. 237, 263 A. 2d 395 (1970).
[145] 263 A. 2d at 398.
[146] *DiSimone* v. *Greater Englewood Housing Corp.*, 56 N.J. 428, 267 A. 2d 31 (1970).
[147] 117 N.J. Super. 11 (Superior Ct. 1971).
[148] Ibid.
[149] *Molino* v. *Mayor and Council of Bor. of Glassboro,* 116 N.J. Super. 195 (Superior Ct. 1971).

tain housing in Glassboro. And in a 1972 decision,[150] a lower New Jersey State court declared that Mount Laurel's zoning ordinance was unconstitutional because it "exhibited economic discrimination in that the poor have been deprived of adequate housing and used governmental finances and resources solely to aid middle and upper income persons." The court then gave Mount Laurel 90 days to submit a program that would provide housing for the low and moderate income families either living or working in the municipality.

While Pennsylvania and New Jersey State courts have been at the forefront in challenging exclusionary zoning, other State courts have also joined the battle. The Michigan Court of Appeals in two recent decisions, *Bristow* v. *City of Woodhaven*,[151] and *Green* v. *Township of Lima*,[152] overturned local ordinances prohibiting mobile home parks. And State courts in Oklahoma,[153] New York,[154] California,[155] and elsewhere have similarly begun to question the constitutionality of exclusionary zoning.

Reaction to the Court's Changed Position Toward Exclusionary Zoning

Exclusionary zoning's critics have understandably welcomed and praised the courts' growing critical view towards restrictive land use controls.[156] But even among those who for years have condemned exclusionary zoning there has been frequent criticism of the courts' changed stance; courts have been accused of becoming "super planning agencies" without the competence and experience needed for such a role. Because of the importance zoning has had and will continue to have on national land use, we shall describe some of these criticisms, which can be grouped into two categories: Broad criticisms of the ability and desirability of courts acting as planners, and specific criticisms directed against specific court decisions.

Antiexclusionary Zoning Decisions: Broad Criticisms: Courts overturning exclusionary zoning ordinances and requiring zoning changes to allow the construction of specified numbers of low and moderate income housing have been accused of becoming de facto regional planners without the necessary competence. One recent law review article,[157] for example, stated:

> I think everyone is somewhat nervous over the prospect of courts deciding future planning for an area without any standards and criteria (other than equal protection). Such standards are properly the role of elected governments to provide. One judge's planning ideas on the appropriateness of the inevitability of highrise housing should not determine the future of a region as, for example, Judge Roberts' determination in the Girsh case when he implied that every community should contain areas zoned for high density housing.

The viewpoint in the passage cited above is not unique; similar sentiments have been expressed by other legal commentators[158] and even by the courts themselves. One article,[159] for example, described that "equally distressing to planners . . . is the tendency of many courts to assume an activist role in an area quite apart from the articulation of basic legal principles. In short, courts have become 'super-zoning commissions' without the necessary expertise to fulfill this function." And even the court in the landmark antiexclusionary decision, *National Land and Investment Co.* v. *Board of Adjustment*, stated that "this court has become increasingly aware that it is neither a super board of adjustment nor a planning commission of last resort. . . . The zoning power is one of the tools of government which in order to be effective must not be subjected to judicial interference unless clearly necessary."

Antiexclusionary Zoning Decisions: Specific Criticisms: Fear that the courts may act as planners without sufficient competence has not been a mere academic worry; already, specific criticisms have been made of certain decisions that have overturned exclusionary zoning ordinances. In the recent *Madison* decision, for example, Norman Williams, who has long criticized exclusionary zoning, commented that the court completely ignored the strong ecological drawbacks of building on the site that was involved in the litigation.[160]

Norman Williams and others[161] have also criticized courts, especially the Pennsylvania

[150] *Southern Burlington County NAACP* v. *Township of Mount Laurel*, 119 N.J. Super. 164 (Superior Ct. 1972).
[151] 35 Mich. App. 205, 192 N.W. 2d 322 (1971).
[152] 40 Mich. App. 655 (1972).
[153] *Dailey* v. *City of Lawton, Okla.*, 425 F. 2d 1037 (10th Cir. 1970).
[154] *Kennedy Park Homes Ass'n Inc.* v. *City of Lackawanna, N.Y.*, 318 F. Supp. 669 (W.D.N.Y.) *aff'd.*, 436 F. 2d 108 (2nd Cir. 1970), *cert. denied*, 401 U.S. 1010 (1971).
[155] *Southern Alameda Spanish-Speaking Organization (SASSO)* v. *City of Union City, Calif.*, 424 F. 2d 291 (9th Cir. 1970).
[156] See Lazerow, "Discriminatory Zoning," pp. 182–183; Davidoff and Gold, "The Suburbs Have to Open Their Gates," p. 58.
[157] Marcus, "Exclusionary Zoning: The Need for a Regional Planning Context," p. 736.
[158] "The Battle for Apartments in Benign Suburbia," p. 355.
[159] 419 Pa. 504, 521, 215 A. 2d 597, 607 (1965).
[160] Norman Williams, Jr., Memo on the Madison Decision.
[161] Williams and Norman, "Exclusionary Land Use Controls," p. 498; Williams, Doughty, and Potter, "The Structure of Exclusionary Zoning," (mimeo), pp. 32–38. See also "Constitutional Law—Equal Protection Zoning—Snob Zoning," p. 353.

courts, for establishing unduly mechanical housing formulae, e.g., that at least one area must allow multiple-family housing, or that no lot sizes shall be over a specified minimum area. Williams has critically noted that the Pennsylvania courts' approach provides no public control at all over the quantity of new housing, provides little or no local control on the location of new housing, and could prove to be potentially devastating to the local environment. In fact he has differentiated between two approaches to modify existing exclusionary zoning: a "sensible" rationale or strategy that would allow municipalities flexibility in providing low and moderate income housing; and the Pennsylvania rationale, the mechanical approach taken by the Pennsylvania courts.

Implemented and Suggested Strategies to Reform Zoning Exclusionary Zoning

Fair-Share Housing Formulas: A Regional Approach to Zoning Reform and Housing Allocation

Need for a Regional Approach to Housing: Underlying Norman Williams' and similar criticisms is the feeling that the reform of land use controls cannot be effected myopically, by focusing on one single community. Instead, a regional perspective is needed. The need for a regional orientation to zoning (as well as housing) has been reiterated by urbanologists and economists, as well as legal scholars.

Norman Marcus, for example,[162] concluded that unless the remaining vacant land in the State is allocated according to a set of sound regional priorities, it may be impossible to undo the mistakes which have been made in central cities. One recent law review article[163] criticized the *Girsh* and *National Land* decisions for not considering whether other areas in the region provided sites for construction while another law review article[164] asserted that the overall solution (to exclusionary zoning) is greater regional planning. And the Douglass Commission has stressed the importance of formulating and evaluating zoning statutes and housing policies according to regional considerations,[165] as have numerous participants in the National Conference on Housing.[166]

Although a regional approach to planning[167] and housing has long been advocated, it is only in recent years that such an approach has begun to attract serious interest. At this writing, at least 16 governmental and quasi-public bodies have either implemented or proposed regional housing allocation strategies, and their number is constantly growing.

But what exactly is fair share? Why has it generated so much recent attention? What are its criteria for housing distribution? What effect have these regional housing strategies had in the past? And what can be expected of them in the future? We shall attempt to answer all of these questions here.

Fair-Share Plans: Objectives and Background

Fair-share housing plans typically determine where housing—especially low and moderate income units—should be built within a region, according to such criteria as broadening the economic mix in communities and the placement of housing in environmentally suitable locations.

The following governmental and institutional bodies have either implemented or proposed fair-share plans:[168] Dade County Metropolitan Planning Board;[169] Delaware River Valley Regional Planning Commission;[170] Fairfax County, Va.;[171] The Greater Hartford Process, Inc.;[172] the State of Massachusetts;[173] Metropolitan

[162] Marcus, "Exclusionary Zoning: The Need for a Regional Planning Context," p. 740.

[163] "Constitutional Law—Due Process—Zoning—Suburban Township Ordinance Which Does Not Provide for Apartments as Permissible Residential Land Use Violates Due Process," *Alabama Law Review*, Vol. 23, No. 1, Fall 1970, p. 166.

[164] Thomas O'Keefe, "Time Controls on Land Use: Prophylactic Law for Planners," *Cornell Law Review*, Vol. 57, No. 5, May 1972, p. 834.

[165] National Commission on Urban Problems, *Building the American City*, pp. 222–224.

[166] See addresses by Eugene Moody, "Regional Housing Issues," and Richard Dosen, "Regional Leadership and Housing," in National Conference on Housing; Regional Issues and Strategies, *Summary of Proceedings*, August 8–10, 1971, St. Louis, Mo.

[167] See Friedmann, "The Concept of a Planning Region—The Evolution of an Idea in the United States," in Friedmann & Alonso, *Regional Development and Planning*, p. 497 (1964).

[168] For an excellent overview of the existing and implemented fair-share plans, see Mary Brooks, "Lower-Income Housing: The Planners' Response," *ASPO Report* (No. 282 July-August 1972); "Fair-Share Idea Begins to Spread," *16 NCDH Trends in Housing* (No. 2 July-August 1972). Much of the first part of this article was derived from Brooks' analysis.

[169] Metropolitan Dade County Planning Department, "Housing in the Metropolitan Plan: Dade County, Florida—Final Report" (undated).

[170] Delaware Valley Regional Planning Commission, "Equal Share Housing Allocation: Criteria, Assumptions and Methodology," Working Paper No. 4 (June 30, 1972).

[171] Amendment 156, Fairfax County Zoning Ordinance, effective Sept. 1, 1971.

[172] See, "Concerted Action in Hartford Region," *16 NCDH Trends in Housing*, at 1 (No. 4 December 1972).

[173] Mass. Gen. Stat. 40B §§20–23, inserted by State 1969, Ch. 774, §1.

Washington Council of Governments;[174] Metropolitan Dade County Planning Department;[175] Metropolitan Council of the Twin Cities Area;[176] Miami Valley Regional Planning Commission;[177] Middlesex County (N.J.) Planning Board;[178] the State of New Jersey;[179] New York State Urban Development Corporation;[180] Sacramento Regional Area Planning Commission;[181] and the San Bernardino County Planning Department.[182] Others developing fair-share mechanisms have included the University of Pennsylvania's Fels Center of Government[183] and the St. Louis Metropolitan Section of the American Institute of Planners.[184]

Although it is difficult to pinpoint the exact reasons for the recent proliferation of fair-share plans, we can isolate a number of precipitating factors, chief among which is the growing recognition of the need for regionalism in land use and housing decisions. Many urbanologists, attorneys, and governmental officials have been pressing for a regional approach as opposed to a local perspective. The National Commission on Urban Problems, for example, has stressed the importance of formulating and evaluating zoning statutes and housing policies according to regional considerations.[185] Similarly, Norman Marcus, in a recent law review article, concluded that unless the State's remaining vacant land is allocated according to a set of sound regional priorities, it may be impossible to undo the mistakes that already have been made in central cities.[186] This sentiment has been echoed by Governor William Cahill of New Jersey[187] and by participants in the National Conference on Housing.[188]

Contributing significantly to the mounting support for regionalism is an increased awareness that piecemeal, local actions in housing and zoning can have an adverse impact upon the environment. Another important reason is the growing recognition that local housing and zoning decisions are dichotomizing our society into white suburban enclaves and minority group cities with adverse racial, social, and economic effects.[189] Many of the fair-share plans are based on concern for increasing the housing availability and choice of those who currently are ill-housed. The Dade County regional allocation strategy, for example, lists among its objectives the substantial improvement of the quality of newly built and rehabilitated low and moderate income housing units, and the provision of open occupancy, low and moderate income housing in suitable, new locations.[190]

Fair-Share: Variations

There are many differences among the fair-share plans. One variation is generated by the type of body selected to formulate or implement the specific strategy. Our enumeration of fair-share plans shows variously that States, e.g., Massachusetts, New Jersey; counties, e.g., Dade County, Fla., Middlesex County, N.J.; Councils of Governments (COG's), e.g., Metropolitan Washington, COG; and regional planning agencies, e.g., Delaware River Valley Regional Planning Commission, have adopted or are considering strategies for regional housing allocation.

Another variation arises from the geographical areas encompassed by the fair-share plans. These can range from groups of adjacent States, e.g., in those plans considered by regional plan-

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174 Metropolitan Washington Council of Governments, "A Fair-Share Housing Formula for Metropolitan Washington," (January 1972).

175 Metropolitan Dade County Planning Department, "Housing in the Metropolitan Plan" (undated).

176 Metropolitan Council of the Twin Cities Area, "Metropolitan Development Guide, Housing Policy Program" (1972).

177 Miami Valley Regional Planning Commission, "A Housing Plan for the Miami Valley Region" (July 1970).

178 John Kim (Principal Planner Middlesex County Planning Board), "Outline for Study on Low and Moderate Income Housing in Middlesex County, New Jersey Analysis Forecast and Allocation of 1975" (undated).

179 Assem. Bill No. 1421 (introduced Nov. 13, 1972).

180 New York State Urban Development Corporation Programming Unit, "Five-Year UDC Development Programs Guide for the Central New York Region" (December 1971).

181 Sacramento Regional Area Planning Commission, "An Approach to the Distribution of Low- and Moderate-Income Housing" (August 1972).

182 San Bernardino County Planning Department, "Government Subsidized Housing Distribution Model" (Jan. 20, 1972).

183 University of Pennsylvania, The Fels Center of Government, *Standards for Suburban Housing Mix, Bucks County, Pennsylvania* (1971).

184 American Institute of Planners, St. Louis Section, "St. Louis Housing: A Regional Problem" (1973).

185 National Commission on Urban Problems, *Building the American City*, pp. 222–24 (Government Printing Office, 1968).

186 Norman Marcus, "Exclusionary Zoning: The Need for a Regional Planning Content," *N.Y.L. Forum* No. 4, 740 (1970).

187 Cahill, "New Horizons in Housing," pp. 27, 33 (March 1972).

188 See addresses by Eugene Moody, "Regional Housing Issues," and Richard Dusen, "Regional Leadership and Housing," in National Conference on Housing, *Regional Issues and Strategies: Summary of Proceedings* at 6 and 17 (Aug. 8–10, 1971).

189 Sager, "Tight Little Islands; Exclusionary Zoning; Equal Protection and the Indigent," 21 *Stanford L. Rev.* 767, (1969); William & Wacks, "Segregation of Residential Areas Along Economic Lines; Lionshed Lake Revisited," *Wis. L. Rev.* 27 (1969); James Coke and John Gargan, *Fragmentation in Land Use Planning and Control*, National Commission on Urban Problems Research Rep. No. 18 (Washington, D.C., 1969); Norman Williams and Thomas Norman, "Exclusionary Land Use Control: The Case of North Eastern New Jersey," 22 *Syracuse L. Rev.* 476 (1970–71); Frank Aloi and Arthur Goldberg, "Racial and Economic Exclusionary Zoning: The Beginning of the End," 1971 *Urban L. Annual* 9 (1971).

190 See note 169 supra.

ning commissions, to much smaller areas, such as individual counties.

But, the most important differentiations in fair-share plans involve these questions: What type of housing is being allocated? What are the criteria for housing allocations? Who is responsible for building the fair-share housing? And, last, will compliance be enforced?

Variations in the Types of Allocatable Housing: [191] Some fair-share programs, e.g., the Miami Valley Regional Planning Commission plan, project the total number of low to moderate income units needed in the region. Others, e.g., the Washington COG plan, allocate only those units subsidized by the Federal, State, or local governments.

The advantage of projecting the total number of housing units needed (both subsidized and unsubsidized units) is that this projection provides a more accurate estimate of the region's need for low and moderate income housing than can be obtained by merely calculating the number of subsidized units to be built. But, on the other hand, it is probable that in suburban areas, low and moderate income families could afford only subsidized housing. Hence, in a fair-share housing formula, it may be more realistic to project only the subsidized housing units, as in the second example, and then to allocate these units to districts or municipalities within the region.

Variations in the Allocation Criteria: The most frequently mentioned criteria [192] for fair-share housing allocations are based on considerations of equal share, need, distribution, and suitability.

Equal Share: One way to achieve the objective of equal housing distribution might be to establish equitable minimum percentages of low and moderate income housing to be contained in each community. The rationale for this strategy is that all areas within a region have the same obligation to meet the region's housing needs.

Such an approach has been adopted by the Massachusetts fair-share plan, which establishes boards of review empowered to overrule local zoning bodies that refuse to allow the construction of low to moderate income housing. Local decisions can be overturned when the review board finds that a proposed housing project poses no environmental problem and in cases where the locality is not meeting its minimum percentage requirements. The minimum standard specifies that 10 percent of the community's housing be comprised of units subsidized for low and moderate income families, or that such housing should occupy 1.5 percent of the community's local land area minus public lands, whichever is less. These long term guidelines are supplemented by annual standards specifying that the review boards cannot permit the construction in any one year of a low to moderate income housing development that would occupy 10 acres or .3 percent of the town's land, whichever is larger. These annual guidelines were instituted to assure communities that they would not be inundated by housing they did not want.

Fairfax County also has opted for an equal-share approach. In 1971, it passed an amendment [193] stipulating that applicants for rezoning in its Planned Development Housing District must provide, or cause others to provide, that at least 6 percent of the total housing units initiated would be for low income families, and an additional 9 percent must be allotted to moderate income units. Developers of 50-unit or larger tracts in the county's residential Garden Court district must provide the same percentages of low and moderate income housing units.

One advantage of an equal-share requirement is that no one community can charge that it is being forced to do more than its sister communities. Another benefit is that it facilitates calculating the number of units to be assigned.

But, equal share has several serious drawbacks. In most instances, the minimum equal-share percentages are chosen arbitrarily, thereby negating the rational objectives of fair share. Such was the case in Massachusetts, where considerable criticism was provoked.[194] The legality of the equal-share approach has also been questioned—Fairfax County's plan was overturned by the Virginia Supreme Court [195] and the constitutionality of the Massachusetts plan was also challenged,[196] although this challenge was subsequently defeated.

Need: In contrast to an equal-share strategy, one could allocate housing to regions where there is the greatest need. These might be areas

[191] See Brooks, note 168 supra at 18.
[192] Id., at 20.

[193] See note 171 supra.
[194] See Nathaniel Taylor, "Reconsidering the Massachusetts Suburban Housing and Zoning Reform Law: The Need for Change," paper submitted at American Institute of Planners Conference, Boston, 1972 (mimeo).
[195] *The Board of Supervisors* v. *DeGroff Enterprises, Inc.*, 198 S.E.2d 600 (1973).
[196] *Board of Appeals* v. *Housing Appeals Comm., Board of Appeals of Concord* v. *Housing Appeals Comm.* (Both cases heard together) 294 N.E.2d 393 (1973).

with a large number of dilapidated or deteriorating units, neighborhoods with extensive, overcrowded housing and geographical sectors, and areas that offer attractive employment potential. Such an approach, especially if the primary aim is to improve the quality of the housing stock, usually results in more housing units being allocated to urban areas than to suburban locations and to more units in slum neighborhoods within these urban enclaves, as opposed to higher housing quality neighborhoods.

Distribution: An alternative strategy is to allocate low and moderate income units to areas lacking such units in order to achieve a greater income and, implicitly, a greater racial mixture in those communities. For example, most of the low to moderate income housing units could be allocated to those communities with the lowest number of families on welfare or the highest incomes or the least amount of subsidized housing. Such a fair-share strategy would allocate the most housing to wealthy white suburban areas and the least to urban areas with high percentages of nonwhites and low income families.

Suitability: Another guideline for allocating housing is the selection of areas containing the most suitable housing sites, e.g., those that are already serviced by sewer and utility lines, or that contain adequate vacant land for development. In addition to physical suitability, there is the matter of a subregion's financial capacity to service additional housing. When financial capacity is of prime concern, then most of the housing units are allocated to subregions with a high property tax base behind each student or resident, since these communities are better able to bear the additional municipal and school expenditures incurred by new housing construction.

Exhibit 1–5. Allocation Criteria of Six Fair-Share Plans

	Implemented				Proposed	
	Metropolitan Washington Council of Governments	Miami Valley Regional Planning Commission	San Bernardino County, Calif.	Metropolitan Council, Minneapolis-St. Paul	Sacramento Regional Area Planning Commission	New Jersey (Assembly Bill 1421, 1972) Voluntary Distribution
Need Allocation Criteria	(1) Number of households of less than $10,000 annual income with commuters into the area (the greater the number of households, the greater the share of new units) (2) Number of overcrowded housing units (the greater the number of units, the greater the share of new units) (3) Number of deficient housing units (the greater the number of units, the greater the share of new units)	(1) Share of households of less than $10,000 annual income ($7,000 in rural areas) (the greater the number of households, the greater the share of new units)	(1) Deficient housing units within income group level appropriate (the greater the number of units, the greater the share of new units) (2) Number of jobs (the greater the number of jobs, the greater the share of new units) (3) Number of households with annual gross income less than $10,000 (the greater the population in this category, the greater the share of new units)		(1) Total population in the area as a percent of the regional population (share is in proportion to the population) (2) Number of households in the 0–$5,000 category as a percentage of the total regional low income households (the greater the number of such households the greater the share of new units) (3) Number of households in the $5,000–$8,000 income bracket (see 2) (4) Number of jobs in the area as a percent of the total region's jobs (the greater the number of jobs, the greater the share of new units)	(1) Substandard housing in the municipality (2) The number of low and moderate income households as a percentage of households in the municipality

(Continued on p. 345.)

Exhibit 1–5. Allocation Criteria of Six Fair-Share Plans (Continued)

Distributive and Equal Share Allocation Criteria	(4) Percent of jobs within 45 minutes of area (used as a modifier) (5) Percent of units less than $25,000 or $250 rent (used as a modifier) (6) Potential per capita fiscal resources (used as a modifier)	(2) Equal share (3) Proportion to the population (4) Inverse of (1) (the greater the number of households, the smaller the share of new units)	(4) Equal share (5) Number of households (share is in proportion to the population)	(1) Percentage of existing low and moderate income housing (the higher priority is given to lower percent)	(5) Inverse of (3) in urban areas	(3) Proximity to existing and projected locations of low and moderate income employment
Suitability Allocation Criteria	(7) Number of acres of vacant serviced residential land (the greater the amount in acres, the greater the share of new units) (8) Number of vacant housing units (the greater the number of units, the greater the share of new units)	(5) Assessed valuation per pupil (the higher the valuation, the greater the share of new units) (6) Overcrowding in schools (the greater the overcrowding, the smaller the share of new units)	(6) Assessed valuation of pupil average daily attendance (the higher the value, the greater the share of new units) (7) Existing additional school capacity (the less the capacity, the less the share of new units) (8) Vacant residential land valued at $10,000 per acre or less (the more acres in vacant land, the greater the share of new units)	(2) Amount of land currently developed (the higher priority is given to areas with more development)	(6) Elementary school district assessed valuation per household as a percentage of the assigned valuation in urban area (for Marysville-Yuba City and urban areas only) (the higher the assessed valuation, the greater the share of new units)	(4) Availability of sites for construction of low and moderate income housing. Uniformity with state development plan and county and municipal master plans. (5) Availability of land and open space area and their intended use (6) Existence, feasibility,and estimated cost of providing local and regional public services and facilities to support proposed housing. Impact on local taxation. (7) Effect on the community and impact on existing land use development regulations

Note: Following Brooks' approach proximity to jobs was considered as a distributive criterion. The proposed New Jersey plan did not specify whether the allocation would be manipulated inversely or directly.
Source: Brooks, *Lower Income Housing: The Planners' Response.* Planning Advisory Service Report No. 282 (July-August 1972), and fair-share reports.

Although we have discussed each of the four allocation criteria separately, it is important to realize that these criteria can be interdependent. For example, in allocating housing to areas where there are jobs, one may well achieve the additional goal of housing distribution since expanding job opportunities are largely in the suburbs. Similarly, if the most suitable housing sites, e.g., those with a well-developed infrastructure, are in urban areas, then the allocation of housing to urban sites may well result in the assignment of housing to areas to greatest need.

Moreover, many fair-share plans are explicitly designed to achieve several objectives. The

Massachusetts fair-share plan, for example, stresses the equal-share approach, but also specifies that the zoning review boards be guided by such suitability considerations as open space and health and safety of local residents. That other fair-share plans also have chosen to combine several criteria is illustrated in Exhibit 1–5.

Responsibility for Building the Fair-Share Housing: The third major variation among fair-share plans involves their implementation. In some cases, the body that formulates the plan builds the housing. For example, the Urban Development Corporation's housing allocation plan is primarily a corporate planning instrument for its own use in deciding where it should build low and moderate income housing units.[197] Similarly, the Chicago Housing Authority's plan for a wider distribution of public housing units throughout the city was designed for its own use.[198]

In instances where the body formulating and promulgating the fair-share plan does not construct the housing itself, the question of just precisely who is responsible for implementing the fair-share plan is often left unanswered. In the opinion of Mary Brooks, a leading authority,[199] those allocation plans establishing priority areas for housing development (rather than allocating specific numbers of housing to subregions) are predominately directed toward developers to try to orient them to focus this construction in the priority locations. But, since the specifics of how developer compliance is to be insured is often rather vague, there is some doubt about the viability of such a strategy. In contrast, the fair-share plans that allocate specific numbers of units to communities make the locality primarily responsible for seeing that the allocated housing is built. The community can either construct the allocated housing itself or arrange for or encourage others, e.g., nonprofit housing sponsors, to do so.

Local compliance with the fair-share plan is insured by the agency effecting the fair-share plan using both persuasive and coercive strategies. The first strategy is useful when opposition to the construction of low and moderate income housing is based on unfounded fears that such activity will quickly destroy neighborhoods. In many instances, the fair-share agency can reduce opposition to their plan by attempting to persuade and demonstrate to the antagonists that the entry of lower income housing will not have an adverse impact.

But since persuasive strategy proves ineffective where the opposition is deeply rooted, many agencies have resorted to more coercive methods in order to assure compliance. For example, a regional unit of government, e.g., county government, may withhold financial aid unless a municipality agrees to build low and moderate income housing. But, by far the most popular instrument used by regional governments to insure municipal compliance has been using their A–95 review power.[200] This sanction required that municipal proposals for Federal assistance for public facilities—especially for sewer and water facilities—be first evaluated by regional planning bodies as to their necessity and regional impact. Currently, also subject to such review are all local applications to Federal agencies for subsidies or mortgage insurance for subdivisions of over 50 lots, multifamily and public housing projects of over 100 units, and mobile home courts of over 100 spaces.

Frequently, the agencies formulating and effecting the fair-share programs also are empowered to conduct the A–95 review. Therefore, they have considerable leverage in persuading municipalities to comply with fair-share requirements; because these municipalities often cannot construct sewers and other facilities without Federal aid, they tend to avoid doing anything that would incur the wrath of the review bodies. The effectiveness of this review power is corroborated by Dale Bertsch, executive director of Dayton, Ohio's fair-share program, who reports that the A–95 review power of Miami Valley Regional Planning Commission is his most important tool for insuring compliance with fair-share objectives.[201]

Fair Share: Potential Impact

Because fair-share plans are still in their infancy, it is too early to conclusively gauge their impact. But we can attempt a preliminary evaluation by discussing their potential impact and then examining their performance to date and their prospects for the future.

Fair-share plans are designed to substantially increase housing choice and housing mix

[197] Interview with James D. Wiley of the UDC, February 1973; also see foreword, New York State Urban Development Corporation, Program Development Division, Programming Unit, "Five-Year UDC Housing Development Program Guide for the Central New York Region" (December 1971).

[198] Chicago's public housing distribution action was prompted by *Gautreaux* v. *Chicago Housing Authority* 436 F.2d 306 (7th Cir. 1970).

[199] Note 168 supra at 19.

[200] See David Myhra, "A-95 Review and the Urban Planning Process," 50 *J. Urban L.* No. 3, p. 449 (February 1973), and William Brussat, "Knowing Your A-95," *Urban Land*, p. 13 (March 1973).

[201] Bertsch, in National Conference on Housing, note 188 supra at 49.

in suburban areas. The Washington, D.C., COG fair-share plan illustrates this. Back in October 1971, almost 60 percent of the federally subsidized housing units in the metropolitan Washington area were allocated for the District of Columbia.[202] Many subregions had few or no subsidized units—Fairfax County, for example, had only 6 percent while Arlington contained none. The COG plan would markedly change this uneven distribution by allocating only 20 percent of the future subsidized units to the District of Columbia—i.e., one-third its current total. Conversely, suburban areas would be given a much larger share of the region's low and moderate income housing. Fairfax County, for example, would be allocated 24 percent, while Arlington's share would be 9 percent. The projected impact of the Washington COG fair-share plan throughout the region is shown in Exhibit 1–6.

Marked changes were also envisioned by the Sacramento Regional Area Planning Commission's plan which would, if effected, significantly increase the percentage of subsidized housing units allocated in many of the region's suburbs.[203] This projected impact is not surprising, for the goal of many fair-share plans is to increase housing opportunities in the suburbs. Progress has been made in achieving this objective, but not without some difficulty, as we shall demonstrate shortly.

Fair Share: Impact to Date

Fair share has had a mixed but promising track record to date. The Metropolitan Council (Minneapolis-St. Paul) and Washington COG fair-share plans have both begun auspiciously and have elicited widespread approval. The Dayton plan, having confronted and solved numerous problems, is quite successful today. But some fair-share strategies—namely the Fairfax County, UDC, and Massachusetts plans—have encountered significant problems.

Before we examine the individual performance records, we must reemphasize that because fair share has just started, our conclusions about its results can be regarded as only tentative.

Metropolitan Council and Washington COG Plans: Auspicious Beginnings: Both the Metropolitan Council (Minneapolis-St. Paul)[204] and Washington COG fair-share plans[205] have gained strong support in their areas. The former has generated considerable suburban acceptance, as well as actual construction of low and moderate income housing; some suburban communities had even complained that they were not allocated sufficient housing. At lease 10 suburban communities already have established public housing authorities and have issued bonds to finance these authorities. Some localities have even gone so far as to adopt a Fairfax County strategy, requiring private large-scale developers to construct certain minimum percentages of low and moderate income housing.

The Washington COG fair-share plan also has received considerable initial support from both the Department of Housing and Urban Development and the COG's constituent members. The former agreed to subsidize over 6,000 housing units under the 221(d)(3)–236, 235, rent supplement, Project Rehab, Operation Breakthrough, and public housing programs. About 1,800 of these units were granted as a bonus by HUD in recognition of the COG's innovative regional allocation strategy. The COG's members cooperated in many ways—agreeing occasionally to construct public housing and granting property tax abatements on the projected subsidized housing that would be built.

To date, however, little subsidized housing has been built under the Metropolitan Council and especially the Washington COG fair-share plans. One reason for their low output is their relatively short existence—both plans were adopted in early 1972. Other restraints have been the high cost of undertaking housing without financial aid, combined with the uncertainty of obtaining housing subsidies.

Dayton Plan: Initial Difficulties Overcome: The Dayton plan was formulated in cooperation with local public officials, planning consultants, and community groups.[206] This team approach, coupled with favorable press coverage during its gestation period, resulted in the Dayton plan's unanimous adoption in September 1970 by elected officials of the Miami Valley Regional Planning Commission (MVRPC).

Its smooth beginning led to the expectation that the Dayton plan could be effectuated without opposition. However, such optimism was unfounded, according to the account of one observer:[207]

[202] See note 174 supra at II and 10.
[203] See note 181 supra at 5.
[204] Telephone interview with Metropolitan Council staff, October 1973.
[205] Telephone Interview with Washington COG staff, October 1973.
[206] Dale Bertsch and Ann Shafer, "A Regional Housing Plan: The Miami Valley Regional Planning Commission Experience," *Planner's Notebook*, pp. 2-5 (No. 1, April 1971).
[207] Lois Craig, "The Dayton Area's 'Fair Share' Housing Plan Enters the Implementation Phase," 1972 *City* 50, p. 54 (January-February 1972).

Exhibit 1–6. Impact of Washington COG Fair-Share Plan

Jurisdiction	1971 Distribution of Subsidized Housing Units	Percent of New Federally Subsidized Housing Units to be Allocated to Indicated Jurisdiction under the Fair-Share Plan
Alexandria	3.5	2.6
Arlington	.0	9.0
Bowie	.0	.2
College Park	.3	.8
District of Columbia	59.6	20.3
Fairfax County	5.9	24.4
Fairfax City	.2	.6
Greenbelt	.0	.6
Loudon County	.5	1.4
Montgomery County	7.8	26.7
Prince George's County	18.1	10.9
Prince William County	2.2	.2
Rockville	1.3	1.0

Source: Metropolitan Washington Council of Governments, "A Fair Share Housing Formula for Metropolitan Washington" (1972) at II and 10.

Consensus [in adopting the Dayton plan] did not mean mandate. Now the struggle is taking place over finding flat sites for real housing units. And if emotion did battle with reason in getting the plan accepted that was only a skirmish compared with the difficulties of implementation.

Not surprisingly there is resistance in white suburbs. There is also passionate resistance in a middle income black suburb. There is trouble too when MVRPC tries to stop proposed projects.

Resistance to the Dayton plan was often vociferous. Some of its supporters were roundly defeated in the November 1971 election. Two counties and 10 municipalities even threatened to secede from the MVRPC.[208] And when the MVRPC proposed a 166-unit for Miamisburg, a blue-collar suburb of Dayton, a local ad hoc committee was formed to oppose it. The Committee's persuasive arguments that the proposed housing would increase local taxes and overburden schools, sewers, and transportation facilities, resulted in overwhelming defeat for the Miamisburg housing plan.

Today such opposition has largely died down.[209] The reasons for the sudden change in attitude are not clear. Among the mitigating factors might be the MVRPC's established reputation, the dynamism of its executive director, Dale Bertsch, and the willingness and patience of the MVRPC's staff in explaining the fair share's intentions to hostile communities. The decline in opposition is reflected in the fact that no county or municipality ever made good on its withdrawal threats. Furthermore, there was a sharp rise in the Dayton plan's construction peace; whereas a 1972 report[210] revealed that 800 units had been built since the plan's inception, there were 3,000 completed as of early 1973 (over 4,000 if we include housing built under HUD's 235 and 502 subsidy programs). The Dayton plan, then, after weathering stiff opposition, now seems on its way to dispersing considerable numbers of low and moderate income units in the region's suburbs.

The Massachusetts Plan: Limited Success: During fiscal years 1971 to 1973, almost 50,000 low and moderate income housing units were constructed in Massachusetts under subsidy programs from HUD, Massachusetts Department of Community Affairs (MDCA), Massachusetts Housing Finance Agency (MHFA), and other agencies.[211] Although much of this housing has been built in the major cities, especially Boston, there has been considerable construction in suburban areas as well. In the opinion of MacDonald Barr, MCDA's Coordinator of Planning and Program Development, this construction has significantly broadened Massachusetts' suburban housing mix.[212]

This dispersion has not been effected through the Massachusetts zoning review plan, however, rather, it has resulted from the independent efforts of private developers. The State's fair-share strategy has in itself accomplished very little.

Two 1972 reports[213] corroborate the Massachusetts fair-share plan's slow pace. The State plan provides two levels of zoning review—one by local zoning boards of appeals and another by a State Housing Appeals Committee. As of mid-1972, only 19 appeals had been received by the latter group and perhaps more significant, a total of only 35 applications had been filed before the former group. Of this 35, 18 had been denied and subsequently appealed, 12 were still awaiting a decision, and only 5 had resulted in permits to build.[214] Of these 5 approvals, 2 were

[208] Id., at 56.

[209] Telephone interview with Ann Shafer of the Miami Valley Regional Planning Commission, October 1973.

[210] Craig, note 207 supra at 53.

[211] Telephone interview with MacDonald Barr of the Massachusetts Department of Community Affairs, October 1973.

[212] Id.

[213] See Taylor, note 194 supra and MacDonald Barr, "The Massachusetts Zoning Appeals Law: Lessons of the First Three Years," paper submitted at American Institute of Planners Conference, Boston 1972 (mimeo).

[214] Barr, note 213 supra at 6–7.

stalled until recently by court action, and the remaining 3 resulted in the construction of 364 units, all for the elderly. Clearly, the Massachusetts track record has not been impressive.

Why such a slow pace? One explanation is that until recently, the entire Massachusetts fair-share plan was under a legal cloud.[215] And there have been substantive problems as well—poorly defined administrative procedures and high out-of-pocket costs for developers who submit to the zoning review process.[216] The following account summarized the defects: [217]

> The Massachusetts suburban housing and zoning reform law is not working. Its failure can be summarized in the following manner: first its approach to the problem of inadequate housing and exclusionary zoning is negative. Rather than attempting to implement an affirmative housing strategy, the law seeks only to break down exclusionary suburban barriers where they conflict with the construction of low and moderate income housing.
>
> Second, it establishes an undesirable adversary system between developers of subsidized housing on the one hand and suburban communities which are generally opposed to such housing on the other. This increases the risk of financial loss to developers, puts communities unprepared to accept such housing in the defensive, requires an almost automatic appeal to the state, and diminishes the legitimacy of the entire housing effort. . . .
>
> Third, the law provides insufficient policy direction, planning standards and state legislative mandate by which conflicts can be resolved at the local level. . . .

The UDC Plan: Stalled by Opposition: The New York State Urban Development Corporation (UDC), established in 1969,[218] had tremendous potential for dispersing large numbers of low and moderate income housing in the State's suburbs. It had a dynamic executive director, Edward Logue, and strong support from Governor Nelson Rockfeller. Moreover, as a fair-share plan, it was unique on two counts: It had its own financing capability and was legally empowered to override local zoning restrictions. Yet, despite its commendable achievements—the construction of more than 30,000 housing units [219] and the implementation of such innovative projects as industrial condominiums—the UDC has done little in the way of housing dispersal.

Opposition to the UDC has been most vehement in Westchester County. The State's fair-share approach was initiated in this county through a UDC proposal for the construction of 900 units in the unincorporated areas of the towns of Westchester,[220] with no more than 100 units to be built in any one town or school district. The 900-unit objective was established after analysis of the UDC's statewide construction capability in relation to both the overall needs of Westchester County and to the specific requirements of the UDC's current and proposed programs in the cities and villages.

Anticipating vigorous opposition by many Westchester communities, the UDC made special conciliatory efforts. Not only would the scale of the housing projects be small (100 units each), but they would be of low density with each development situated on no less than 10 acres. In addition, each site would be provided with its own recreation spaces. And the UDC also recommended State reimbursement to those communities incurring cost-revenue deficits because of the projects.

Despite all of these concessions, the UDC projects were vociferously opposed. In September 1972, Governor Rockefeller imposed a moratorium on the UDC Westchester projects so that both UDC and local Westchester officials could further discuss the proposed housing units.[221] The present status of the UDC Westchester proposals remains unclear; no housing has been built to date; and in light of continued protest, there is some doubt whether the UDC is still committed to building these projects. The strength of the opposition is evident in the successful pressure brought to bear upon the New York legislature to strip the UDC of its power to override local zoning—a move that many feel resulted from the UDC's fair-share efforts.[222] Although it would be premature to conclude that the UDC will abandon future fair-share efforts, its experiences to date clearly reveal the potential difficulty of such undertakings.

The present impact of fair share, then, is mixed—widespread acceptance by communities in the Minneapolis-St. Paul and greater Washington areas, belated success in Dayton, and limited success in Massachusetts and New York. But what about the future? Will we be likely to see more regional allocation strategies? And what will their impact be?

Future of Fair Share

Current trends indicate increasing adoptions of fair-share plans in the future. With racial and

[215] See note 196 supra.
[216] Barry, note 213 supra at 9–12.
[217] Taylor, note 194 supra at 1.
[218] See Reilly and Shulman, "The State Urban Development Corporation: New York's Innovation," 1 *Urban Lawyer* 129 (1969).
[219] Telephone interview with New York State Urban Development Corporation staff, November 1973.
[220] See New York State Urban Development Corporation, "Fair Share" at 6 (undated).
[221] The New York Times, Dec. 27, 1972.
[222] "UDC Zoning Power Cut," in NCDH 17 *Trends in Housing* (July-August 1973).

environmental problems intensifying, there will be increasing pressure to centralize zoning-housing decisions through such instrumentalities as fair share. A growing advocacy for regional review of zoning-housing policies underlies both the American Law Institute land-use revisions [223] and national land-use bill(s).[224] Such sentiment undoubtedly will encourage the further adoption of regional housing allocation strategies.

We can expect support for fair share from at least three groups: developers, the courts, and suburban communities themselves. Housing developers, seeking expanding business opportunities in the suburbs, already have sided with antiexclusionary zoning groups, e.g., the Suburban Action Institute; [225] this same motive may also prompt developers to support fair share. Many courts involved in exclusionary zoning suits have voiced their support for a legislatively established regional housing and zoning plan that would free them from their current duties as "super planning agencies." [226] This sentiment, which has already been echoed by political leaders, points to further adoption of fair-share plans. And, finally, suburban communities themselves may well support fair share, viewing it as a lesser evil when compared to court challenge and possible overrule of their present zoning-housing policies.

Although we can expect the spread of fair-share plans, we cannot confidently predict their success in dispersing significant amounts of housing. A major restraint is the Federal housing subsidy moratorium, which already has stalled many fair-share plans. Almost no housing has been built under the Washington COG fair-share plan, for example, because the area's high housing costs would place unsubsidized units beyond the reach of low and moderate income families.[227] The continued success of the Dayton plan is also jeopardized by Federal housing subsidy cutbacks.[228] And, although increased State subsidies might compensate for Federal cutbacks in most cases, State housing aid does not match recent Federal housing subsidies.

With fair-share plans addressed primarily to housing location rather than to housing finance, their success, assuming their elimination of local opposition, depends largely upon the availability of housing subsidy funds. Lacking adequate housing subsidies, regional allocation strategies can have little impact upon the distribution of low and moderate income housing units in suburban areas.

Another possible obstacle to fair share is its conflict with nongrowth sentiments.[229] Such a hold-the-line position may well be a convenient justification by suburban communities for retaining their exclusive nature; but whatever its origins, its spreading popularity and its underlying conservatism pose a direct threat to fair-share programs. Whereas the latter strategy advocates rapid housing production within a regional plan, the nongrowth position completely rejects the desirability of speedy construction maintaining instead that housing production should be reduced, and in some cases, halted entirely. It is upon the outcome of this philosophical-social conflict and the availability of subsidies that the future of regional housing allocation depends.

Conclusion

If widespread interest is a reliable indicator, then the fair-share plan is an idea whose time has come. A marked change from the status quo requires careful analysis of the variations in such plans as well as their drawbacks and potential impacts. This article has attempted to facilitate such analysis.

[223] American Law Institute, "Model Land Development Code" (Tentative Draft No. 3, 1971).

[224] See Vance Hartke, "Toward a National Growth Policy," 22 *Catholic U.L. Rev.* 279 (1973); William Reilly, "New Directions in Federal Land Use Legislation," 1973 *Urban Law Annual* 29.

[225] See Geoffrey Shields and L. Sanford Spector, "Opening Up the Suburbs: Notes on a Movement for Social Change," 6 *Yale Rev. L. & Social Action* 300 (1972).

[226] *National Land and Investment Co.* v. *Board of Adjustment* 419 Pa. 504, 521, 215 A.2d 597, 607 (1965).

[227] See note 205 supra.

[228] See note 209 supra.

[229] See Finkler, "Nongrowth as a Planning Alternative," *ASPO Report* 283 (September 1972).

The Impact of Countercyclical Monetary and Fiscal Policies on Housing

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Introduction: The Issues

The Federal Government is now involved in the housing field in different ways and for many reasons. The purpose of this report is to examine some of the rationales often advanced for the special treatment of housing which stem from the contention that tools of monetary and fiscal policy aimed at general economic stabilization have specific impacts on housing that are differentially severe and discriminatory. The alleged discrimination against housing construction expenditures is then taken to justify special and compensatory treatment of housing under a wide range of Federal Government programs. The report will examine whether the usual tools of countercyclical monetary and fiscal policy discriminate against housing, but it leaves the evaluation of housing programs resulting from this and other concerns to others.

Cyclical Volatility

There is essentially universal agreement on several characteristics of the housing construction expenditures component of gross national product. First, housing construction expenditure is one of the most volatile of the important components of gross national product. Second, housing construction expenditures lead the business cycle at both peaks and troughs. Third, it is generally agreed that housing expenditures are more responsive to credit market conditions and exhibit shorter response lags to interest rates than other gross national product components.

The volatility of housing construction expenditure is not surprising in view of some of its economic and technological characteristics. Housing is very durable, long-lived capital with perhaps the longest life of any important GNP component. This means that the demand for the total stock of housing will tend to be relatively stable and unresponsive to many of the short-period fluctuations of the economy, especially when these changes are understood to be temporary. (These are the kinds of fluctuations that have generally characterized the relatively mild business cycles since World War II.) Like the demand for most goods and services, the demand for housing depends upon the level of income. The relevant concept of income, however, is not current income. Instead, it is permanent or lifetime income which considers a person's anticipated future income in addition to his current income.[1]

Because the business cycles of the past generation have been mild, permanent income has been relatively stable even when business turned down during periods of recession. Downturns have tended to be viewed as temporary disturbances, so the demand for the stock of housing has been little affected. By contrast, the Great Depression of the 1930's was severe. Permanent income declined, resulting in a correspondingly sharp fall in the demand for the stock of housing.

Housing construction represents additions to the stock of housing. While the demand for the stock of housing is highly stable, small changes in the demand for the stock cause large changes in the rate of construction activity. It also means that changes viewed as temporary in the remainder of the economy and also with respect to the demand for housing may, and do, show up as large shifts in housing construction. When demands for other products decline and the demand for housing remains stable, resources shift out of other uses into housing construction, and vice versa. This is why there is a widespread view that housing construction is a balance-wheel for the remainder of the economy.

For example, when temporary fluctuations produce a situation where there is a slack in labor, materials, and financial resources, some of this slack will tend to move into housing construction. Alternatively, as the economy moves closer to full employment, resources tend to be bid away from housing construction, both to other forms of construction and to other activi-

[1] Frank de Leeuw, "The Demand for Housing: A Review of Cross-Section Evidence," *Review of Economics and Statistics;* Margaret Reid, *Housing and Income* (Chicago: University of Chicago Press, 1962); and Richard E. Muth, "The Demand for Non-Farm Housing," in Arnold C. Harberger, ed., *The Demand for Durable Goods* (Chicago: University of Chicago Press, 1960).

ties, especially if some of the expansion and tightened markets for labor, materials, and credit are viewed as temporary.

Interest Sensitivity

Interest rates typically rise during the expansion phase of the cycle. The tightening of credit markets is one of the mechanisms whereby financial resources are bid away from housing construction to other purposes. Correspondingly, interest rates typically fall during the contraction phase of the cycle, which leads to an expansion of housing construction. Since some part of the change in interest rates and credit market conditions is typically viewed as temporary, there is an incentive for an amplified response on the part of housing either to take advantage of temporarily loose credit on the one hand or to postpone construction activities when credit is viewed as temporarily tight.

Several features in the U.S. financial system, some of which are direct consequences of legal and regulatory restraints, amplify these shifts. A proportion of mortgage funds used to finance housing, especially single family dwellings, is supplied by the so-called thrift institutions, savings and loans, and mutual savings banks. Savings and loans, and to a lesser degree, mutual savings banks, specialize in using their funds to make mortgage loans, in part because they are legally restricted on the type and volume of loans they can make. The sources of funds of these institutions are also regulated, especially with respect to the maximum interest rates they are permitted to pay to attract funds. Thrift institutions must compete for funds with other short term investment alternatives available to a large and growing number of sophisticated people. These funds represent an important share of people's wealth, not merely the current additions to that wealth resulting from current saving.

Thrift institutions essentially borrow short term and invest the proceeds in long term mortgages. The spread between short term and long term rates is an index of market incentives to channel funds from the short term to the mortgage market. When short term rates are low relative to mortgage rates, savings and loans tend to grow and to increase their mortgage loans. When short term rates rise relative to mortgage rates, flows to mortgage markets tend to diminish.

All interest rates tend to move with the business cycle, rising during expansions and falling during contractions. While short term and long term rates tend to move in the same direction, short term interest rates are more volatile. When the level of interest rates is cyclically low, short term rates are low relative to long term rates. When the level of rates is high, short term rates, which rise faster, tend to be higher than long term rates. That is why it is generally necessary to affect the level of rates to alter the relationship between short and long term rates.[2] Thus, interest rate movements impart some countercyclical timing to the flow of funds to thrift institutions; this, in turn, contributes to some of the countercyclical variability of housing construction as well as the corresponding countercyclical shifts in residential mortgage borrowing.[3]

During the business cycle expansion phase, if thrift institutions are prohibited from raising rates they pay, alternatives to savings accounts become more attractive. Fewer funds are thereby attracted to savings and loans and to mutual savings banks. Because of the reduction in the supply of mortgage funds, mortgage rates turn out to be higher than they would be in the absence of deposit ceilings. The effect may be tempered if other important lenders respond to the higher mortgage rates by shifting some of the funds to the mortgage market. If, however, because of State usury laws or other reasons, there also are ceilings on mortgage rates which are below yields on other uses of funds, there are no incentives for other lenders to shift into the mortgage market. Mortgage funds simply dry up.

Role of U. S. Financial System and Regulation: These mechanisms are some of the reasons why, even without government intervention or changes in public policy, housing construction would tend to be relatively volatile and to lead business cycle turns, turning up in mid-recession and down in mid-expansion.[4] It would seem that

[2] See David Meiselman, *The Term Structure of Interest Rates* (Prentice-Hall, Inc., 1962); and David Meiselman, "The Policy Implications of Current Research in the Term Structure of Interest Rates," *1968 Proceedings, Conference on Savings and Residential Financing.*

[3] Lyle E. Gramley, "Short-Term Cycles in Housing Production: An Overview of the Problems and Possible Solutions," Federal Reserve Staff Study: *Ways to Moderate Fluctuations in Housing Construction,* Board of Governors of the Federal Reserve System, (December 1972).

[4] See the charts depicting the cyclical patterns of the residential construction component to Gross National Product in both nominal and constant dollars in "Business Cycle Developments," *Department of Commerce,* various issues. See especially the chart showing the comparison of new private housing units started in the five post-World War II recoveries on page 117 of the September 1972 issue. See also charts 1 through 5 in Lyle E. Gramley, "Short-Term Cycles in Housing Production: An Overview of the Problems and Possible Solutions," Federal Reserve Staff Study: *Ways to Moderate Fluctuations in Housing Construction,* Board of Governors of the Federal Reserve System, (December 1972).

the effect of ceilings on deposit and mortgage rates tends to amplify this variability.

Does Interest Sensitivity Create a Bias Against Housing Construction? It is important to acknowledge that the interest sensitivity of housing or its cyclical variability does not necessarily represent an overall bias against housing construction. The principal reason is that the response of housing to interest rates and to the business cycle appears to be symmetrical. Analyses which emphasize the depressing effects of high and rising rates typically neglect the other side of the coin—the expansionary effects of falling rates. (In this sense, it would seem that the discussion of the phenomenon may well be the strongly biased element here, not the phenomenon itself.) The argument that cyclical variability results in higher costs is weakened by the fact that the housing construction industry is characterized by low startup costs, low fixed costs, larger numbers of relatively small firms with highly variable and nonspecialized inputs, many of which readily move between housing and other forms of construction. In addition, direct evidence on costs of variability is lacking. The term "bias" suggests that the outcome systematically differs from a norm, especially an attainable norm. The attainable norm is not specified.

Countercyclical Fiscal and Monetary Policies and Their Impacts on Housing

In the context of the above analysis of housing's sensitivity to changing credit market conditions, let us now turn to an analysis of the roles of countercyclical fiscal and monetary policies, especially with respect to their impacts on housing. Most of the differences among economists' analyses and judgments on the impact of stabilization policies on housing reduce to differences in the interpretation of the effects, especially on interest rates, of monetary and fiscal phenomena, rather than the relationship between interest rates and housing construction. Consequently, the emphasis of the report is on the interest rate effects of monetary and fiscal policies rather than on questions of the responsiveness of housing to credit market conditions.

We shall first discuss fiscal policy, then monetary policy, and finally combinations of the two. Fiscal policy is generally understood to describe the use of the spending and taxing powers of the Federal Government to moderate economic fluctuations, especially to achieve stable prices and high levels of capacity utilization. Reaching these goals is understood to be helped by stabilizing the fluctuations in aggregate expenditures.

Fiscal Policy: Changing Government Expenditures and Tax Rates

Government expenditures are seen as potentially making a contribution to the stability of aggregate expenditures by rising when aggregate expenditures are too low, and declining when aggregate expenditures are too high. The purpose of varying government expenditures is to offset some or all of the fluctuations in aggregate expenditures, especially the expenditures of the private sector, in order to achieve stability in the total of both public and private expenditures. Taxes, especially individual and corporate income taxes, are also understood to contribute to overall stability of aggregate expenditures if tax rates increase when there are excess aggregate expenditures and decrease when there are deficient aggregate expenditures. Changes in tax rates alter the amount of income left in the hands of private individuals after taxes, thereby affecting their ability and willingness to spend.

An increase in government expenditures channels resources into the public sector. If, as in the 1930's, there are vast amounts of unused resources, government expenditures may merely put to work resources which might otherwise be idle. This extreme situation surely has not been typical of the economy since the end of World War II. Thus, whatever income payments are generated by a rise in government expenditures, the rise in government expenditures typically leaves fewer resources that can be devoted to other purposes, including housing. In this general sense, there would seem to be no essential difference between housing and other uses to which the Nation's limited resources can be put.

Changing Government Expenditures. Some General Effects on Resource Allocation and Housing: There is, however, another sense in which there may be a differential shortrun, but not necessarily longrun, impact of increases in government expenditures on housing. This relates to the permanent income context of the demand for housing and the other technological factors discussed above. If there is a sharp increase in aggregate government expenditures, resources in the shortrun may be made available for government purposes by being driven out of housing. Alternatively, a decline in government expenditures, by freeing resources in the short run, may also make them available for housing construction in a similar manner. If there is a bias in this situation, it would have to reflect a secular bias in the growth of government expenditures relative to private capacity and expenditures which, in the shortrun, due to the relative mobility of resources, may affect housing more than other spending.

Along these lines it is useful to cite the research of Leonall Andersen and Jerry Jordan of the Federal Reserve Bank of St. Louis [5] regarding the shortrun impact of changes in Federal Government expenditures. It turns out that shortrun changes in government expenditures have a very shortrun impact on gross national product when taxes, as well as the stock of money, the main tool of monetary policy, are held constant. According to their findings, within 3 months after the increase in Federal Government expenditures, gross national product rises by approximately 89 percent of the initial increase in government expenditures. Thereafter, however, gross national product declines. Within a year, GNP is essentially back to its original point. Government expenditures replace or "crowd out" private expenditures, and alter the composition of expenditures and output. This is in the context of a given stock of money, which seems to be the central variable controlling aggregate GNP.

The change in government expenditures mainly changes the composition of expenditures and of output. Thus, holding the stock of money constant, if we consider a large increase in government expenditures, we may well get a lagged, but abrupt, decline in housing expenditures as private GNP shrinks. Alternatively, for a significant decline in government expenditures the resulting increase in private GNP may have a differentially large positive impact on housing expenditures in the shortrun. There is, however, no direct evidence on the relationships between government expenditures in general and housing expenditures in particular.

Finally, there would seem to be relatively little support for the use of variations in government expenditures as a stabilization tool. The reasons generally offered are well known and typically reflect concern about the long lags required to change government expenditures, problems involved in specifying which expenditures are to be altered over which span of time, and uncertainty about the aggregative and resource allocative effects of what is generally taken to be an extremely crude instrument of stabilization policy. These are some of the reasons that most discussions of monetary and fiscal policy tools for stabilization typically center on varying either tax rates or the money supply.

Changing Tax Rates. Impacts on Interest Rates and on Household Spending and Saving: For given levels of government expenditures and the stock of money, variations in tax rates also have been proposed to stabilize aggregate demand and influence housing expenditures. During periods of excess demand pressures, an increase in income tax rates tends to reduce aggregate demand by draining off from the private sector some of the income that might otherwise be spent. It is as if the increase in tax rates and the corresponding rise in tax revenues become instruments for increasing the saving of the private sector. The increase in Treasury receipts necessitates the sale of fewer bonds if there had been a deficit (or the retirement of more debt if there is a surplus). The decline in bond offerings tends to lower the interest rate. Because housing is taken to be especially sensitive to interest rates, the increase in tax rates is seen as simultaneously reducing expenditures in the aggregate and stimulating expenditures for housing in particular. This is especially true if the tax rise is coupled with an expansionary monetary policy. These were some of the reasons advanced in support of the 10 percent surtax which was enacted in 1968.

The evidence from many studies of consumer behavior indicates that consumer outlays depend largely on longrun expected income—permanent income, rather than current income after taxes. Changes in income tax rates, especially when understood as temporary, have little effect on permanent income. Variations in tax rates for short-period stabilization purposes are bound to be interpreted as temporary, especially with repeated use. They can be expected to have only small effects on consumption outlays. If income tax rates increase, consumer spending is little affected in the shortrun. Consumers adjust to the higher taxes by reducing saving.

Impacts on Investment Outlays: Similarly, the evidence from many studies on investment behavior also suggests that outlays for capital goods depend on longrun expected profits after taxes, not current profits after taxes. Thus, a temporary rise in corporation income tax rates, rather than reducing capital outlays, merely tends to lower net corporate retained earnings,

[5] Leonall C. Andersen and Jerry L. Jordan, "Monetary and Fiscal Actions: A Test of their Relative Importance in Economic Stabilization," *Review, Federal Reserve Bank of St. Louis,* Vol. 50 (November 1968).

current corporate saving. Because capital outlays are little affected, corporations, too, pay for the higher taxes mainly by reducing saving.

The Permanent Income Hypothesis: A corollary of the permanent income hypothesis is that changes in income tax rates viewed as temporary also tend to have very minor effects on interest rates. Most current saving shows up as an addition to the supply of loans, however complex the network of financial intermediaries the funds pass through. When saving falls in response to the temporary rise in income tax rates, the supply of loan funds declines, roughly matching the decline in the Treasury's borrowing needs. On balance, then, very little happens to interest rates. The same mechanisms also hold for shortrun decreases in income tax rates. These are also some of the reasons why there has been widespread disenchantment with the use of shortrun variations in tax policy, so-called "fine-tuning," to offset the effects of shortrun variations in public as well as in private spending. The same analysis holds for the impact of shortrun variations in the Investment Credit.

It should be noted that temporary variations in sales taxes would tend to have a significant impact for the same reasons that temporary changes in income taxes do not. A rise in sales or excise taxes, when viewed as temporary, would tend to cause people to reduce or postpone purchases until the tax fell. Thus, the effect on spending would be greater than if the sales tax increase were understood to be permanent. Little use has been made of sales taxes for stabilization purposes, and there appears to be no widespread support for the countercyclical use of general or specific sales taxes or value added taxes.

Is There a Bias For or Against Housing? The limited shortrun effects of countercyclical variations in income tax rates would seem to leave little basis for any bias for or against housing. Of course, the long-period permanent tax structure does affect resource allocation, including housing, since permanent tax levels influence saving, or using resources for investment in housing rather than other purposes.

Monetary Policy

Let us now turn to monetary policy. There are two main analytical orientations for evaluating monetary policy. One looks to interest rates and credit market conditions as the appropriate indicators of monetary policy. The other emphasizes the quantity of money as the correct indicator of monetary policy. The interpretation of both the intent and the impact of monetary policy, including the implications for housing, depend crucially on which analysis is used. Because the two approaches often yield contradictory results, it may prove helpful to delineate each in order to understand, and perhaps to reconcile, apparent differences in analyses and in policy conclusions.

The quantity of money is essentially whatever the Federal Reserve desires or permits it to be. The Federal Reserve can control the quantity of money within rather narrow limits as a matter of deliberate policy. However, it may prefer to control other variables such as interest rates, or to exert no specific control at all.

Money is usually understood to be the volume of currency and coin held in private hands outside banks plus commercial bank deposits—checkbook money. Some monetary experts prefer to define money to include all commercial bank deposits in addition to currency and coin. The two measures of money typically move together and the relationships between either money concept and GNP and other important economic variables tend to be similar. Thus, for most discussions it makes little difference which concept of money is used. (One slight difference is that the broader definition of money, M_2, tends to have a somewhat longer lead, rarely more than one quarter, over GNP and business conditions than the narrower definition of money, M_1.)

Money and Interest Rates: According to the credit view, when there is an increase in the quantity of money, people take some of the additional money and use it to make loans, buy bonds, or acquire other credit instruments, thereby lowering interest rates. (A decrease in the demand for money would tend to have the same easing effects on interest rates and credit market conditions.) Alternatively, a decrease in the quantity of money would lead some people to try to reestablish their cash positions by selling bonds and other credit instruments or by making fewer loans, thereby raising interest rates.

The change in interest rates becomes more than a financial matter because changes in interest rates alter incentives to spending, especially on long-lived assets such as housing, plant and equipment, and other producer durables. The sequence of events is understood to lead from money to interest rates to capital goods.

This is why, following the credit view, the initial impact of monetary policy, and under many circumstances the intent of monetary policy, too, is largely evaluated in terms of interest rates and credit markets. Indeed, the terms money and credit generally are used interchangeably. Rising interest rates are interpreted as reflecting a restrictive monetary policy—tight money—and falling interest rates are interpreted as a consequence of an expansionary monetary policy—easy money.

Impacts on Resource Allocation: Because interest rates respond to Federal Reserve action, and spending for capital goods responds to interest rates, it therefore follows that monetary policy can influence total spending and total income as well as the division of the economy's output between capital goods and consumer goods.

There is a presumption that changes in interest rates affect various parts of the private sector differently. For example, housing is taken to be especially sensitive to interest rate changes, but outlays on consumer services or food are assumed to be relatively insensitive. Thus, credit policy is understood to affect both the level of output, the composition of output, and the rate of growth. There are also parallel and reciprocal effects on many kinds of financial institutions and financing activities that depend on the level of interest rates. Deliberate use of monetary (credit) policy is thereby taken to imply an added dimension of control over the size and composition of output, the rate of economic growth, and the many other issues involving the allocation of both real and financial resources as well as the welfare of particular industries and financial institutions.

The Mix of Monetary and Fiscal Policies: This view of monetary policy also encourages its use in combination with fiscal policy and is correspondingly associated with great concern over the "mix" of monetary and fiscal policies. The basic rationale for the "mix" is as follows: If more money leads to lower interest rates, and low interest rates encourage capital formation, there may be such a large volume of expenditures for capital goods that excess demand pressure is created which leads to inflation. One prescription for encouraging large-scale capital formation without inflation is to combine an easy credit policy with budget surpluses—a tight fiscal policy. The expansionary monetary policy's low interest rates encourage capital formation; the tight fiscal policy's high taxes restrain the boom. This policy "mix" envisages public sector surpluses and the use of taxation to force people to consume less of their current income, thereby freeing resources to move into capital formation. The low interest rates encourage the use of the resources for the production of housing and other capital goods. If higher interest rates were employed to achieve the same reduced consumption, these higher interest rates would be a deterrent to capital formation.

Following this analysis, the use of credit policy to affect aggregate demand has frequently led to charges that monetary policy is discriminatory because it appears to bear most heavily on those classes of expenditures that are interest-sensitive, including housing. As mentioned above, most of this discussion is itself biased because it generally focuses only on periods of restrictive monetary policy and omits differentially stimulating effects of easy credit at other periods of the business cycle.

One proposal to moderate the alleged discriminatory effects of monetary policy is to vary the "mix" of monetary and fiscal policies. If, for example, there is undesirable inflationary pressure, reliance on restrictive monetary policy to counter the inflation is taken to involve higher interest rates. To mitigate the rise in rates and still achieve the same restraint on aggregate expenditures, this approach suggests that income tax rates be raised in order to place less of a so-called "burden" on monetary policy. A proportionate increase in income tax rates is assumed to reduce all demands more evenly than if monetary policy achieved the same aggregate effects. At the same time, the additional restraint imposed by higher taxes would permit an easier monetary policy with its associated lower interest rates. This was a major part of the case for the 1968 surtax that failed to stem both accelerating inflation and rising interest rates.

These arguments are flawed for several reasons. The first, discussed above, relates to the weak shortrun impact on aggregate demand of changes in tax rates, which brings into serious question whether there is any effective trade-off in the short period of the business cycle. The second relates to the analysis of monetary policy with respect to the consequences of changes in the quantity of money for interest rates and, therefore, for housing. In my judgment, the response of interest rates to monetary change is almost exactly the opposite of that indicated by the above analysis. This is why I conclude that the quantity of money rather than interest rates should be used as the indicator of monetary policy.

The approach that emphasizes the quantity of money rather than interest rates as the appropriate indicator of monetary policy does not presume that people use money only to buy securities and credit instruments. When there is an increase in the quantity of money, people can take some of the money and use it to buy goods as well as securities. Monetary change can and does affect spending directly; it need not pass through credit markets. (I shall report below some recent findings in my research regarding the response of housing expenditures to monetary change.)

Traditional credit analysis of monetary change has another, and possibly more important, flaw because it overlooks virtually all of the feedback effects of the initial impact of monetary change on credit markets, which tends to contradict the initial impact. The credit view, by focusing on the initial impact, takes many of the initial effects of monetary change to be the final ones. It turns out that the feedbacks are so great that they generally swamp the initial effects of monetary change. This explains why expansionary monetary policy eventually leads to higher, not lower, interest rates. Further, even though in the very first instance monetary contraction may temporarily drive up rates, contractionary monetary policy eventually produces lower interest rates. The initial impact of monetary change on housing is only the first scene in a larger drama.

There are two mechanisms that help to explain these feedbacks.[6] First, an increase in money eventually leads to an increase in aggregate demand. Interest rates may initially fall if the increase in money is associated with a corresponding increase in bank credit, as it usually is. Later, the increase in aggregate demand tends to drive up prices. As we have learned in recent years, inflation tends to cause interest rates to rise.[7] Second, if the monetary expansion starts from a period when the economy has some slack, the resulting rise in aggregate demand generally leads to higher employment and to a rise in real income. Business profits also tend to rise. In fact, profits generally rise proportionately more than output during business cycle expansions. As the profitability and the productivity of capital rises during the expansionary process, business loan demands to finance capital expenditures increase. In addition, as incomes rise, many consumers also increase their demands for credit to finance the acquisition of durable goods and other purchases.

After a lag, the simultaneous increase in consumer and business demand for credit eventually swamps the change in the supply of credit stemming from the initial increase in the money supply. Thus, the rate of interest rises. When a rise in interest rates stems from an increase in demand for credit, the Federal Reserve attempts to keep rates from rising by increasing the money supply and bank credit will lead to still higher interest rates. The opposite sequence of events occurs when there is a contraction of the money supply. Although interest rates may rise initially, they tend to end up lower than before the monetary contraction. This is why interest rates are high during booms and low during business cycle contractions. This also explains why interest rates are very high in countries that experience much inflation; why rates were very low during the Great Depression of the 1930's, despite the severe contraction of money, which was its major cause; and why the focus on interest rates may lead people to misinterpret both the impact and the intent of Federal Reserve policy.

The Lagged Impact of Money on Housing: I have been conducting research on the impact of changes in the quantity of money on both the aggregate of expenditures and the differential impact of money on components of GNP[8] and have experimented with different estimating techniques, including the Almon lag technique, for estimating the response of housing construction expenditures and other GNP components.[9] The distributed lag relations between first differences of the nominal stock of money, M_1, and housing construction expenditures, using quarterly, seasonably adjusted data for the period 1952 through 1969, are as follows:[10]

[6] See Milton Friedman, "The Role of Monetary Policy," *The American Economic Review*, Vol. 58 (March 1968); David Meiselman, "The Role of Money in National Economic Policy," *Controlling Monetary Aggregates* (Boston: Federal Reserve Bank of Boston, 1969), and William E. Gibson, "Interest Rates and Monetary Policy," *Journal of Political Economy*, (May-June 1970).

[7] See David Meiselman, "Bond Yields and the Price Level: The Gibson Paradox Regained," in *Banking and Monetary Studies*, Deane Carson, ed., (1963).

[8] See David Meiselman and Thomas Simpson, "Monetary Policy and Consumer Expenditures: The Historical Evidence," *Consumer Spending and Monetary Policy: The Linkages*, Federal Reserve Bank of Boston, 1971.

[9] A 4th degree interpolating polynomial constrained to zero at $(t + l)$ and $(t - n)$, where n is the length of the lag, was used for the published results. Experiments with unconstrained regressions as well as single-ended constraints at $(t + l)$ and $(t - n)$ were also performed. Some of these results will be presented in this paper.

[10] See Meiselman and Simpson, "Monetary Policy and Consumer Expenditures," table 13, page 252.

$$\Delta H = 0.085 + \underset{(5.86)}{0.395\Delta M_t} + \underset{(7.17)}{0.291\Delta M_{t-1}} + \underset{(0.35)}{0.019\Delta M_{t-2}}$$
$$(0.54)$$
$$\underset{(-3.84)}{-0.202\Delta M_{t-3}} \underset{(-6.16)}{-0.261\Delta M_{t-4}} \underset{(-2.20)}{-0.157\Delta M_{t-5}}$$

Sum: 0.084
(0.75)

$R^2 = 0.46$

Durbin-Watson statistic = 1.54

The "t" statistics for the regression coefficients are in parentheses.

For the broader definition of money, M_2, the distributed lag relations between first differences of money and first differences of housing construction expenditures are similar.[11] In commenting on these results, the study noted:

> The responsiveness of expenditures for residential construction, H, to changes in M_1 is one of the most interesting aspects of (the study). Monetary policy has a relatively great impact on housing expenditures in the same quarter. The coefficient of 0.395 indicates that when M_1 increases by one dollar, housing expenditures in the same quarter increase by 39.5¢, which is about 28% of the synchronous change in GNP explained by the change in M_1. One quarter later, housing expenditures expand to 68.6¢ for each dollar increase in M_1, or 29.1¢ more than in all the quarter before. One quarter later, the effect of the once-for-all change in the stock of money or the flow of housing construction expenditures is essentially a maximum of 70.5¢ for each dollar increase in M_1. By the third quarter housing construction expenditures fall by 20¢. In the fourth quarter they continue to fall. By the fifth quarter the cumulative effect is essentially zero, and housing construction expenditures have returned to the level that existed before the once-for-all change in M_1. Housing construction expenditures are affected only temporarily, but the temporary change in housing construction does tend to alter the stock of housing permanently.
>
> The pattern of lags for housing suggests several elements of the adjustment process to monetary change, including an apparent tendency for overshooting, which may help to generate cycles in housing construction expenditures, especially in the context of variable rates of monetary change. If the demand for housing is related to interest rates, as is generally conceded, the initial increase in the stock of money, by lowering interest rates, quickly causes a sharp increase in housing construction expenditures. However, once the effects of monetary change result in an increase in aggregate demand, interest rates start to rise, moderating the increase in demand. As GNP rises further, there is a tendency for interest rates to continue rising and to over-shoot, ending up higher than before the monetary expansion. The resulting tendency for a housing retardation may also be strengthened by resources being bid away from housing construction by the expansion of other GNP components which respond to monetary change with longer lags. These may be some of the damping mechanisms for both housing and consumer durables, as well as for the economy as a whole. (Note that the lag patterns for consumer durables suggest a response generally similar to housing but somewhat weaker and slower.) The U.S. financial structure and regulation would appear to accentuate these tendencies. (pp. 261–262)

[11] Ibid., table 14, page 254.

More recently I have attempted to test, extend, and replicate these results by examining the distributed lag relations between monetary change and housing construction expenditures by experimenting with alternative forms of the Almon lag estimating technique as well as other estimating techniques, including ordinary least squares and spectral regression. Although there are some differences in the distribution of the coefficients—the lags may be somewhat larger than in the original study—the sum of the coefficients remains essentially zero. This means that monetary change has no longrun effect on housing construction expenditures.

There is a complementary analysis by Arnold Harberger that emphasizes the permanent income hypothesis in explaining the strong impact of monetary change and the weak impact of fiscal policy on housing.

> . . . I don't believe that fiscal policy is designed for the fine tuning of the economy. I think that our experience with the temporary surcharge shows that if people know that an extra tax is temporary and that it is soon going off, it doesn't much affect their behavior. Nor does a temporary reduction in taxes much affect their behavior.
>
> The permanent income hypothesis and a number of other explanations of consumption behavior all lean in the direction of saying that the reaction of people to unexpected or short-run changes in their income position is much weaker than their reaction to longer-run changes in fiscal policy. Reactions to price changes, on the other hand, are quite different. The reaction of a housewife to a permanent reduction in the price of white sheets will be smaller than the reaction of the same housewife to the January white sale. Since sheets are cheaper only so long as you buy them in January, the response to a short-term price reduction will be larger than that stemming from a permanent reduction of the same magnitude in the price of sheets.
>
> Monetary policy is like that. When interest rates go down in a fashion which is not regarded to be permanent, you get people to enter the market as borrowers in order to take advantage of the bargain price of credit. When interest rates go up in a way that is not regarded to be permanent, people hold off the market in a way that they would not do if those higher interest rates were to prevail forever. So, you get a lot of bang out of fine tuning the economy by way of monetary policy—an amount of bang that I do not think can be duplicated readily by temporary movements in fiscal policy. As a consequence I think that the proper way of operating the economy—not just proper, but even almost necessary—is to set fiscal policy with regard to relatively longer term considerations, and to leave to the monetary authority the job of helping us attain our particullar policy goals in the shorter run. This is my first major point.
>
> If one accepts that position, there is a consequence that almost inevitably follows. That is that historically the construction industry has been what I call the handmaiden of monetary policy. When monetary policy is tight, the construction industry is squeezed. The purpose of tight monetary policy is to free resources some—to reduce the total demand for resources, if you like—and that squeeze takes place largely by pushing resources out of the construction industry. And when monetary policy is easy, somehow the

resources crawl out of the woodwork to allow housing starts to go up by three or four hundred thousand, as between a tight and an easy period.

. . . the housing industry has acted as a sponge, absorbing resources when money is easy and releasing them when it is tight . . . [12]

Does Countercyclical Stabilization Policy Discriminate Against Housing?

To sum up, based on analysis and the evidence there is no clear or convincing case that the tools of fiscal and monetary policy aimed at short-period economic stabilization discriminate against housing.[13] The instruments of monetary and fiscal policy in the shortrun may cause some intertemporal shifting of housing construction activity, but there is no evidence that they have any permanent effects on construction.

It is worth noting that special concern for short-period variations in construction activity, on the other hand, may have had a role in the inflationary bias of public policy in recent years. Paradoxically, concern for housing may have worsened housing rather than the other way around. Because rising interest rates in the short run appear to bear heavily on construction, the attempt to modify the depressing impact of rising interest rates on housing has contributed to the excessive focus of monetary policy on interest rates. To stem a high rise in interest rates, the Federal Reserve has repeatedly resorted to excessive money creation. In the very shortrun, the easy money has moderated the rise in interest rates, and as a consequence has tended to stimulate housing in the very shortrun. However, the longer-period effect of the additional money is to cause still more inflation, and still higher interest rates, without at the same time causing any permanent change in the volume of nominal housing construction expenditures. Because prices have risen, I suspect that if the estimates presented in this report were corrected for price change and were in real rather than nominal terms, it would turn out that monetary increase might well lead to a decrease in real construction rather than returning it to the zero point.

[12] Arnold C. Harberger, "Discussion," *Housing and Monetary Policy*, Conference Series No. 4, Federal Reserve Bank of Boston, (October 1970), pp. 36–37.

[13] See also Norman N. Bowsher and Lionel Kalish, "Does Slower Monetary Expansion Discriminate Against Housing?" *Review, Federal Reserve Bank of St. Louis*, (June 1968).

Although there is no evidence that the cyclical instability of housing construction seriously increases costs, nobody argues that the high cyclical variability of housing construction is "good" for housing. But housing is not the entire economy, and even though construction varies widely, the stock of housing and the flow of housing services are very stable from year to year. If there are specific policies to insulate housing, there may be greater instability elsewhere in the economy with, perhaps, greater costs than in housing construction, an activity uniquely well suited to minimize the costs of changes over mild business cycles. Much of this discussion would be helped if it were placed in the context of what is attainable for the economy as a whole. To the extent that instability in monetary and fiscal policies is reflected in instability in housing, there is still another argument for avoiding the stop-go policies which themselves have been independent sources of economic instability. For monetary policy, this requires a relatively stable rate of growth of money, and for fiscal policy, corresponding stability and predictability in both tax rates and expenditures.

Secular Inflation and Housing Policy

It is also important to note that even though this report is skeptical regarding the claims of discrimination against housing during the business cycle, there does appear to be some merit to the claim that the lack of effective long-period stabilization policy, notably the inability to maintain stable prices over time, is likely to have a depressing effect on housing construction. In other words, secular inflation, especially at a variable and unpredictable rate, would seem to bias investment decisions against housing. Some of the reasons relate to the nature of financial regulation, especially regulations relating to maximum interest rates on both mortgages and deposits that do not take the inflation adjustment into account. Another reason is that long-period, variable, and unpredictable rates of inflation tend to shorten the planning horizon, biasing people's spending decisions toward shorter-period consumption expenditures and away from long-period commitments of the kind required for housing production and finance.

The Housing Hunt: An Analysis of Buyer Behavior and Market Structure in Light of Recent Research

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Introduction

The study to follow analyzes housing search behavior, the relevant institutions of the housing market and the interaction between the two. The study will proceed by describing first the relevant aspects of the search for housing when viewed as a behavioral process; then by describing the structural elements of the housing market that affect the search process, and finally by describing the actual and potential empirical indexes used to evaluate and describe the search process.

Search Behavior

The search for housing must be viewed as part of a larger field of study: consumer behavior. Consumer behavior, for the purpose of this study, is defined as, "the acts of individuals directly involved in obtaining and using economic goods and services including the decision process that precedes and determines these acts." (Engel, p. 5.)

Thus, search must be viewed in the center of a larger analytical model of the consumer decision process. The consumer decision process can be analyzed through the following classification system: in the first stage, the consumer becomes aware of a particular need. In so doing, the consumer generates a perception of the goal object desired. In the second stage, the search process is initiated. The search process involves the following steps: First, the acquisition of information; second, with the help of this information, recognition of alternative solutions; third, the evaluation of these solutions; fourth, the selection of a consumption strategy; fifth, the purchase decision. (Donald H. Grambois, 1963.)

In a more formal sense, consumer search is defined as a set of information seeking and information processing activities in which a consumer engages, preliminary to a decision on obtaining some goal object presumed by that consumer to be available in the market place. (Kelley, p. 273.)

In order to link together each stage in the consumer search process, a tacit or explicit decision must be made by the consumer involving an evaluation of both the previous stages and those still to be performed. Thus, search behavior and its duration depend upon the consumer's perceptional value of the results of search and the costs involved in engaging in search. Thus the rational consumer will proceed only when the increment to the perceived value of the good purchased through a unit of search is equal to the perceived cost of the unit of search.

The perceived value of the good can be affected by the store of information available to recall to the person, the appropriateness of the stored information, and the perceived risk obtained through the procession of this acquired goal. Use of this information is occasionally termed "internal" search. The determinant of internal search can be analyzed in terms of social, psychological, and financial risks.

In turn, external search involves the transformation of wealth into activity within the housing market. Additional increments of search extend the time that the consumer must live with the awareness of the initial problem; the seller searching for the best buyer faces this same situation. Thus, the consumer's perception of a lengthened search process may induce two alternative behaviors: First, search may be intensified in order to reduce the perceived time delay, or second, search may be retarded through a reevaluation of the initial goal.

The performance of external search involves actual costs; that is, real inputs of resources must be spent in the process of gathering the information. Similarly, the cost of search is elevated for some persons as well as social groups due to the psychological risk perceived to exist for them when confronting the various sources of information.

The Structural Determinants of Housing Search

Of equal importance, consumer search can be viewed from the point of view of the structural determinants of the entire consumer decision process. Search behavior is itself determined by the disposition of the various elements and institutions whose presence defines the particular market in which the consumer finds himself. To the extent that an actor's perception does not match reality, personal satisfaction will require a change in the perceptual goal image. In the long run, the structural determinants of the search process will alter the initial goal present to the consumer. A marked absence of the commodity desired will probably halt the search process. Likewise, the presence of the object, but at a price exceeding that which the consumer can pay, will halt the search process.

From the point of view of the economist, search behavior is analyzed as the outgrowth of price dispersion. To the extent that the seller offers a homogeneous product, price dispersion becomes a measure of ignorance in the market. (Stigler, p. 214.) Thus the removal of ignorance through search will probably alert the buyer to a lower selling price. It is assumed, however, that increased search will yield diminished returns as measured by the expected reduction in the minimum asking price. (Stigler, p. 215.)

The market for unique goods such as housing is representative of a problem of ignorance. Out of the difficulty manifested in finding the correct buyer or seller has emerged a diverse set of institutions capitalizing upon the reduction in housing market ignorance. The principal middleman is, of course, the real estate broker. However, of equal importance at certain stages of the search process are the financial institutions, friends and associates, newspapers, and the channels of purposeful or accidental information flow. Under certain conditions the searcher can also be a source of information. To the extent that past experiences are relevant, memory will serve to modify (most likely to shorten) search behavior. Housing does not represent a repetitively purchased item; the circumstances of spatial location, time frame, and a high, but subtle, degree of complexity render even the highly mobile individual unfamiliar with the housing market he is presently involved in. These factors necessitate the transformation of personal resources into the search process. Thus the seller will place signs directing prospective buyers or renters to his property, acquire real estate agents, and/or advertise through one or more types of newspapers; however, this is not so much for the purpose of reducing price dispersion as it is for the identification of a product to be marketed. It is the prospective buyers who reduce the price dispersion through their varying degrees of search and as a result find available houses, observe them, find financing, and close the transaction. Income-related search behavior has also been clarified by economists. Several empirical studies over the preceding decade have indicated that the quantity of housing bought, as measured by its purchase price, increases but at a decreasing rate with increases in family income. For this reason it will pay the wealthier buyer to search longer to find the best package of housing services available to him. (Mincer, p. 80.) Therefore, it is expected that the private market will respond with middleman services that are income-dependent in their provision.

The Structural Determinants

The structural determinants of the search process can be analytically identified as the following:

1. The goal elements whose purchase (sale) is desired by the consumer.

2. The set of objects responsible for producing information regarding the availability of the goal objects.

3. The socioeconomic conditions of the searcher that determine his ability to proceed through the search process.

The Goal Objects

Thus independent of the perception obtained by the searcher, there exists a set of real objects, the quantity and price of which are formed independently of the shortrun efforts and desires of the searcher. In the case of housing, the stock of acceptable housing is determined by structural configuration, neighborhood effects, and price level. In other words, the search for adequate or acceptable housing is constrained by the initial specification placed upon housing by the searcher, the characteristics of the stock, and its relation to present job location.

Preconceived specifications limit the applicability of many information sources. In one of the original studies in this field, Rossi found that 51 percent of the families seeking housing had specific space dimensions as a prerequisite.

Overlapping with this, he found that 50 percent of the families had particular design requirements involving heating, layout, and utilities. Although less important, specific neighborhood attributes formed constraints to search. Among the most important is the location of a proposed dwelling unit. In a similar fashion, tenure forms a constraint to the search process. Rossi's 1950 study found that a relatively small percentage of searchers avail themselves of both the rental and the ownership market in their search for dwelling units. It was found that 89 percent of present renters search only within the homeownership market. Thus, depending upon the supply of dwellings in either market, prior commitment to one market but not the other can extend the search process. When viewed on the macro-level, this suggests that the rate of transfers will be markedly slowed when compared to the situation in which the searcher will avail himself of both markets.

Information Channels: The characteristics of channels of information materially affect the search process. The basic channels for housing information are six:

- Friends, relatives, and business associates;
- Real estate agencies;
- Mass media;
- Signs on or directing searchers to a specific location;
- Banks, lending institutions;
- Builders and contractors.

The characteristics used to define are two:

- The breadth of coverage;
- Its effectiveness vis-a-vis successful completion of the search process.

Socioeconomic Determinant of Search Behavior: The socioeconomic characteristics of the potential consumer determine the outcome of each of the stages within the search process. From the perspective of consumer behavior, four socioeconomic characteristics have been found to increase the intensity of the search process. These are:

- The consumer is in the middle income category (as opposed to high or low income category);
- The consumer has a college education;
- The consumer is under 35 years of age;
- The consumer's education falls in the white collar class. (Engal, Kollat and Blackwell, p. 387.)

Empirical Research: The empirical analysis of the search process as it relates to the housing market requires a set of operational definitions of search behavior. Donald Hempel, in the most exhaustive study of the phenomenon yet performed, resolves this issue by defining the three dimensions of search. The first dimension is the length of time during which the buyer is engaged in the search process. Duration of search is both a measure of the buyer's behavior and structural determinants of the housing market. From the point of view of the individual it represents the period during which information sources will be actively utilized. All other things being equal, it represents the presence of a pre-established set of object attributes and the ability of the searcher to maintain his present residential location over that period of time. From the point of view of the housing market the duration of the search represents either a limitation in the supply of the type of dwelling unit or the failure of information channels to alert the searcher to the existence of available units.

The second dimension to the specification of search behavior is the number and types of information sources. This is viewed as an indirect measure of search behavior. As in the previous dimension the meaning imputed to the indexes of the dimension have both a behavioral and structural perspective. On the personal level utilization of various information sources depends upon the previous store of knowledge held by the searcher. The degree of urgency placed upon the acquisition of the goal object and the personal resources, i.e., time and/or money available to the searcher. Interacting with the behavioral determinants of search intensity are structural characteristics. The structural determinants of search intensity are both intrinsic to the searcher and a property of the market within which he is an actor. Socioeconomic characteristics of the searcher can eliminate certain information sources from his effective utilization. Race and ethnicity are known to limit the searcher to certain spatial locations and specific information sources. Similarly, the lack of ability of the searcher to purchase the essential professional help will block entry of certain types of institutionalized middlemen to the low income housing market.

The intensity of search also depends upon the characteristics of the market. For example, a tight market for a particular type of housing will necessitate a more intensive search effort. The ability to obtain a specific level of financing is determined to a certain extent by national or regional economic conditions as well as the existence of government aid. Finally, the perception of the owner, agent, or landlord of the acceptable occupant vis-a-vis phase of life cycle, race, or income level will generate varying degrees of search intensity on both sides of the market.

The third dimension used to measure search behavior is the degree of active participation performed by the searcher. This includes personal observation, examination, and inspection of the dwelling unit. Activity in this dimension generates the greatest cost for the searcher; thus, it is to be expected that all other things being equal, the termination of the search activity should be most closely related to activity on this dimension.

Analysis: The basic research into search behavior comes largely from the work of Donald Hempel. The empirical results to follow for the most part fill out Hempel's three-dimensional empirical paradigm of the buyer's search process. Search from the housing seller's point of view is limited to secondhand observation and conjectural statements.

Hempel's research involves an analysis of 335 questionnaires obtained from two Connecticut metropolitan areas for home buyers in 1967 and 1968. In order to obtain a homogeneous sample, houses were chosen for inclusion in the study if their sale price ranged from $18,000 to $35,000 (p. 242).

The initial analysis is conducted in two parts. First, an analysis of the three dimensions of search behavior obtained from the aggregate samples, and second, the analysis of the same information when the sample is partitioned by means of various socioeconomic characteristics of the buyers.

The first dimension measuring search behavior is the duration of search. Exhibit 1 shows that this is conceptualized in terms of three timeframes: First, the time interval between decision to look and the signing of the purchase agreement; second, the interval between actual newspaper search and purchase agreement; and third, the interval between contact with the real estate agent and the purchase. Clearly, each time the prospective buyer takes a more active stance the search period is shortened. Therefore, all other things being equal, individual initiative is an effective input in the search process.

The second dimension of search behavior is the extent of information seeking. Four measures describe behavior on this axis: First, the number of information sources actually used; second, the number of dwelling units about which information is acquired; third, the number of real estate agents contacted; and fourth, the number of agents contacted regarding financing. Exhibit 2 displays this information.

Exhibit 1. The First Dimension of Search Behavior: The Duration of Search in Terms of Months

Operational Deviation	Median	Mean	Standard Deviation	No. of Respondents
Time interval between decision to look for new residence and signing of purchase agreement.	4	8.8	14.0	251
Time interval between start of search through homes-for-sale section of newspaper and signing of purchase agreement	3	7.8	10.7	352
Time interval between contacting first real estate agent and signing of purchase agreement	2	6.7	12.5	244

Source: Donald J. Hempel, "Search Behavior and Information Utilization in the Home Buying Process," Center for Real Estate and Urban Economic Studies, The University of Connecticut, p. 243.

The median score shows that the first 50 percent of the respondents, as rank-ordered on the number of information sources used, specified the use of up to four sources. Most likely this includes newspapers, friends, signs, and real estate agents. In that the mean for the total distribution of respondents is 4.8 sources, it is safe to say that only one major population of search was identified by this characteristic. In fact, only in the case of the "number of dwelling units for which information is sought" is there evidence for the existence of several subpopulations of buyers. The reason for this is that 50 percent of the buyers were successful after at most 10 dwelling unit inspections. However, the search by the remaining 50 percent increased the average number of dwelling units for which the information was asked up to 19 per buyer. Why some buyers should want or need to carry on such extensive information seeking will be explored

Exhibit 2. The Second Dimension of Search Behavior: The Intensity of Information Source Utilization

Operational Deviation	Median	Mean	Standard Deviation	No. of Respondents
Number of different types of information sources used	4	4.8	2.3	335
Number of dwelling units about which information was requested	10	19.0	26.7	252
Number of real estate firms contacted	3	3.8	4.4	335
Number of lending institutions contacted about mortgage loan	2	2.9	6.6	250

Source: Donald J. Hempel, "Search Behavior," p. 243.

Exhibit 3. The Third Dimension of Search Behavior: The Intensity of Dwelling Unit Examination

Operational Deviation	Median	Mean	Standard Deviation	No. of Respondents
Number of different towns in which houses were inspected	3	2.9	1.4	249
Number of dwelling units actually visited	9	21.6	30.5	252
Number of houses visited with intent of considering for purchase	4	4.9	3.3	249
Number of houses entered for inspection	8	12.8	12.0	256

Source: Donald J. Hempel, "Search Behavior," p. 243.

within the socioeconomic determinants of search. However, in light of the policy orientation of this report, it must be recognized that any governmental intervention must be to minimize search. Those who by choice extend their search endeavor must be encouraged to do so only by means of their own resources.

The third dimension of search behavior measures the intensity of dwelling unit examination. Four indexes measure behavior on this axis: One, the number of different towns in which houses were inspected; two, the number of dwelling units actually visited; three, the number of dwelling units visited with consideration of purchase; and four, the number of dwelling units entered for inspection only. Exhibit 3 displays this information.

It is found that 50 percent of the recent buyers inspected up to eight houses. However, they entered only up to four with the actual intent to purchase. The conclusion here is that there exists a conscious educational process on the part of this set of buyers. In a result similar to that obtained here, it is shown that the number of dwelling units actually visited prior to purchase is at most nine for 50 percent of the buyers. But the remaining 50 percent move the value up to 21.6. This evidence also emphasizes the existence of several sets of home buyers within Hempel's data set.

The previous section has described the search dimensions for the sample set taken as a whole. At several points of the analysis it was emphasized that several subpopulations may exist within the sample set; this was indicated by the fact that the mean and median scores were quite far apart. Further, as indicated by the standard deviation for each distribution, the variation in the value of the scores may be due to variation in one or more structural determinants of the search process. Specifically, the analysis to follow concentrates upon the socioeconomic characteristic of the recent home buyers. The technique used by Hempel to study the various possible determinants is first, the identification of the determinant; second, the construction of nominal or ordinal scales; third, the calculation of group means for each nonimal category or ordinal cell value; and fourth, the visual comparison of the group means. In essence these are analyses of variances without the use of significance tests.

The understanding of the socioeconomic determinants of search behavior is derivable from Hempel's summary indexes constructed for each search dimension. Each index is a linear sum of an ordinal value assigned to each behavioral measure: For example, a low value is assigned a number 1, an intermediate value is assigned a number 2, and a high value is assigned a number 3. Thus, a maximum of 12 and a minimum of 4 are obtainable on each summary index. The use of socioeconomic characteristics as structural determinants of consumer behavior is well-established in studies of consumer consumption function (Maisel & Winnick, pp. 359–435).

The paradigm most commonly used to describe the three socioeconomic structures of population groups is social area analysis (Shevky & Bell, pp. 226–235). In essence, three independent dimensions are hypothesized to exist within human populations; each of these dimensions explains certain types of human behavior. The explanatory model applied by Hempel fits into the social area paradigm. The model contains three indexes of social class—education, occupation, and income; and two dimensions of life cycle—age of husband and number of homes purchased. The third social area dimension is ethnicity. Apparently, the sample set constructed by Hempel did not permit his analysis of this dimension's impact upon search behavior. Fortunately, a recent Knoxville, Tenn., study will help shed some light on this structural determinant.

Social class is commonly described as the measure of perceived life style. The indexes commonly used to describe the presence of a social class factor are median education of the head of household, occupation of head, and family income. Income is the more complex index and therefore less revealing in that it is not only the temporal link between education and occupation but also indicates the seniority level of the worker. In addition to this, income can also indicate the presence of a working wife and the age of the chief wage earner. Empirical studies of the consumption function for housing have removed these confounding influences by arguing that the true income determinant is the normal, permanent, or expected income obtainable from a specific class of wage earners (Maisel & Winnick). However, in this study Hempel utilizes current measured family income.

Current or measured family income, roughly speaking, is an index both of an ability to pay and of the increased opportunity costs faced by personal search. As shown in Exhibit 4, the intensity of search behavior describes an inverted U-shaped curve when compared with increasing family income. Families in the lower income category obtain the longest time for search but are lowest in the intensity of information seeking and product examination. In contrast, families in the intermediate income ranges tie for the lowest duration of search but obtain high intensity search for information and product examination. Families in the high income class obtain the lowest on all three search indexes. On the surface, it may be said that if low income families made a more intensive search effort, their duration of search may be reduced to that found in the upper income levels. However, this ignores several factors. Based upon studies of the consumption function of housing, it is expected that higher income families will be spending more of their income on housing but in addition will be willing and capable of purchasing the time reducing middleman services. However, what these specific services may be and at what income or housing price level they may effectively mediate in the market is not known. Second, this analysis ignores the supply determinant of search behavior. The ability of the required types of dwelling units (in terms of prices, bedrooms, location, etc.) is not known from the Hempel study. Nor is the impact of these factors upon the search behavior for the different socioeconomic groups known.

Exhibit 4. The Average Score on Each Summary Search Index by Level of Annual Family Income

Income Level	Duration of Search	Intensity of Information Source Utilization	Intensity of Dwelling Unit Examination
Less than $10,000	8.3	7.5	7.6
$10,000-$14,999	7.6	8.1	8.0
$15,000 or more	7.6	7.7	7.6

Source: Donald J. Hempel, "Search Behavior," p. 245.

The effect of education on search behavior is displayed on Exhibit 5. It can be summarized by stating that the higher level of education corresponds with extensive search behavior, both in terms of information seeking and product examination. As a result, the period of search is shown to be reduced.

greater problem locating the right house. The data displayed on Exhibit 7 confirm this rationale.

Exhibit 5. The Average Score on Each Summary Search Index by Educational Level of Husband

Educational Level of Husband	Duration of Search	Intensity of Information Source Utilization	Intensity of Dwelling Unit Examination
High school graduate or less	8.1	7.4	7.4
Some college or tech. school	8.3	7.9	7.6
College graduate or more	7.4	8.0	8.2

Source: Donald J. Hempel, "Search Behavior," p. 245.

Occupation is partitioned into professional, managerial, and other groups. This is shown on Exhibit 6. The clearest finding is that managerial homebuyers are lower on all indexes. Although not explained by Hempel, it is expected that this refers to the force mobility of corporate managers and the corresponding housing aid they receive from their firms to minimize relocation problems.

Exhibit 6. The Average Score on Each Summary Search Index by Occupation of Husband

Occupation of Husband	Duration of Search	Intensity of Information Source Utilization	Intensity of Dwelling Unit Examination
Professional or technical	8.0	8.0	8.2
Managerial or administrative	7.6	7.6	7.7
Other	7.9	7.7	7.8

Source: Donald J. Hempel, "Search Behavior," p. 245.

The stage in the family life cycle has been found to affect significantly the consumption function for both durable and nondurable goods (Lansing and Kish, 1957). It is argued that younger families, due to their more severe budget constraints and requirements for a location adaptable to young children, will have a greater problem locating the right house. The data displayed on Exhibit 7 confirm this rationale.

Exhibit 7. The Average Score on Each Summary Search Index by Age of Husband and Number of Previous Moves

	Duration of Search	Intensity of Information Source Utilization	Intensity of Dwelling Unit Examination
Age of husband			
Under 35	8.0	8.0	8.1
35-44	8.0	7.6	7.6
45 or older	7.3	7.4	7.1
Number of homes purchased			
One (first home)	8.1	7.8	7.9
Two	8.0	8.1	7.8
Three or more	7.1	7.8	7.4

Source: Donald J. Hempel, "Search Behavior," p. 245.

However, life cycle as a determinant of search behavior is not a simple independent variable. Rather, several confounding influences serve to complicate its interpretation. First, young families associate highly with lower current income levels. Likewise, being young, they will have less experience in the search for housing. Each of these facts acts to bias upward each of the search dimensions.

On the other end of the life cycle dimension, the confounding influences act to reduce search behavior. Intrinsic to the over-45-years-of-age life cycle is the increasing absence of children and therefore the lessening of size and location requirements. However, in addition to this, many families will have experienced several housing hunts in the past with up to three or four moves in their background; thus, they will be more knowledgable of the problems to look for in the purchase of a house. Exhibit 7 also shows the impact of these factors. In addition to this consideration, this class of families will be at their upper income range and capable of purchasing the available middleman services. This should reduce the cost and effort expended as well as lower the duration of search.

Personal Motivation and Search: The attitudinal structure within the family, to the extent that it is independent of the preceding socioeconomic characteristics, is shown by Hempel to have an impact upon search behavior. Three propositions were designed to elicit responses

Exhibit 8. The Average Score on Each Summary Search Index for Various Attitudes toward Homeownership Held by Members of the Family

Operational Statement of Attitude	Duration of Search	Intensity of Source Utilization	Intensity of Dwelling Unit Examination
Children should not have to grow up in an apartment or rented house			
Attitude important to both	8.2	8.3	8.5
Attitude important to husband only	7.9	7.8	8.0
Attitude important to wife only	8.6	7.7	8.0
Attitude important to neither	7.2	7.6	7.8
Owning your home is a means of achieving personal satisfaction			
Attitude important to both	8.5	7.7	8.0
Attitude important to husband only	8.6	8.5	8.9
Attitude important to wife only	7.2	7.9	7.9
Attitude important to neither	7.2	7.6	7.9
Buying is less expensive than renting a residence of similar size			
Attitude important to both	7.6	7.7	7.7
Attitude important to husband only	8.1	8.4	8.5
Atitude important to wife only	8.3	8.1	8.8
Attitude important to neither	7.8	7.6	7.9

Source: Donald J. Hempel, "Search Behavior," p. 245.

testing the impact of favorable attitudes toward homeownership on the part of husband or wife, and both husband and wife upon the three summary indexes of search behavior. Exhibit 8 displays these results.

When the proposition is important to neither party, duration and intensity of search are relatively low. When questioned regarding aspects of owning the house independent of child-rearing purpose, the concern by one but not the other member maximizes the value of each of the three indexes. In terms of concern for a child-rearing environment a positive attitude by the husband greatly reduces the duration of search but does not affect the intensity of search. When both husband and wife are affirmative toward houseownership, both duration and intensity of search behavior are elevated. The exception to this occurs in the response to the assertion that buying is cheaper than renting. This serves to reduce all indexes.

Information and the Search Process: Information flow is essential for both the search for the correct buyer and the search for the correct seller. However, information flows are only made possible through the various housing-market institutions or structures. Included in this category are newspapers, realtors, and friends and associates. One or more of these elements of structure must act as agents to the principles of market agreement, in both formal and/or accidental ways.

Information Indexes: The analysis of the various channels of information in the context of questionnaire research is carried out by means of two indexes: the index of coverage and index of impact. The index of coverage is the percentage of respondents who use the specific information source sometime during the search period. The index of impact is the percentage of respondents who found their place of residence as a direct result of the information obtained through the specific information source.

Rossi's 1950 survey of recent movers provides the first empirical insights into these characteristics. Exhibit 9 reproduces a part of this work.

Exhibit 9. Measures of Utilization of Channels of Information in the Housing Market

Information Source	Index of Coverage	Index of Impact
Newspaper	63%	18%
Personal contact	62	47
Walking or riding around	57	19
Real estate agents	50	14
Windfall	31	25

Source: Rossi, Why Families Move, p. 161.

This shows that well over half of the recent movers referred at some point to the newspaper, personal contact, and actual search for "for sale" signs. At an even 50 percent were real es-

Exhibit 10. Relative Importance of Information Sources for Selected Decisions in the Home Buying Process

Decision for which Information was Obtained	Percent Exposed to Information Source and Index of Effectiveness							
	Friends & Business Associates	Relatives	Real Estate Agents	Bankers	Builders and Contractors	Newspapers	Other	N
Preferred neighborhood or location	54%[1]	19%	35%	8%	8%	30%	7%	244
	.66	.52	.33	.00	.21	.22	.00	
Price range to be considered	16%	11%	38%	34%	13%	30%	8%	240
	.41	.48	.43	.52	.42	.34	.33	
Which real estate agents to contact	51%	10%	3%	4%	3%	59%	3%	215
	.64	.57	.43	.38	.71	.65	.33	
Where to apply for a mortgage loan	33%	11%	.38%	27%	8%	3%	5%	236
	.66	.62	.69	.70	.90	.29	.67	
Which firm to contact for property insurance	44%	13%	.13%	6%	1%	3%	22%	232
	.87	.74	.10	.43	.67	.43	.90	

[1] Interpretation: The first number in each set indicates the proportion of respondents reporting that they referred to the information source in making the decision listed. The second number is an index measure representing the ratio of the number designating the source as that having the "most influence" for each decision to the total number referring to that source. For example, 54 percent of the respondents mentioned friends and business associates as sources of information they referred to in decision making concerning their preferred neighborhood or location; 66 percent of those using this source also designated it as the most influential source of information for this decision. The exposure percentages do not always total 100 percent because some respondents mentioned several sources or their own personal evaluations.

Source: Donald J. Hempel, p. 247.

tate agents and trailing behind were windfall accidents. The impact of each source varied considerably from that of coverage. Peronal contact was by far the most directly responsible channel for ultimate transactions. Following this is the presence of windfall accidents with real estate agents falling far behind with 14 percent.

Information Sources and the Consumer Decision Process. Hempel has extended this analysis by considering the steps in the decision process for which different types of information sources must be located by the prospective buyer. At least five decisions must be made by the buyer. Briefly these are:

- The neighborhood in which to search.
- Price range, for consideration of purchase.
- Real estate agent.
- The financing source.
- The insurance agent.

Exhibit 10 shows both the percentage of respondents who used a particular information channel to make one of their five decisions and the percentage of persons using the channel who thought it was the most important information source for the particular decision.

Hempel's research shows that friends and associates are most often consulted regarding a prospective residential neighborhood and are the most effective. Following this are real estate agents and newspapers. Locating a real estate agent is most often accomplished through the newspaper search, followed by inquiries among friends and associates. Information requisite to the procurement of financing most often comes from the realtor; however, friends and associates as well as bankers also provide inputs. More often than not, once a source is used for the purpose of locating a house, it is also used for procurement of financial information. In contrast to this, the search for the insurance agent is largely performed within the context of friends and associates.

The Socioeconomic Determinants of Information Source Utilization: Underlining these conditions is a set of socioeconomic characteristics that may direct individuals toward predictable information sources. However, the interpretation of Hempel's data is hindered by the inability to control for confounding influences. For example, the impact of education cannot be separated from that of age. That is, those with high school or less education have a high probability of being older than average for the population as a whole. Income suffers from a similar disability. However, since empirical research is severely limited; Hempel's data will again be utilized for this analysis.

As in the previous analysis of the socioeconomic determinants of the duration and intensity of search behavior, the social class, life cycle, and ethnical paradigm will again be utilized.

Exhibit 11. Relation Between Buyer Characteristic and Most Helpful Source of Information in Locating and Purchasing Home

	Percent Mentioning as "Most Helpful" Source of Information in Locating Home				Percent Mentioning as "Most Helpful" Source of Information in Arranging for Purchase of Home				
Buyer Characteristic	Friends Relatives Bus. Assoc.	Real Estate Agents	News-papers	Riding Around	Friends Relatives Bus. Assoc.	Real Estate Agents	Banks & Lending Insti-tutions	Builders and Con-tractors	N
Education of husband									
High school graduate or less	31%	29%	32%	6%	22%	44%	16%	7%	77
Some col. or techn. school	22	38	29	15	13	47	13	9	78
College graduate or more	15	53	23	10	7	53	14	10	120
Annual family income									
Less than $10,000	23	43	28	16	14	57	8	7	83
$10,000-$14,999	19	48	25	8	14	47	19	9	134
$15,000 or more	26	26	34	9	4	43	11	13	53
Occupation of husband									
Professional or technical	18	39	33	11	12	50	12	11	94
Managerial or administrative	23	43	25	9	18	41	16	14	56
Other	24	44	25	11	10	52	16	7	122
Age of husband									
Under 35	19	45	31	9	12	46	13	10	156
35-44	19	41	25	12	14	44	16	12	73
45 or older	33	33	22	13	9	44	16	9	45
Number of homes purchased									
One (first home)	20	44	27	11	12	54	11	8	142
Two	27	37	30	15	13	49	14	17	71
Three or more	18	39	32	3	5	42	18	8	38

Source: Donald J. Hempel, "Search Behavior," p. 248.

Social Class: The social class determinants are once more education, occupation, and income. The impact of an increase in the husband's educational level on the selection of information sources is to increase the importance of the real estate agent in the purchase and location of a home. In terms of husband's occupational level, managers and administrative personnel rely most heavily upon real estate agents for the location of the home. However, purchase arrangements are more likely to be made with friends or associates or the bank. In contrast, professionals rely upon both real estate agents and newspapers for the location of their home; however, the real estate agent is used most often in arranging purchase of the house.

Family income operates in three different ways depending upon the level of income. Families with an annual income less than $10,000 are more reliant upon friends, et al., newspapers, and personal inspection for the location of the house than are families in the $10,000–$15,000 bracket. However, for help in purchasing the house, dependence is highest upon real estate agents. Families with incomes greater than $15,000 annually do not concentrate their information sources for either home location or purchase to the same extent that occur in low income brackets; that is, with higher income there comes a flexibility in the use of the various market information sources.

Life Cycle: The increase in the age of the husband reflects both a gradual lifting in the family budget constraint and the experience acquired from previous moves as well as its usual life cycle connotation. Increasing age acts to lessen the impact of the use of real estate agents in both the location and the purchase of the house. This information is summarized on Exhibit 11.

Ethnicity: Neither search behavior nor use of information sources by ethnicity was included in Hempel's study. And in spite of the widespread concern for racially segregated housing patterns, relatively little research has been reported involving ethnicity and the search for housing. An opening has recently been made through a case study of a southern city.

In a questionnaire-based study of housing costs and race in Knoxville, Tenn. (Neufeld and Kenney, 1971), the distribution by race of the most important information sources for the location of the respondent's present home has been constructed. This information is displayed on Exhibit 12.

Exhibit 12. The Percentage of Respondents Within Each Racial Category Answering the Question: "Which of the Following Did You Most Use in Helping You Find Your Present Home? One Only." By Type of Information Channel Used

Information Channel	Negro	White
Newspaper ads	10.9	28.2
Driving around to see what was available	31.9	29.5
Information from relatives or friends	33.6	24.8
Real estate agents (owners only)	16.0	10.7
Rental agents (renters only)	4.2	0.7
Old landlord (renters only)	3.4	6.0

Source: J. L. Neufeld and K. B. Kenney, "The Lack of Relation Between Race and Housing Costs: A Case Study of Knoxville, Tennessee," Civil Defense Research Project, Oak Ridge National Laboratory, 1971, pp. A-8 and B-4.

The sample consists of 137 Negro respondents and 156 white. In terms of income, both subsets were evenly matched. However, white families had, on the average, a slightly higher average family size.

Based upon this sample, it is argued that black and white families exhibit essentially different search behavior in terms of information sources. The information source most significantly influenced by racial groupings was the use of the newspaper. White families indicate that the newspapers were most important 28 percent of the time, whereas black families indicate this only 11 percent of the time. As a consequence of this, blacks utilize to a greater extent both word of mouth and personal inspection. Lastly, but of minimal importance, is the utilization of real estate agents and rental agents; in both cases black families relied more heavily upon the agency of middlemen than whites.

Not having alternative case studies by which to compare this finding, the increased use of structural middlemen by black searchers must be thought of as quite possibly a property of the Neufeld and Kenney sample set. However, it is quite reasonable to argue that racial barriers are a root cause of the added reliance upon personal as opposed to mass media search techniques by black buyers.

The Search Process and the Housing Consumption Function

To the extent that this is the case, the search process adds an additional cost onto the price of the housing unit transaction. Since the cost of housing to a certain extent determines the quantity of housing bought, the added price for search by black over white families theoretically alters the quantity of housing capable of being consumed by black Americans.

Thus, the analysis of the search process leads back to the study of the housing consumption function. Aggregate studies of black versus white have found that: "Negro families spent less on housing in 1950 than white families of the same size and with the same measured income." (Maisel and Winnick, 1960, p. 381.) Kain and Quigley's study of the probability of homeownership on the part of St. Louis black and white families shows that after other socioeconomic considerations as well as prior tenure are held constant, black families are still less likely to be homeowners.

Neither of these studies explicitly considers the cost of search. However, as shown by Mincer (1963, pp. 67–69) the opportunity cost of time (the increased personal search by black families over whites) biases the income parameter upward. Therefore it would appear that separate housing consumption functions must be constructed for each racial group.

Kain and Quigley recognize that psychic costs involved in the search process might well be more significant than out-of-pocket costs for the explanation of the black family's housing consumption. However, when the dependent variable is the probability of homeownership, stratification by race does not significantly alter the previous conclusion (Kain & Quigley, 1972, p. 209).

In an alternative approach to the study of the outcome of the search process for black families, Chester Rapkin finds that the percentage of families living in substandard dwellings decreases with monthly rental for both white and black families. However, an increase in monthly rentals reduces the presence of the whites in substandard dwelling units to minimal numbers; whereas the decrease in the percentage of substandard dwellings occupied by black families under similar rental increases remains relatively low (Rapkin, 1966, p. 242). It is, therefore, concluded that the result of the search process for black families is significantly different than it is for whites. The environment places a different set of structural determinants to the search process upon the black families.

Therefore, although the use of a racial specific equation to explain housing ownership was not required in the Kain-Quigley analysis, studies investigating the quantity of housing consumed may find it beneficial to construct separate consumption functions for each racial category.

Information Sources and the Low to Moderate Income Housing Market

Further insights into the effectiveness of the various information sources can be gained from an analysis of the search process vis-a-vis recently rehabilitated housing. In 1972 a study was made to determine the effectiveness of the Camden, N.J., Housing Improvement Projects (CHIP).

Camden, as with many older cities, has experienced extensive demolition and deterioration of its housing stock. Between 1950 and 1967, 2,217 units had been destroyed, leaving approximately 37,000 dwelling units standing at the end of that time period. However, it is estimated that due to demographic shifts, an additional 6,000 dwelling units should be added to the housing stock. This is needed in order to satisfy both new household formation and the inevitable decay and demolition of the older stock (Listokin, p. 111). The result has been a severe housing shortage impinging specifically upon low and moderate income families.

Within this context, CHIP has inserted its rehabilitated units. As of May 1972, CHIP had rehabilitated over 400 dwelling units. Marketing techniques are relatively simple: open houses are held in various neighborhoods and brochures are distributed both at the open houses and at community centers catering to the target population (Listokin, p. 137). In terms of the number of successful transactions, these marketing devices appear to be unnecessary. The successful application for a CHIP house depends mainly upon the recommendation passed to the searcher by a present CHIP homeowner. Exhibits 13 and 14 display this finding. This is clearly shown from the question, "If you found out about CHIP from friends or relatives, are they CHIP homeowners?" Respondents who have been CHIP owners for more than 2 years are evenly split on this question. More recent owners relied on previous CHIP owners fully 64 percent of the time. Therefore, in conclusion, successful homeownership within the context of a tight housing market depends to a large extent upon the good fortune on the part of the applicant in having someone in a position to provide specific housing information.

Exhibit 13. How Did You Find Out About CHIP?

Response	CHIP Homeowner for less than 2 Years Percent	CHIP Homeowner for over 2 Years Percent
Relative	15.0	10.4
Friend	46.2	43.8
Newspaper	5.0	8.3
Radio	—	1.0
Welfare department	11.2	11.5
Office of Economic Opportunity	2.5	—
CHIP employee	8.7	13.5
Other	8.1	11.5
No response/Don't know	3.1	—
Total	99.8	100.0

Source: David Listokin, *The Dynamics of Housing Rehabilitation: Macro and Micro Analyses* (CUPR, 1973, p. 138).

Exhibit 14. If You Found Out About CHIP From Friends or Relatives, Are They CHIP Homeowners?

Response	CHIP Homeowner for less than 2 years Percent	CHIP Homeowner for over 2 Years Percent
Yes	64.3	51.9
No	34.7	46.2
No response/Don't know	1.0	1.9
Total	100.0	100.0

Source: David Listokin, *Housing Rehabilitation*, p. 139.

Information Sources, the Search Process, and Welfare

The search for housing takes on its more severe personal aspects for those families that are under the poverty level. Extensive information is now available identifying the housing search process incurred by poverty families who are enrolled in one of four welfare programs. The study centers on New York City as of 1970. Four categories of welfare families are investigated: home relief, old age assistance, aid to disabled, and aid to families who have dependent children (AFDC).

Existing housing patterns find that home relief and aid to dependent children families mainly occupy apartments in the private sector, and old age and aid to dependent children families are the most frequent residents found in public housing. The growth of welfare occupancy during the period 1968–1970 shows that the search for housing has been fruitful for the most part only in developments already obtaining extensive welfare occupancy. This is producing what has been termed welfare structures.

The problem evidenced in the search for housing is shown by the fact that one of five families sampled require accommodations for six or more persons. When asked, "How did you find your apartment?" the dominant response by all types of welfare families was that word of mouth by relative or friend directed them to the successful conclusion of the quest for housing. Exhibit 15 shows these results. Public agencies such as public housing, welfare, and relocation services account for a modest 10 to 15 percent of the successful conclusions to the search process. Ethnicity also enters the search pattern for welfare families. Although white and black families are equal in their use of brokers and word-of-mouth information channels, close to 20 percent of the black families responded that information from various public agencies did help them to find their present housing. This is close to double that found in white and Spanish-speaking respondents.

When asked, "In searching for housing, were you always treated fairly?" only in the case of families receiving aid for dependent children did a large number of welfare recipients say no. (See Exhibit 16.) This occurred more than 25 percent of the time. More often the reason for this treatment was thought to be the result of their welfare status (40 percent). Twenty-seven percent felt that racial discrimination was the cause.

In addition to the dual problems involved in finding an acceptable dwelling and a willing landlord, other factors impact on the operation of the search process for welfare families. As an example of this, most landlords (75 percent) require a security deposit: this factor weighs far more heavily on AFDC families than on others. Similarly, most welfare recipients pay deposits for their utilities—gas, electricity, telephone, etc.

Exhibit 15. The Percentage Distribution of Answers by Welfare Families to the Question: "How Did You Find This Apartment?" by Category of Welfare, New York City, 1970

"How did you fiind this apartment?"	Category of Welfare: Home Relief	Old Age Assistance	Aid to Disabled*	Aid to Dependent Children	Total
Broker	13.3%	1.8%	17.5%	11.6%	11.4%
Newspaper	4.0	3.6	0.0	4.9	3.9
Relative or Friend	54.7	54.5	45.6	44.4	47.8
Sign on Premises	6.7	9.1	7.0	6.7	7.0
Applied to Public Housing	5.3	5.5	5.3	8.0	6.8
Through Welfare	4.0	3.6	3.5	4.0	3.9
Relocation	4.0	3.6	1.8	3.6	3.4
Other	6.7	16.4	17.5	15.6	14.3
NA/DK	1.3	1.8	1.8	1.3	1.5
Total	100.0%	1 00.0%	100.0%	100.0%	100.0%

* Includes Aid to the Blind and Veterans' Assistance

Source: George S. Sternlieb and Bernard P. Indik, *The Ecology of Welfare* (New Brunswick: Transaction, 1973).

In light of the problems faced by welfare recipients within the search process, the respondents were asked if the welfare department aided in the search for housing. Twenty-six and one-half percent of the sample said that it had; it must be recognized, however, that 16 percent of the sample was not on welfare at the time of their housing search. Of the 87 percent of the AFDC group that looked for housing while they were on welfare, nearly a third (32.4 percent) indicated they received aid from the department. This is shown in Exhibit 17. It was further found that Spanish-speaking families received aid with greater frequency (25 percent) than either black (14 percent) or white (10 percent) welfare recipients.

The type of assistance most often provided by the department is financial. This aid covers charges such as landlord deposits and first rents. Thus the most difficult and time-consuming

Exhibit 16. The Percentage Distribution of Answers by Welfare Families to the Question: "In Searching for Housing, Were You Always Treated Fairly?" by Category of Welfare, New York City, 1970

	Category of Welfare				
Treated Fairly	Home Relief	Old Age Assist-ance	Aid to Dis-abled*	Aid to De-pend-ent Chil-dren	Total
Yes	84.0%	92.7%	87.7%	73.8%	80.1%
No	16.0	7.3	12.3	26.2	19.9
Total	100.0%	100.0%	100.0%	100.0%	100.0%

* Includes Aid to the Blind and Veterans' Assistance

Source: George S. Sternlieb and Bernard P. Indik, *The Ecology of Welfare*, 1973.

part of the search process is for the most part left to the initiation of the welfare recipients, in that these families are for the most part extremely vulnerable to the demands of the landlord. The development of a tenant referral service may produce a more satisfactory solution to the search process as well as a better landlord-tenant relationship at the lower end of the rental spectrum. However, in light of the scarcity of adequate housing, this may force marginal income nonwelfare searchers into rental levels that may well require them to move on to welfare.

The preceding section has identified the existence and use by housing searchers of information sources. Ideally, each of the information sources should, in turn, be analyzed from both a functional and behavioral point of view vis-a-vis search. In no case can this be done. Only in the case of the real estate broker can fragments of evidence be acknowledged.

From the perspective of many homebuyers, the real estate agent has not been considered the most important market information source. However, he is the institutionalized and licensed middleman designated to bring together the buyer and the seller. To improve this system and to increase the rate of the transactions, multiple listing services (MLS) have been developed. In New Jersey, a multiple listing service is chartered as a nonprofit organization by a local real estate board. Although MLS's are widely utilized empirical research identifying the structural characteristics of the MLS as well as their operating procedures is singularly absent. Thus the analysis of MLS vis-a-vis the search process is necessarily fragmentary. Ideally the function of the MLS should be to maximize the number of transfers and thereby minimize the duration of the search process. Although this may be the case for some sectors of the housing market, persistent commentary by critics indicates the presence of exclusionary listing services.

Exclusive MLS's may develop in two ways: First, by limiting the number of members in the local MLS, and second, by selective placement of listing on the MLS. The latter has not been substantiated by empirical evidence. Rather it is an indictment commonly found in popular criticisms of this establishment. More readily available is information regarding the first exclusionary device. The limitation of membership in the MLS has been attacked by the courts as being an unlawful restraint of trade (*Grillo* v. *Board Realtors of Plainfield Area* 91 N.J. 205).

In the 1966 New Jersey case, the operation of the MLS by a local real estate board to the exclusion of nonboard members was ruled un-

Exhibit 17. The Percentage Distribution of Answers by Welfare Families to the Question: "Did You Receive Any Assistance from the Welfare Department in your Search for Apartment?" by Category of Welfare, New York City, 1970

	Category of Welfare				
Received Assistance	Home Relief	Old Age Assist-ance	Aid to Dis-abled*	Aid to Dependent Children	Total
Yes	17.3%	20.0%	21.1%	32.4%	26.5%
No	64.8	58.2	61.4	54.2	57.5
Not on Welfare	18.7	21.8	17.5	13.3	16.0
Total	100.0%	100.0%	100.0%	100.0%	100.0%

* Includes Aid to the Blind and Veterans' Assistance

Source: George S. Sternlieb and Bernard P. Indik, *The Ecology of Welfare, 1973.*

constitutional. Before that time membership was acquired only after a difficult testing period—that is, the applicant had to operate within the board's region for a year prior to application. Further, he had to have three board members as references and a $1,000 initiation fee. *Grillo* was recently upheld in a case involving the admittance of a black realtor to the MLS. (*Oates* v. *Eastern Bergen Co. Multiple Listings Services Corp.* (113, N.J. Super 371), 1971).

Since that time, membership requirements have been relaxed and broad use of the MLS by regional brokers is permitted. However, a potential source of exclusion does appear on the horizon. There is presently a move by several members of the Eastern Bergen County, N.J., MLS to remove an area under their immediate interest from the Eastern Bergen MLS and incorporate a new MLS. Thus, just as in the delimitation of school district lines, gerrymandering local real estate board lines will continue the existence of racially exclusive residential patterns (Jobs and Housing, 1970, pp. 70–71).

Efforts to Aid the Search for Housing

The preceding sections have identified the search behavior of the buyer as well as the market structures used by him in the acquisition of housing. It has been documented that several subgroups of searchers have more difficulty within the search process than others; therefore, this concluding section studies several formal and informal programs that have been designed to aid persons in their housing search problems Two sections follow: The first describes the housing problem faced by employees of recently relocated firms to suburban areas and the second describes the efforts of the State of New Jersey through its division of civil rights to overcome discrimination in housing.

To what extent does the private sector aid employees in their search for housing? A recent study conducted by the Rutgers Center* questioned 739 firms in northern New Jersey regarding housing problems of their employees. Firms were chosen only if they had recently moved into one of the newly developed suburban communities. Thus, employment problems brought about by deficiencies in the housing market should be clearly evident to them.

When asked the question regarding their firm's awareness of housing conditions in their new location, 85 percent of the firms indicated that no consideration was made regarding the housing market faced by their employees. Exhibit 18 displays these results. However, the two groups of firms, raw resource refining and machinery, that were most concerned with the housing market prior to moving identified themselves as two of the three sectors with the most hiring problems resulting from the housing shortage. Exhibit 19 displays these results.

Exhibit 18. The Percentage of Firms in Each Reporting Classification Answering the Question: "Did You Consider Potential Worker Housing Deficiencies at the Time of Initial Location to Area?" By Type of Response.

Industrial Classification *	Response Yes	No	Total
Soft Goods	8.4	91.6	100
Hard Goods	16.1	83.9	100
Raw Resource Refining	20.7	79.3	100
Metallurgy	7.0	93.0	100
Machinery	27.3	72.7	100
Miscellaneous	18.2	81.8	100
Business and Education	0.0	100.0	100
All firms	15.5	84.5	100

* Appendix contains the component industries within each major industrial classification.

Source: "Employer Survey of the Mahwah Primary Housing Region," Center for Urban Policy Research, Spring 1973.

When asked about the housing market within their new municipality, significant numbers (52 percent) of the firms in each sector registered a recognition of a housing shortage in their new location. (See Exhibit 20.) The shortage is perceived to exist in both the homeowner and rental markets. The price range most often cited as requiring additional housing ranged from $17,500 to $29,000. When asked about the most needed rental range, the values ranged from $100 to $174 per month rentals. These data are displayed on Exhibits 20 and 21.

The following analysis shows the awareness on the part of the respondent firms of housing shortages. The next series of questions identifies the types of problems faced by the recently relocated firms vis-a-vis the housing market.

Compared to their previous location, 41 percent of the firms indicated that their level of difficulty in finding production workers was about the same. About 34 percent indicated that it was greater. Firms requiring clerical and executive help have for the most part benefited from their move. Only 12 percent indicate a greater level of difficulty in finding these types of employees. Exhibits 22, 23, and 24 show these results.

* Rutgers Center for Urban Policy Research, *After Zoning*, study presently in progress.

Exhibit 19. The Percentage of Firms in Each Reporting Classification Answering the Question: "Are There Currently Any Housing Deficiencies in the Town of Your Firm's Location Which Would Inhibit Your Future Hiring Plans?" by Type of Response.

Industrial Classification	Response Yes	No	Total
Soft Goods	19.5	80.5	100
Hard Goods	17.8	82.2	100
Raw resource refining	24.6	75.4	100
Metallurgy	12.7	87.3	100
Machinery	20.1	79.9	100
Miscellaneous	17.8	82.2	100
Business and Education	34.3	65.7	100
All firms	19.3	80.7	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 20. The Percentage of Firms in Each Reporting Classification Answering the Question: "Do You Think There is Currently a Shortage of Housing in the Town of Your Firm's Location?" by Type of Response.

Industrial Classification	Response Yes	No	Total
Soft Goods	42.9	57.1	100
Hard Goods	54.0	46.0	100
Raw Resource Refining	66.9	33.1	100
Metallurgy	44.0	56.0	100
Machinery	65.0	35.0	100
Miscellaneous	28.4	71.6	100
Business and Education	24.5	75.5	100
All firms	52.1	47.9	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 20a. The Percentage of Firms in Each Reporting Classification Answering the Question: "If You Think There is a Current Shortage of Housing in the Town of Your Firm's Location, in What Rental Price Range Does it Exist?" by Type Response.

Industrial Classification	Monthly Rental Range of Housing Shortage: Under $100	$100 to $135	$136 to $174	$175 to $249	$250 to $399	No Response
Soft Goods	7.0	34.5	22.0	8.9	0.0	27.6
Hard Goods	3.9	15.9	11.5	35.4	0.0	33.2
Raw Resource Refining	0.0	31.4	31.1	3.2	0.0	34.3
Metallurgy	0.0	25.6	25.0	0.0	0.0	49.4
Machinery	0.0	13.9	23.8	9.5	2.5	50.3
Miscellaneous	0.0	16.9	64.0	0.0	0.0	19.1
All firms	2.7	24.8	23.9	10.9	0.6	37.2

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 21. The Percentage of Firms in Each Reporting Classification Answering the Question: "If You Do Think There is a Current Shortage of Housing in the Town of Your Firm's Location, in What Purchase Price Range Does it Exist?" by Type of Response.

Industrial Classification	Purchase Price Range of Housing Shortage: Under to $12,000	$12,000 to $14,999	$15,000 to $17,499	$17,500 to $24,999	$25,000 to $29,999	$30,000 to $49,999	No Response	Total
Soft Goods	0.0	0.0	0.0	50.7	14.0	2.5	32.7	100
Hard Goods	0.0	0.0	14.9	18.7	41.6	0.0	24.8	100
Raw Resource Refining	0.0	10.6	3.5	25.3	29.9	3.1	27.6	100
Metallurgy	6.3	15.2	0.0	31.3	18.2	0.0	29.0	100
Machinery	0.0	4.6	0.0	23.8	12.6	6.6	52.4	100
Miscellaneous	0.0	0.0	0.0	21.7	54.8	0.0	23.5	100
Business and Education	0.0	0.0	0.0	0.0	0.0	100.0	0.0	100
All firms	0.6	4.8	3.3	30.0	22.9	3.5	34.8	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 22. The Percentage of Firms in Each Reporting Classification Answering the Question, "How Would You Rate the Work Force in the Area Compared to Your Previous Location for Executive Workers?"

Industrial Classification	Easier to Hire	More Difficult to Hire	About the Same	Total
Soft Goods	29.9	11.5	58.6	100
Hard Goods	40.2	9.6	50.2	100
Raw Resource Refining	10.3	9.6	80.1	100
Metallurgy	46.1	2.7	51.2	100
Machinery	24.5	24.8	50.7	100
Miscellaneous	26.7	0.0	73.3	100
Business and Education	39.3	19.7	41.0	100
All Firms	29.8	11.1	59.1	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 23. The Percentage of Firms in Each Reporting Classification Answering the Question, "How Would You Rate the Work Force in This Area Compared to Your Previous Location for Clerical Workers?"

Industrial Classification	Easier to Hire	More Difficult to Hire	About the Same	Total
Soft Goods	41.1	10.1	48.8	100
Hard Goods	61.8	2.1	36.1	100
Raw Resource Refining	17.7	4.1	78.1	100
Metallurgy	55.4	13.8	30.8	100
Machinery	26.3	25.3	48.3	100
Miscellaneous	5.1	20.5	74.3	100
Business and Education	39.3	19.7	41.0	100
All Firms	38.0	11.9	50.1	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

As a further indication of the severity of this problem, the firms were asked if there was a problem of absenteeism within the technical, clerical, or production employment force. If such a problem exists, the reason from the firm's point of view was elicited. Absenteeism among technicians and clerical workers was largely absent or unrelated to the issue at hand. Among production workers the problem appears to be of concern. Nearly fifty percent of the firms indicated the existence of a problem. However, as Exhibit 25 shows, most of the problem is perceived to be poor work habits. Only 10 percent of the firms viewed the length of journey to work as a possible problem.

Exhibit 24. The Percentage of Firms in Each Reporting Classification Answering the Question, "How Would You Rate the Work Force in this Area Compared to Your Previous Location for Production Workers?"

Industrial Classification	Easier to Hire	More Difficult to Hire	About the Same	Total
Soft Goods	48.5	20.2	31.3	100
Hard Goods	25.3	35.3	39.4	100
Raw Resource Refining	10.5	23.2	66.3	100
Metallurgy	32.4	45.9	21.7	100
Machinery	24.0	36.7	39.2	100
Miscellaneous	6.8	45.9	47.3	100
Business and Education	32.4	32.4	35.2	100
All Firms	25.8	33.7	40.5	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 25. The Percentage of Firms in Each Reporting Classification Answering the Question "If Absenteeism is a Serious Problem at this Location, Why?" by Type of Response.

Industrial Classification	Work Habits	Reason for Length of Work Trip	Production Illness	Worker Weather	Absenteeism Other	Total
Soft Goods	41.0	6.8	19.7	0.0	32.6	100
Hard Goods	81.0	0.0	3.7	0.0	15.3	100
Raw Resource Refining	59.9	0.0	10.0	2.1	28.1	100
Metallurgy	38.2	32.7	9.3	0.0	19.8	100
Machinery	65.0	2.3	27.4	0.0	5.3	100
Miscellaneous	86.9	0.0	13.1	0.0	0.0	100
Business and Education	48.0	52.0	0.0	0.0	0.0	100
All Firms	54.2	9.0	15.0	0.4	21.4	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

It is not surprising, therefore, that housing assistance is provided by only 29 percent of the firms interviewed. As Exhibit 26 shows, most of the aid is provided by the firms in the machinery industry, with the soft goods industry a distant second.

Exhibit 26. The Percentage of Firms in Each Reporting Classification Answering the Question: "Does the Firm Make Any Arrangements to Assist Newly Hired Employees to Find or Buy Housing?" By Type of Response.

Industrial Classification	Response Yes	No	Total
Soft Goods	22.1	77.9	100
Hard Goods	22.1	77.9	100
Raw Resource Refining	29.3	70.7	100
Metallurgy	21.3	78.7	100
Machinery	37.2	62.8	100
Miscellaneous	75.9	24.1	100
Business and Education	43.5	56.5	100
All Firms	29.3	70.7	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

In order to grasp the magnitude of housing aid provided by each sector, the employment distribution must be known. The hypothesis is that sectors rich in executive employment will be most apt to provide housing aid.

Exhibit 27 displays the employment composition within each of the seven industrial classes. Each value is the median percentage of workers of a particular job classification. Machinery and soft goods production industries represent the two extremes in employment specialization. (The business and education industry includes nine firms and employs fewer than 2,000 employees, whereas the machinery sector has over 12,000 employees and soft goods production, 9,000. Therefore, the machinery sector is used as most representative of worker specialization).

Exhibit 27. The Median Percentage of Each Type of Worker Employed Within Each Industrial Classification

Industrial Classification	Type of Worker: Executive	Clerical	Production
Soft Goods	9	7	81
Hard Goods	12	12	72
Raw Resource Refining	11	10	75
Metallurgy	15	11	72
Machinery	19	15	60
Miscellaneous	15	26	46
Business and Education	28	60	4

Source: "Employer Survey," Center for Urban Policy Research, 1973.

With a median of 81 percent production workers per plant, the soft goods production industry displays the greatest dependence upon the blue collar worker. On the other side, the machinery sector shows the second highest dependence upon executive staff. Clerical workers are most strongly associated with business and educational industries obtaining a median of 60 percent of the firms's labor force.

In spite of the spread in employment specialization, housing assistance is strongly limited to one employment group, the executive staff. While only 29 percent of all firms provide any housing assistance, 83 percent of these firms provide it only for executives and 12 percent offer assistance to production workers. Exhibit 28 displays these results.

In addition, Exhibit 28 shows that with employee specialization, there is increased assistance in the procurement of housing. Twenty-one percent of the soft goods manufacturing firms that offer housing assistance do so for production workers. In contrast, firms in the machinery and instruments industry offer no housing assistance to their production employees. The highest level of assistance to production workers comes from the firms in the miscellaneous sector (19 percent). Only 5 percent of the soft goods production firms offer housing assistance.

Housing assistance takes the following forms: relocation money, housing loans for downpayment, mortgage guarantees, information on specific dwelling units, and assistance to local builders. Firms that provide housing assistance ranked the type of assistance as of primary or secondary importance. As Exhibit 29 shows, 55 percent of the firms grant relocation money while 33 percent primarily grant housing information. Fifty-eight percent of the firms provide housing information and 28 percent provide housing loan downpayments (both services are ranked as secondary in importance). Unfortunately the affirmative response to the information form of housing assistance indicates neither the quality of information nor the effectiveness, vis-a-vis the occupational groups.

Efforts of State Government

State government efforts to improve the search for housing have taken several forms. Financing procured through the department of community affairs has permitted the construction of low and moderate income developments, thus allowing more successful termination to the housing search for some families.

Exhibit 28. The Percentage of Firms in Each Reporting Classification Answering The Question: "Who are the Most Frequent Recipients of Housing Assistance?" by Type of Response.

Industrial Classification	Executive	Clerical	Production	No Response	Total
Soft Goods	75.8	0.0	20.6	3.7	100
Hard Goods	81.3	0.0	14.4	4.3	100
Raw Resource Refining	92.5	0.0	7.5	0.0	100
Metallurgy	68.7	5.9	20.1	5.4	100
Machinery	92.9	2.3	0.0	4.8	100
Miscellaneous	75.2	0.0	24.8	0.0	100
Business and Education	100.0	0.0	0.0	0.0	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

Exhibit 29. The Percentage of Firms in Each Reporting Classification Answering the Question: "If You Do Offer Housing Aid What Types of Primary Assistance Do You Offer?"

Industrial Classification	Relocation Money	Loan for Down Payment	Mortgage Guarantee	Information on Available Housing	Other	Total
Soft Goods	46.7	3.9	0.0	31.8	17.7	100
Hard Goods	47.5	4.5	9.7	33.4	4.9	100
Raw Resource Refining	70.8	0.0	0.0	21.2	8.0	100
Metallurgy	35.3	5.7	0.0	59.0	0.0	100
Machinery	75.6	0.0	0.0	24.4	0.0	100
Miscellaneous	30.6	0.0	24.8	44.7	0.0	100
Business and Education	67.6	0.0	0.0	32.4	0.0	100
All Firms	55.3	1.9	4.6	33.0	5.1	100

Source: "Employer Survey," Center for Urban Policy Research, 1973.

A more direct stance is being pursued by the division of civil rights of New Jersey. In response to current demands for open housing for all racial groups, the division has instituted court action on specific discrimination complaints and is now developing a framework for a broader attack upon this problem.

In a recent decision, the New Jersey Supreme Court has upheld a two-pronged attack upon discrimination. In *Jackson* v. *Concord Co.* (54 N.J. 115) the plaintiff, a Negro, attempted to secure an apartment within the Concord apartment complex. Having been thwarted in these attempts, Jackson, with the help of the division, took the development to court and asked for injunctive relief and damages. In its referral to the New Jersey Supreme Court, the court upheld a lower court ruling enjoining the Concord owners from further discrimination in renting apartments to blacks; in addition, it asserted the right of the N.J. division of civil rights to order reimbursement for out-of-pocket costs suffered by the aggrieved individual in the housing accommodation case.

The court's decision is essential to the implementation of the Federal civil rights law. Without it, persons operating with a tight budget constraint were easily dissuaded from taking their complaint to the courts. With it, landlords know that overt discriminatory action on their part will be unsuccessful if taken to court and that a payment will be required to be made to the aggrieved individual.

The successful attack upon overt housing discrimination practices has forced these practices into more subtle forms.

Recent testimony by Kay Potter of the Fair Housing Council of Bergen County, N.J., indicates the new direction of this thrust.

> Techniques of discrimination are becoming increasingly subtle and we have sensed over the last year an increasing tendency for apartment owners to hide behind brokers instead of advertising directly. This impression was confirmed recently by a white apartment seeker who was told by a broker that a large apartment development in Ridgefield no longer advertised directly but depended upon the broker to screen out Negro applicants as the Ridgefield development did not allow Negroes. (Appendix N, Edited Transcript of the Hearing on the proposed Multiple Dwelling Rule enforc-

ing Fair Housing Laws; *Apartments in White Suburbia*, A Report by the Administrative Process Project, Rutgers Law School, Newark, N.J., p. 186.)

Recognition of the more subtle forms of discrimination in the search process is brought out in the recent brief for *Civil Rights Division in Blair* v. *Knoll Manor, et al.* This action involves 18 of 22 multiple housing developments in Parsippany Troy Hills, N.J. Of the 5,684 dwelling units involved, only 35 are occupied by black families. In this case, effective search is initiated by the landlord group; "respondents rely upon signs on the premises and word-of-mouth referrals by present tenants as their method of recruiting tenants" *(Apartments in White Suburbia*, p. 240).

The processing of referrals also inhibits search. The lack of waiting lists discriminates against minority persons because, "they are more likely not to pursue housing in a white neighborhood after a first rebuff than are whites" (Ibid., p. 241). Similarly, the building superintendent sets the minimum income requirements for entrance and evaluates the outcome of credit checks. Often income earned by wives is excluded from the family income for purposes of evaluating an application.

The Landlord Reporting Rule

The measures used to thwart the obstruction of the search process have taken the form of individual actions. These have been effective from the point of view of establishing legal precedent. However, the broad-range impact is missing. As a means of advancing beyond the case-by-case attack on discrimination in the search process, the N.J. division of civil rights in 1970 proposed in an administrative rule requiring owners of multiple apartment developments of 25 units or more to report annually to the division the following information:

- Racial designation of applicants for apartment rental.
- Racial designation of apartment leaseholders.
- Apartment rental turnovers.
- Apartment rental recruiting techniques.
- Rental rates and apartment sizes.
- Such other information as the State attorney general determines is necessary to perpetuate the purposes of this rule (Ibid., p. 120).

The purpose of this rule is adequately summarized by Justice Mountain in his recent decision upholding the rule:

> As the testimony at the hearing made clear, it was the hope and the expectation that the statistical data derived from the reports of property owners would serve to identify particular instances of housing discrimination and that where pronounced patterns of racial balance emerged, these might offer appropriate targets for investigation and such action as might then be indicated. (*N.J. Builders, Owners, and Managers Association* v. *Blair* 60 N.J. 335.)

The essence of the search process is the manipulation of information by the principals in the housing market. Interference with the flow of information necessitates the creation of new information channels. The reporting rule is not a direct aid to the searcher; however, it presents the designated State agency with information on rental turnover, landlord search procedure, minority group occupation, and occupancy ratios to use in developing administrative remedies.

To insure a direct impact upon the search process, the N.J. division of civil rights is further proposing a tenant referral system. As proposed, the landlord must notify a specified group of open housing organizations of all units owned or operated by the landlord, as well as a description of each unit presently available or due to become available for rental within the next three months. The civil rights division will receive quarterly reports, thereafter including all rejected minority group applicants, the reason for the rejections, and all new minority group tenants (Appendix Z, Tenant Referral System, Enforcing Fair Housing Laws, p. 382, ibid.)

The need for such action can be clearly seen within the context of *Blair* v. *Knoll Manor et al.*

The Parsippany Troy Hills action offers the unique opportunity to analyze the obstructions placed within the search process. Parsippany Troy Hills, a municipality in Morris County, N.J., is approximately 15 miles and 35 minutes by car from Newark. Newark, as well as other older cities within the same radius from Parsippany Troy Hills, has become a large enclave of minority population. Due to the structural change within modern industry, many jobs are moving to the suburbs. However, many blacks desiring to follow their jobs have been unable to move because of housing discrimination.

Evidence exists that many large industrial plants in the Parsippany Troy Hills area employ blacks. However, blacks seeking to find housing in the area have had great difficulty. Edward

Thomas, an executive for the Warner Lambert Corporation, is responsible for finding housing for workers and employees. He has testified that 8.5 percent of the Warner Lambert employees are black and that they earn enough to live in Parsippany Troy Hills apartments. However, he has found that his black employees have much greater difficulty finding apartments in Parsippany Troy Hills than do white employees (*Enforcing Equality in Housing and Employment Through State Civil Rights Laws,* the Administrative Process Project of Rutgers Law School, Newark, N.J. and the N.J. Division of Civil Rights, 1969–1972, p. 190).

Effective search is initiated by apartment owners, not by the potential tenants. Based upon interviews with the landlord group, five search techniques are found to exist:

1. Five of 18 developments use newspapers.
2. Two of 18 developments use road signs.
3. Seventeen of 18 developments use on-site signs.
4. None of the 18 developments use broker listings.
5. Of those that responded, all indicate that the source of tenants are walk-ins.

In no case was it reported that a sign stating that discrimination is illegal was visible on development property.

The landlord reporting rule, though in operation for more than a year, is maintained through the voluntary compliance of landlords. Present use of the information involves the identification of high turnover developments, i.e., more than 25 percent per year, followed by the formal notice by the division of possible action in light of continued absence of minority tenants. More intensive use of this information must await an expanded budget and continuing leadership by the new division director.

On occasion the division has acted as a referral service through the forwarding of vacancies to open housing groups. However, the combination of time delay and tight rental markets render these efforts minimally effective.

The impact of the various division of civil rights proposals has been markedly limited to date. Field research indicates that oppressively tight markets for intermediate and low income apartments render the efforts to improve the search process negligible. For example, in Bergen County, a large area of postwar industrialization near New York City, the open housing organizations could not find 'two-bedroom apartments for under $250 a month rental. Further, the establishment of a formal tenant refferal service has not been acted upon by the division. This is largely the result of the traditional deadlock involving the division's suit against the Parsippany Troy Hills developers: *Blair* v. *Knoll Manor, et al.,* which has been before a hearing examiner for the preceding year and a half. In *Blair* v. *Knoll,* the division asserts that "the maintenance of a segregated development combined with the failure to provide notice of vacancies to minority groups constitutes a withholding of property on account of race, and therefore violates Section 10:12–5(G) of the Law Against Discrimination." (Appendix O, Brief for Civil Rights Division in *Blare* v. *Knoll, et. al.,* Enforcing Fair Housing Laws, p. 254.)

Conclusions

There is a substantial potential in perfecting the housing search process. The present situation is marked by substantial variation in procedures as a function of socioeconomic factors—particularly age, race, and income. Defining the Federal Government's possible role will require more analysis of current procedures and the market reaction to alternate activity. The process is not simple; the payoffs, however, look promising.

The Housing Search and a Governmental Posture

The purpose of this report was to describe the existing theory and research centering upon the search for housing. In review, the search itself was analyzed first through its behavioral or decisional components. Second, the conditions within which this behavior was manifested were analyzed into the structural determinants of search.

Both theory and research are still in an incipient form. Each of the studies reported herein uses a highly restricted group of individuals and records their impressions regarding the several aspects of their last housing search. Hempel's pioneering work has uncovered the socioeconomic characteristics associated with both the duration and intensity of search as well as the types of information sources most likely to be used by different types of families. However, a clear separation of housing markets awaits future work. For example, the search for rental units has yet to be adequately described. Neither the search behavior nor the type of government policy needed to improve it is known for the large number of young families as well as older persons without children at home who appear to prefer apartment living and rental tenure over the other alternatives.

Save for the Neufeld-Kenney study, nothing is known of the search behavior of black Americans; similarly, the existence and impact of the structural barriers and the several market openings upon the various social-class and life-cycle groupings of black Americans is unknown.

Most debilitating, from a policy perspective, is the inability of the present research to deal with specific search behavior in light of its market-specific supply of housing. We have taken the a priori view that housing supply is a determinant of search behavior; however, how it affects the recent homeowner, renter, and the unsuccessful searcher is not known.

The deficiencies previously noted deal with either the supply or demand side of the market. The institutional and informal middlemen linking the two sides of the market provide us with little additional knowledge. At best, we have identified a group of institutional middlemen and services such as the real estate broker, rental agent, and multiple listing service; however, their operation in each of the submarkets for housing, as well as their influence upon the housing transaction process in tight housing markets, does not provide sufficient knowledge from which to predict future behavior.

We are aware of the presence of a new institutional middleman in the market; the housing warehouse. The service is designed to increase a family's mobility by holding their present house and where possible relocating them in another city through a cooperative warehousing firm. Unfortunately, where and in which housing submarket these services appear is still conjecture.

Information regarding middlemen services internalized into the processing sector of our economy offers little more in the way of effective guidance. It has been found that firms move into suburban areas knowing that a housing shortage exists and that it will affect both the relocation of their present employees as well as their ability to hire new employees. However, even after acknowledging the problem, little help is extended to that class of workers most affected by the difficult search process. What is not known is whether the firms have been ingenuous in their responses, and if so, whether their present lack of adequate resources to deal with the problem or the costs involved in absenteeism and labor force shortages are insufficient to provoke much more than a personal complaint by the firm's respondent.

Thus, although many governmental postures can be suggested, the insufficiency of our present models linking behavior with structural characteristics renders each policy relatively blind. As of this writing, it is in no way clear which of several personal or family search goals should guide a governmental posture. Undoubtedly, families seek housing for income, security, status, and amenity goals; in turn, each most likely has a shortrun and a longrun dimension. A feasible governmental policy must be capable of identifying and controlling the goal or goals felt to be the most needed. As yet, this cannot be done.

Traditional policy has centered upon the structural aspects of the housing market. Local tax and mortgage interest deductions from the Federal income tax benefit the homeowner only after the successful completion of his search. The National Housing Act has helped construct and/or finance new dwelling units as well as rehabilitate existing developments. To the extent that these deal with the housing market, they deal with it on the supply side. However, a policy involving search must deal either with the elements of the demand side or with the institutional middlemen. Before preceding upon such a policy, a realistic model must be built that will not only project the direct effects of any governmental policy but also the indirect and feedback effects both upon the housing market and the political structure of the governmental level involved.

Appendix 1: Components of Industrial Sectors

The Center's employer survey has grouped together firms in various SIC for the purpose of clarifying the questionnaire response patterns. The following section identifies the 6 major classifications referred to in the text, and the 2 digit SIC numbers as well as a description of each industrial group included within the major classification.

SIC Number	Description
1. Soft Goods	
20	Food and Food Products
21	Tobacco and Tobacco Products
22	Textiles
23	Apparel

2. Hard Goods
   - 24 Wood and Wood Products
   - 25 Furniture
   - 26 Paper and Paper Products
   - 27 Printing and Publishing

3. Raw Resource/Refining
   - 28 Chemicals
   - 29 Petroleum
   - 30 Rubber and Rubber Products
   - 31 Leather and Leather Products

4. Metallurgy
   - 32 Stone, Clay and Glassware
   - 33 Primary Metals
   - 34 Fabricated Metals

5. Machinery
   - 35 Non-Electrical Machinery
   - 36 Electrical Machinery
   - 37 Transportation Equipment
   - 38 Instruments

6. Miscellaneous
   - 39 Toys, Sporting Goods, Jewelry, etc.

7. Business and Education

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A Rationale for Government Intervention in Housing: Minority Construction Workers and Contractors Are Victims of Discrimination

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Summary

There is much evidence that minorities have been prevented from entering the skilled building trades. The major offenders in most areas are the highly skilled mechanical crafts and the carpenters rather than the trowel trades.

Some progress has been made in involving minorities in crafts in the past decade. Outreach programs have successfully identified and prepared candidates for union apprenticeship classes. "Pressures" and "plans" have forced unions to allocate a larger share of training slots to minority youth. Government subsidies have helped to finance many of these programs. I recommend that they be continued and intensified where necessary.

Consideration should be given to expanding the nonunion sources of training. Perhaps trainees could be subsidized to work as electricians' and carpenters' aides in conjunction with some vocational school training. This might be fruitful in the housing sector, which in many cities is nonunion.

Quota plans sometimes tend to overlook training and assume incorrectly that minority journeymen would be available, if only unions and contractors would look for them. As a result, such plans often fail. Contractors hire travelers and permit holders, and reshuffle available minorities in an attempt to find shortrun expedient solutions.

The problems of minority contractors have been less well identified. Although they face serious difficulty, there is little evidence that these contractors encounter greater problems in construction than in other industries. Minority contractors have difficulty obtaining financing, insurance, reliable labor, and "know-how" but so do minority firms in all other industries. The one distinguishing factor is that there are fewer minority employees in the industry who might eventually utilize their accumulated knowledge as managers and employers. But this difference eventually will be eliminated through training programs.

Repeal of the Davis-Bacon Act will aid minority labor and contractors by loosening the monopoly power of unions. Maintenance of a generally prosperous and growing construction sector will make integration more palatable to unions and hence more successful.

Carefully conceived subsidies to minority training and upgrading programs seem to me to be the natural and direct approach to the problem. The more general housing subsidy plans such as the National Housing Act are too indirect to be the major weapon in the battle against discrimination in construction labor markets. They may be a helpful complement in a balanced attack against such discrimination or may be quite appropriate for other purposes. But in my opinion, housing subsidies cannot be justified primarily as a weapon to fight discrimination against minority construction workers and contractors.

This paper attempts to assess the problem of racial discrimination against workers and contractors in the construction industry and to make recommendations on the proper role of Government.

To the extent that unions have been able to exercise monopoly power and exclude minorities and others from the skilled building trades, Government has an obligation to eliminate either the source of this monopoly power or to regulate it so as to correct its abuses. This paper will investigate the role of unions in detail.

To the extent that minorities are underrepresented in the skilled crafts for reasons such as general social discrimination in the public schools, a case might be made for corrective government action on the grounds of equity. However, Government should be aware of the actual impact of the policy relative to the intended impact. This paper will attempt to analyze the effectiveness of current Government programs.

The first section discusses and interprets the facts concerning discrimination in the skilled building trades. The second focuses on the vital role of apprenticeship training. The third analyzes the quota and preferential treatment plans that of late have been invoked in the construction industry. The fourth section highlights the special problems of minority contractors. The fifth section presents some alternative policies and programs. The final section draws conclusions and makes recommendations.

History of Blacks in the Union Movement

Blacks have not always been excluded from the building trades. It is well documented that many slaves were trained for a variety of skilled jobs needed in the plantation economy, especially for construction. But it is clear that blacks have been excluded since emancipation. Northrup and Marshall discuss the history of discrimination by craft unions in the South and the North in detail.[1]

Table 1 presents census data on the representation of blacks in various building trades from 1890 to 1970. The highly skilled mechanical trades for electricians, plumbers, and structural metal workers, among others, did not develop until after the Civil War and appear to have been exclusive from their beginnings. In the older skills of carpentry, painting, paperhanging, and roofing, blacks accounted for less than 4 percent of the membership in 1890. Minority entry has been relatively easy only into the trowel trades (plastering, cement finishing, and bricklaying). Minorities have always been admitted into the ranks of the unskilled laborers.

[1] See H. R. Northrup, *Organized Labor and the Negro*, Chpt. 2; and F. R. Marshall, *The Negro and Organized Labor*, Chpts. 1, 5, 6.

Table 1. Male Negro Representation in the Building Trades

	Negroes as Percent of Employed							Negroes as Percent of Unionists			
								Census Bureau		EEOC	
	1890	1910	1930	1940	1950	1960	1970	1966	1970	1967	1969
All Civilian Occupations and Industries	11.2	10.0	10.1	9.4	9.4	10.2	10.1	10.6	11.1	N.A.	N.A.
Skilled Building Trades	3.7	3.8	3.8	3.6	4.7	5.5	7.1	3.2	5.1	2.5	3.1*
Electricians	N.A.	0.6	0.7	0.7	1.0	1.4	3.0			0.6	1.9
Plumbers-Pipefitters	1.1	1.7	2.0	2.2	3.3	3.3	4.7			0.2	0.8
Carpenters	3.6	4.3	3.5	3.9	3.9	4.4	5.5	4.5	3.6	1.6	2.9
Excavators-Graders	—	—	4.4	N.A.	3.1	3.6	7.5			4.0	2.7
Painters-Plasterers	3.0	4.4	5.8	5.1	6.9	7.8	10.0			6.8	9.3*
Painters-Paper	2.0	2.9	3.6	3.8	5.5	6.9	9.9			3.7	4.2
Plasterers-Cement	10.3	13.0	15.8	15.2	19.6	21.3	27.6			14.0	15.3
Brick & Stone Masons	6.1	7.5	6.9	6.0	10.9	12.1	15.9			9.6	9.5
Other Building Trades	N.A.	2.9	2.8	2.3	4.9	7.1	13.4			3.3	3.3*
Structural Metals	N.A.	0.9	1.2	2.9	2.7	3.9	2.3			1.7	1.7
Roofers	4.0	4.3	3.1	N.A.	6.9	10.9	11.6			13.5	13.3
Building Trades Apprentices	2.9	2.7	2.2	N.A.	1.6	2.4	4.5			N.A.	5.3
Unskilled Laborers (Building)	20.0	19.8	21.4	19.0	25.0	25.9	22.4	33.9	23.2	30.5	24.1

* Estimated by author from incomplete data.

Sources:

R. Marshall, *The Negro and Organized Labor*, John Wiley & Sons, 1965, p. 157 for many trades 1890–1950.

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U.S. Bureau of Census, Current Population Reports, Series P–20, N. 216, "Labor Union Membership in 1966," March 8, 1971.

U.S. Bureau of Labor Statistics, Report 417, "Selected Earnings and Demographic Characteristics of Union Members, 1970," October 1972.

A. Blumrosen, *Black Employment and the Law*, Rutgers Univ. Press, 1971, p. 318.

H. Hammerman, "Minority Workers in Construction Referral Unions," *Monthly Labor Review* (May 1972), p. 21.

Table 1 also indicates that little progress was made during the 50 years between 1890 and 1940. In fact there is evidence of retrogression during the Depression of the 1930's. The tight labor markets of the 1940's stimulated a full percentage point increase in the black proportion of skilled building tradesmen. Progress continued during the 1950's, although more slowly. Job opportunities for blacks expanded most rapidly among the traditional trowel trades and least rapidly in the mechanical crafts. The greatest decennial increase in black employment occurred during the 1960's. Presumably this has been due in part to relatively tight labor markets as well as to the civil rights legislation and agitation of the last half of the decade.

Data on Negro membership in unions are available only for recent years. Bureau of the Census survey estimates show that in 1970 only 5.1 percent of all skilled building craft unionists were Negro, compared to 7.1 percent of all skilled building craft workers (union and nonunion). More detailed information is available only from reports submitted to the Equal Employment Opportunity Commission (EEOC). In 1969, plumbers, electricians, and structural metals unions had a Negro membership of less than 2.0 percent while the carpenters, excavators, and painters unions had between 2.0 percent and 4.5 percent.[2] In virtually all trades (except laborers), blacks are better represented in the nonunion construction sector than in the union sector. That does not necessarily imply that they are not also discriminated against in nonunion employment.

The limited evidence available in Table 1 suggests that the building trade unions did admit more blacks during the late 1960's. The 1967 and 1969 EEOC surveys should be treated with caution, however, because in some trades the reporting unions differed greatly between the two years.[3]

Table 2 presents the available data for Spanish-speaking Americans. In general Mexican, Puerto Rican, and Cuban Americans have the same labor patterns as Negroes, although the degree of exclusion is less pronounced. Overall the Spanish were as well represented in the skilled building trades in 1970 as they were in the labor force. They were underrepresented among the electricians and plumbers in general and underrepresented within the operating engineers unions.

[2] The Census Bureau and EEOC samples are different and not strictly comparable. See H. Hammerman, "Minority Workers in Construction Unions"; and U.S.B.L.S., *Selected Earnings and Demographic Characteristics of Union Members, 1970.*

[3] See H. Hammerman, op. cit.

Table 2. Male Spanish-American Representation in the Building Trades

	Spanish as Percent of Employed	Spanish as Percent of Unionists	
	Census Bureau 1970	EEOC 1967	EEOC 1969
All Civilian Occupations	3.9	N.A.	N.A.
Skilled Building Trades	4.0	2.9	N.A.
Electricians	2.8	1.8	3.9
Plumbers-Pipefitters	3.0	1.4	1.4
Carpenters	3.7	2.7	4.9
Excavators-Graders	4.0	1.4	1.4
Painters-Plasterers	5.8	8.5	N.A.
Painters-Paperhangers	5.7	6.7	8.0
Plasterers-Cement Finishers	6.7	12.6	15.8
Brick and Stone Masons	3.9	2.1	2.8
Other Building Trades	5.8	3.4	N.A.
Structural Metals	2.7	3.4	3.8
Roofers	5.3	3.3	4.7
Building Trades Apprentices	3.8	N.A.	3.1
Unskilled Laborers (Building)	7.6	9.8	10.7

Sources:
Bureau of Census, Census of Population, 1970, *Occupational Characteristics,* Final Report PC(2)-7A, Washington 1973, Tables 38-39.
A. Blumrosen, *Black Employment and the Law,* Rutgers Univ. Press, 1971, p. 318.
H. Hammerman, "Minority Workers in Construction Referral Unions," *Monthly Labor Review* (May 1972), p. 21.

It is clear that the skilled construction crafts exclude minorities. Do they also discriminate in pay? That is, do black unionists gain less from union membership than do white unionists? Ashenfelter has concluded, "We also consistently find the ratio of black to white wages in labor markets organized by craft or 'referral' unions differs little from the ratio in unorganized labor markets."[4] Unions will promote the interests of black members if blacks can get into the unions. Ashenfelter estimates that exclusion of blacks from the skilled crafts alone has reduced the national ratio of black to white male wages by 5 percent.[5]

In the early years of the movement to integrate minorities into the construction trades, unionists often argued that they were not discriminatory but that few qualified blacks ever applied for apprentice training. In part they were correct. As Marshall, Briggs, and others have argued, however, young blacks seldom were aware of apprenticeship programs because of the secrecy imposed by the crafts. Closely held information helped sons and relatives to enter the crafts and minimized the "risk" of a glut of unqualified outsiders diluting skills. Even when minority youths were aware of the programs they were discouraged from applying by parents and counselors who recognized the low probability of successfully challenging the white crafts.[6] Such arguments are now only of historical interest, given the recent interest of minority youths in entering the trades.

Other factors also have played a role. Discriminatory and inferior public education has left minorities less well prepared to enter the white collar professional, technical, and managerial jobs as well as the blue collar trades. A particular difficulty has been the achievement-aptitude tests required for entry into the crafts. Many have argued that these are heavily dependent upon educational and cultural background, which often are inferior (or at least different) for minorities.

In conclusion, the underrepresentation of minorities in the skilled construction crafts is due to a complex of social and economic factors. Unions have played an important but not exclusive role in this phenomenon, as shown by the small numbers of Negro skilled craftsmen in the nonunion sector of the industry.

Increasing Minority Participation in Apprenticeship Programs

One of the most important and effective means for expanding the supply of minority craftsmen would be to integrate the apprenticeship training programs. The Federal Government and many States have legislation that regulates apprenticeship. Until recently, this power was exercised primarily to improve the quality and vigor of the programs. For years, the laws have required nondiscriminatory selection of candidates but only recently have governmental agencies made any effort at enforcement. Since February 1971 the Federal Bureau of Apprenticeship and Training (BAT) has required that minority enrollment within each program be in proportion to minority representation in the area population.[7]

The rules apply only to programs that are voluntarily registered with BAT. A Department of Labor survey indicated that two out of three apprentices in the U.S. are registered.[8] Apparently there are relatively few advantages to induce unions and management to register the programs. Participants at one time were eligible for military deferments but this is no longer a factor. Registration allows the beginning apprentice to be paid somewhat less than the prevailing minimum wage; however, in many areas and trades the apprentices begin well above the minimum wage anyway.[9]

The February 1971 BAT regulation is unlikely to be effective because the only penalty provided is deregistration. In addition observers often have charged that BAT and the State regulatory agencies tend to be staffed by ex-craftsmen sympathetic to the unions.

One of the more effective techniques for increasing minority participation in apprenticeship programs has been the "outreach" concept. To provide better information and reduce some of the secrecy surrounding the programs, Apprenticeship Information Centers have been opened in some of the larger cities. In many cities agencies have been set up in conjunction with the National Urban League (NUL), the Workers' Defense League (WDL), and the local Building Trades Councils to recruit, tutor, and advise minority youths for apprenticeship training. In late 1971, at least 110 local outreach programs were in operation, many with financial support from

[4] O. Ashenfelter, "Racial Discrimination and Trade Unionism," p. 462.
[5] Ibid., p. 463.
[6] See F. R. Marshall and V. M. Briggs, *The Negro and Apprenticeship*, pp. 29–45.
[7] A. Maurizi, "Minority Membership in Apprenticeship Programs in the Construction Trades," p. 200.
[8] F. R. Marshall and V. M. Briggs, *Equal Apprenticeship Opportunities*, p. 9.
[9] Ibid., p. 14.

the U.S. Department of Labor and private groups.[10]

Marshall and Briggs attribute much of the success of the outreach programs to the fact that they concentrate on locating qualified and motivated minority youth. These programs tend to recruit among persons working steadily at low-paid unskilled jobs rather than among those "hanging around street corners" or those going to college. Recruits are tutored intensively in taking and passing verbal and mathematical aptitude exams. They undergo dress rehearsal interviews for the real interview they must pass in order to be admitted to apprenticeship. Upon completion of this pre-apprenticeship training, the recruit is directed to the appropriate office and is aided in filling out the application form, paying fees, and obtaining a medical exam. He may be aided in finding temporary work if there is a long lag between admittance and the beginning of the apprenticeship class.[11]

Some less successful attempts have been made to evade union controls over training. In particular, the extended lengths of the classes have been questioned. Maurizi reports that training time varies from 2.5 years for roofers to 4.5 years for plumbers and electricians.[12] Undoubtedly, unions design lengthy classes to increase the costs of entry, thereby limiting supply and increasing the incomes of trained journeymen.

Strauss has observed that those who complete the full apprenticeship program obtain a broad and deep knowledge of their occupation. In fact many of the available jobs do not require that much expertise and versatility. This allows many of the apprentice graduates to move up to supervisory and management positions while the more routine tasks are filled by nongraduate craftsmen. Many of the latter are apprentice dropouts or received on-the-job training in a more casual, nonunion environment. Others may have learned some skills in public vocational schools and still others simply picked up some skills by watching others at work.[13]

One attempt at bypassing formal apprenticeship training was made in Buffalo, N.Y. Enrollees were given 9 weeks of intensive classroom training followed by 20 weeks of on-the-job work experience. Upon completion of the 7-month project and the passing of an examination, the enrollees were certified as Journeyman Trainees by cooperating unions. Out of 50 students initially enrolling in this experimental program, 25 eventually were certified as carpenters, masons, electricians, and painters. Fifteen others who completed the training were not allowed to take the final exam by rebellious unions. Analysts of this project suggest that its "success" might not be applicable to large scale programs because the applicants had unusually good qualifications prior to selection.[14]

Public vocational schools are widely utilized as a source of more formal theoretical training of apprentices in conjunction with on-the-job training. This suggests that expanded use of the schools for preapprenticeship or "para-apprenticeship" training might be attempted. However, there is some criticism of the vocational schools' performance and their "academic" rather than "applied" orientation.[15]

The Federal manpower training programs (Manpower Development Training Act programs and the Job Corps) have been utilized to train some craftsmen. Marshall and Briggs report that these efforts were limited initially.[16] More recent evidence suggests that they have expanded.[17]

In many onsite construction projects, unskilled laborers work directly with skilled craftsmen in "teams." Since entry is relatively easy into the Laborers Union, it would seem natural to try to upgrade minority laborers who are members of these teams. Such an approach relies heavily upon the willingness of the craftsmen to take the time and effort to instruct the laborers. Such cooperation may be limited in view of the attitude of craftsmen toward those who "pick up" the skills more cheaply than they.

In my opinion, discrimination in apprenticeship has been most effectively breached by beating the unions at their own game. The outreach programs have located, tutored, and placed many minorities in union training programs by meeting and surpassing the unions' own standards. However, more effort might also be made in shortening the length of training and upgrading minority laborers.

Federal "Goals" Programs

A second tactic used by Government to promote integration in the crafts has been to impose quotas (now called goals) in various major

[10] See U.S.D.L., *Manpower Report of President 1972*, p. 95.
[11] Marshall and Briggs, *Equal . . .* , pp. 26–54.
[12] A. Maurizi, op. cit., p. 205.
[13] See G. Strauss, "Apprenticeship: An Evaluation of the Need."
[14] See D. B. Lipskey and J. B. Rose, "Craft Entry for Minorities: The Case of Project Justice."
[15] Marshall and Briggs, *The Negro and . . .* , p. 259.
[16] Marshall and Briggs, *Equal . . .* , p. 25.
[17] See U.S.D.L., *Manpower Report of the President, 1973*, p. 233.

cities. Construction firms bidding for Federal contracts (of $500,000 or more) must submit "affirmative action" plans to make minority employment in their firms equal the percentage of minority representation in the metropolitan area's labor force. This is to be done by upgrading skills of laborers and helpers, increasing apprenticeship training, and recruiting currently qualified minority journeymen. Plans are to be completed in steps over 4 to 5 years. Pressure is applied to contractors who (along with minority interest groups) in turn are expected to apply pressure to unions to meet the goals. The penalty for refusing to participate in "good faith" is permanent debarment from eligibility for Federal contracts. If the contractor cannot meet his goals but has participated in "good faith" he will not be harmed.[18]

Opponents of the plans criticize them as discriminating in reverse—that is, in favor of blacks and other minorities. Proponents defend the plans as being fair compensation to make up for years of exclusion and discrimination. They point out that the goals are intended to be met by attrition and expansion rather than by replacement. Regardless of the philosophical issues involved, the Supreme Court in effect upheld a lower court decision that the plans were legal by denying review in 1971.

Executive Order 11246 was first invoked in the Philadelphia construction industry in 1969 and hence affirmative action plans are sometimes referred to as "Philadelphia Plans." The Department of Labor prefers that hometown plans be voluntarily devised by labor, management, and minority groups rather than imposed by the Federal Government. The first hometown plan was signed in Chicago in 1970; similar plans are sometimes called "Chicago Plans." In late 1972 there were 56 imposed and voluntary plans in operation in major cities.[19]

Experience with the Involuntary Plans

The evidence suggests that the quota plans have induced some limited progress in certain cities but that they have encountered many difficulties. In this section we discuss some of these experiences.

Initially the Philadelphia Plan applied only to Federal construction sites. One reaction to the goals was that contractors and unions shifted minority craftsmen from private sites to Federal sites. They thereby met or partially met their goals without increasing minority employment in the industry as a whole. In response, the Government developed a plan that was applied to the Washington, D.C., area in 1970. Federal contractors were required to attain goals for their public and private construction sites jointly.

Rowan and Rubin have examined the Washington Plan experience in detail. They report that there are still many loopholes in the rules that reduce the pressure to expand minority participation.[20] First, contractors have often been able to meet their goals by using temporary employees such as "trainees," "travelers" from out of town, and nonunion workmen who are given temporary union permits to work for the duration of the contract but who lack union membership and guarantees of work once the Federal project is complete. Second, there is some evidence that minority laborers have been "promoted on paper" to skilled crafsmen. They may be paid the higher rate for the duration of the contract but lack prospects for upgrading in the long run. Third, subcontractors are still able to shift minority workers from private sites to Federal sites to help the general contractor attain his goal. Only the general contractor reports on his own job sites. Fourth, contractors readily agree in principle to meet the goals but rely upon "good faith" efforts as a safety valve to get them off the hook. This appears to be a rational strategy since the Government's will and resources to enforce the orders are limited. Through mid-1972 no contractor had been debarred in Washington despite numerous findings of noncompliance. A single case of debarment of a plumbing contractor in Philadelphia in late 1972 was newsworthy enough to be written up in a recent issue of the *Monthly Labor Review*.[21] Fifth, nonunion contractors and craftsmen have generally been uninvolved with the Washington Plan because of the implicit assumption by Government that they are nondiscriminatory. In fact, however, the proportion of minorities employed in nonunion firms differs little from union firms, at least in the Washington area. "Minority concentrations in the lower skilled categories may be primarily due to educational and training inadequacies in the community at large. . . . we believe that the average nonunion contractor is nonexclusionary and indeed wants quality work for the wages he pays. . . . Many nonunion contractors have always hired minorities, but as in

[18] Much of this section draws upon R. L. Rowan and L. Rubin, *Opening the Skilled Construction Trades to Blacks.*
[19] "Philadelphia Plan Backed," p. 69.

[20] See Rowan and Rubin, op. cit., pp. 49–110.
[21] "Update on Philadelphia Plan," p. 50.

the union sector, blacks are rare in the electrical, mechanical, and plumbing trades." [22] To the extent that nonunion firms do little Government work and are not covered by the plan, nonunion minority craftsmen undoubtedly will be bid away by other contractors to meet their quotas. Again minority employment will simply be redistributed rather than promoted.

In conclusion, there is some evidence that the involuntary plans have induced some token increase in aggregate opportunities for minorities (particularly in the previously all white crafts) and have guaranteed steady employment for existing black craftsmen. But short term expediencies to meet goals are no substitute for long term training of minority representatives.

Experience with the Voluntary Plans

In principle, Chicago-type plans are superior to imposed plans to the extent that they are based on cooperation rather than threat. On paper, they also are preferable in that they aim at longrun attempts to train minority journeymen rather than on shortrun attempts to find expedient solutions. And in many cases the voluntary plans cover all contractors in the area including those without Federal contracts. This reduces the possibility of meeting goals simply by reshuffling labor.[23]

On the other hand, Chicago-type goals tend to be general. They set no goals by specific craft. They provide no penalties for noncompliance other than the implied threat of a Government-imposed plan. The Chicago operations ran into heavy opposition from local unions that refused to comply with the rules agreed upon by the area Trades Council. Because of this and various other problems, the hometown plan was abandoned in 1971 and replaced in mid-1972 with a new voluntary plan.

Rowan and Rubin have studied the Indianapolis voluntary plan in detail. They conclude that "the Indianapolis Coalition was the only one of its kind that genuinely wanted the hometown plan to succeed." [24] Planners recognized that there were only 35 to 40 qualified minority journeymen in all of Indianapolis and wisely emphasized outreach training and apprenticeship. As a result some progress has been made, although some unions have been less enthusiastic participants than others.

With the possible exception of Indianapolis and a few other cities, there is little evidence that the voluntary plans have actually been more successful than the involuntary plans. The major problem in many cases is that these plans are "voluntarily" signed primarily in order to avoid a compulsory plan. Rowan and Rubin suggest that a periodic review of the progress of the operation is necessary to maintain vigilance. A prosperous construction market also may be a prerequisite as integration is less painful during a period of expanding employment than contracting opportunities.

Minority Contractors

It has been suggested by many that Government should help minority contractors in the construction industry as a weapon against discrimination. Not surprisingly, there are even fewer minorities on the ownership and management side of the industry than on the labor side. Table 3 presents Census Bureau estimates of minority ownership. In 1969, blacks owned only 1.9 percent of all construction firms in the United States and these tended to be the smallest (often one-man) operations. When measured by the value of total receipts, blacks controlled only 0.5 percent of the industry. The situation is similar, if not quite so pronounced, for Spanish-speaking Americans.

Those minority firms that are in business appear to have just as much trouble getting qualified minority labor as the white-owned firms. "Although major white contractors have hired unskilled trainees, despite the obvious cost, in order to comply with the Plan, few minority contractors can be so generous. . . . In fact we have found signs that minority contractors will hire skilled whites, or seek white referrals from the union, in order to compete effectively. . . . Thus, minorities entering the industry through this route may remain at the lower end of the skill spectrum." [25] Thus, it is not clear that increased Federal contracts granted to minority contractors would necessarily increase minority employment in the shortrun although more evidence should be accumulated.

One of the major problems standing in the way of expansion for minority contractors is a lack of financial resources and credit. This in turn can be traced to a lack of business experience. Second, most public construction projects

[22] Rowan and Rubin, op. cit., p. 93.

[23] Much of this section draws on Rowan and Rubin, op. cit., pp. 135–170.

[24] Rowan and Rubin, op. cit., p. 185.

[25] Rowan and Rubin, op. cit., p. 96.

require "bonding" to insure the public against shoddy or delayed work, misuse of funds, and cost overruns by the contractor. The inexperienced, marginal firms have difficulty becoming bonded. Third, like most marginal operations, minority contractors have difficulty getting and keeping quality labor of any race.[26]

Table 3. Minority Ownership of Business in the Building Trades

	1969	
	Percent Negro	Percent Spanish Speaking Americans
Total Labor Force	10.1	3.9
Number of Firms		
All Industries	2.2	1.3
Contract Construction	1.9	1.2
Total Receipts		
All Industries	0.3	0.2
Contract Construction	0.5	0.3

Source: U.S. Bureau of Census, *Minority-Owned Business: 1969, MB-1*, U.S. Government Printing Office, Washington 1971, Table B, page 2.

Many methods of upgrading minority construction firms have been suggested. The Federal Small Business Administration (SBA) has various programs to help minority firms obtain Federal contracts and bonding. Many departments of the Federal Government require that whenever feasible, contracts should be granted with priority to minority business. Joint contracting ventures between experienced white firms and less experienced minority firms have been suggested and attempted occasionally. Hopefully, the latter will be able to "learn the ropes" and build a record of success in such ventures. It has been suggested that minority contractors' associations be formed and strengthened to provide educational, technical, and political assistance to struggling entrepreneurs.

Glover has been among the first to study such upgrading programs. Focusing on Atlanta and Houston he concludes that, "The power of government programs to assist minority contractors have far exceeded their accomplishments." [27] At least in those cities the SBA appears to have hindered more than helped. Glover finds many instances in which joint venturing yields little obvious payoff for the minority contractor. For example, experience gained while operating under special joint corporate status has often been ruled irrelevant in determining the experience of the minority corporation for bonding or for a loan.

Upgrading minority contractors might be an admirable goal in itself but Glover warns, "By itself, upgrading minority contractors does not offer a 'shortcut solution' to achieving integration in the building trades unions," [28] nor, we might add, in the nonunion trades.

Suggested Reforms

Revising Labor Legislation

Wherever there is monopoly power, Government has an obligation to eliminate its sources or to regulate the monopoly. Most of the policies discussed in this paper emphasize regulation of entry into unions. Would it be possible to eliminate the source of union power?

Government conceivably might outlaw the closed shop and hiring hall arrangement in construction. History suggests that this would be futile. Construction unions were relatively well organized and powerful in the 19th century, long before society accepted unions in general. The 1947 Taft-Hartley Act did outlaw the closed shop but with little real effect. In 1959, Congress amended the law to legalize union referrals in construction.[29] The hiring hall does play a necessary role in this industry where workers move from employer to employer as projects end and begin.

It has been argued by many that the Davis-Bacon Act of 1931 has strengthened union monopoly power. The act requires that all Federal construction contracts (of $2,000 or more) must pay the "prevailing" wage rate in the immediate area in which the work is to be performed. The Department of Labor has usually interpreted the "prevailing" wage to be the union wage, in part because data on union wages is more readily available. In addition to the Federal law, 35 States have similar laws covering State and local government construction contracts.[30]

Several studies by economists as well as by the U.S. General Accounting Office indicate that in practice the Davis-Bacon Act has extended higher than "prevailing" wages to Government building sites. This has provided increased em-

[26] Much of this section draws on R. W. Glover, *Developing and Upgrading Minority Construction Contractors.*
[27] Ibid., p. 118.
[28] Ibid., p. 189.
[29] See S. Cohen, *Labor Law*, pp. 357, 450–451.
[30] Much of this section draws upon J. P. Gould, *Davis-Bacon Act: The Economics of Prevailing Wage Laws*, American Enterprise Institute, 1971.

ployment opportunities for higher wage union labor and has limited opportunities for nonunion labor and contractors. The latter are reluctant to bid on Government jobs because of their lower productivity and because of the labor morale problems they would face when their employees completed Davis-Bacon jobs and returned to "competitive" wages.

Since minority construction workers and firms have been more highly concentrated in the marginal, nonunion sector of the industry, they undoubtedly have been harmed by Davis-Bacon regulations. Attempts to increase minority representation are in direct conflict with this act. It is interesting to note also that attempts under the National Housing Act to subsidize and reduce housing costs to low income families are directly offset in part by the Housing Act's requirement that costs be raised by paying "prevailing" wages.[31]

Repeal of the Davis-Bacon Act would help promote minority interests in the construction industry. However, experience during the brief suspension of the act in 1971 by President Nixon suggests that such an attempt would be met by stiff political opposition from unions.

Expanding Prefabricated Housing

Construction unions are faced with growing competition from lower cost prefabricated products and modular housing units. These are often built on an assembly line basis using less skilled and often nonunion labor. On the surface, it would seem that increased support for the prefabricated building sector might provide leverage to induce unions to integrate. This might not be realistic for several reasons. First, since modular housing operates in regional or national markets, integrated contractors and unions would be penalized just as much as would discriminators. Second, to the extent that modular housing is built in white rural areas, longrun job opportunities may be reduced for minority workers. Finally, declining job opportunities in the onsite construction sector would undoubtedly intensify union attempts to save jobs for current members. In this sense, policies designed to expand the prefabricated construction sector are probably in conflict with policies to involve minority craftsmen. Partially offsetting these effects, however, is the fact that it might be easier to police affirmative action plans in the more permanent (less transient) work setting of a "pre-fab" factory.

[31] Ibid., pp. 6–7.

Housing Subsidies

Many economists have pointed to maintenance of high levels of aggregate demand and intense competition for scarce labor as the most effective means of promoting economic integration. On this ground, larger subsidies and tax breaks for housing and construction might be justified. Such a policy might be quite successful if coupled with outreach apprenticeship programs. But one must be skeptical of this strategy if unions are able to ration training and jobs at will. In Table 1, we see that virtually no minority gains were made during the relatively prosperous period from 1910 to 1930 and only limited gains during the labor shortages of the 1940's.

At least three types of public housing subsidies are in use or have been suggested.[32] Public housing typically has been built under direct Government contract. In this case, Philadelphia- or Chicago-type plans may be imposed to promote minority building interests. However, the limited effectiveness of these plans (as discussed above) is compounded by the fact that such contractors must pay prevailing Davis-Bacon wages.

Section 235 of the National Housing Act provides for subsidies to low and middle income families who locate housing of their own choice. Families pay 20 percent of their adjusted gross income toward the mortgage and the Federal Government pays any residual. In concept, the housing units should have been built by "equal opportunity" contractors, but casual inquiry by the author in Columbus, Ohio, suggests that such requirements may not be strict or binding. Older, existing homes cannot feasibly be checked because of a lack of records. With respect to newly built housing, the local Housing and Urban Development office in Columbus knew of no contractors who did not display their "equal employment opportunity signs" or who did not qualify. But the office did indicate that it would take action if it ever discovered such a case. Unfortunately, more rigorous studies of the enforcement problem do not appear to be available.

More aggressive attempts at enforcement might be made. Lists of approved contractors,

[32] See H. J. Aaron, *Shelter and Subsidies*, Brookings Institution, 1972; R. F. Muth, *Public Housing: An Economic Evaluation*, American Enterprise Institute, 1973; C. L. Edson and B. S. Lane, *A Practical Guide to Low and Moderate Income Housing*, Bureau of National Affairs, 1972.

subcontractors, and homes might be drawn up. Firms engaged in the low-cost housing sector would have an incentive to comply in order to participate in the subsidized sector. However, they would also have incentives to hire available minority workers away from other construction sectors, thereby simply reshuffling minority employment rather than expanding it. This problem can be minimized by making compliance depend upon training and apprenticeship rather than upon the employment of journeymen.

Many have proposed a housing allowance program that would provide a family with a certificate of a fixed amount for the purchase of housing of the family's choice. If eligible housing was unrestricted, the program would have little impact upon discriminatory labor practices. Consumers have limited knowledge of (or interest in) the racial composition of the construction crews that built the housing being considered for purchase. On the other hand, restrictions on eligibility would imply a situation similar to that discussed above under the Section 235 program.

Any housing subsidy program will assist the integration of the building trades in the sense that rising demand for housing and construction labor will make affirmative action plans more palatable to white craftsmen. The grounds for selecting among the various subsidy plans is more limited although in some ways the Section 235-type subsidy or a restricted-choice housing allowance might be preferred. If unions and contractors were required to maintain continuing integrated training and upgrading programs in order to have their housing qualify for the subsidies, the ultimate impact on minority employment might be greater than a subsidy to public housing. In the latter case, contractors may drop their affirmative action programs once the public housing is complete.

The impact of housing subsidies on minority contractors is even more ambiguous. On the one hand, a concerted effort can channel more public housing projects directly to minority firms. On the other hand, the marginal, low-wage nature of most minority firms suggests that they cannot afford Davis-Bacon wages and that they do not have the capacity to handle multistory public housing. Perhaps expanded housing allowances for low cost, single-family homes will aid minority contractors the most.

Many of the proposals to revise labor legislation or to subsidize housing that I have discussed in this section appear to complement rather than substitute for training and upgrading programs. Several of the proposals have limited or questionable prospects for success in reducing discrimination against minorities. The most helpful actions discussed in the section might be to suspend the Davis-Bacon Act and to maintain a growing construction industry.

Conclusion

In my opinion, there is much evidence that minorities have been prevented from entering the skilled building trades. Government can best correct this distortion by helping minorities obtain training.

The major offenders in most areas are the highly skilled mechanical crafts and the carpenters. The focus should be on these occupations rather than upon the trowel trades.

Some progress has been made in involving minority craftsmen in the past decade. Outreach programs have successfully identified and prepared candidates for union apprenticeship classes. "Pressures" and "plans" have forced unions to allocate a larger share of training slots to minority youth. Government subsidies have helped to finance many of these programs. I recommend that they be continued and intensified where necessary.

Consideration should be given to expanding the nonunion sources of training. Perhaps trainees could be subsidized to work as electricians' and carpenters' aides in conjunction with some vocational school training. This might be fruitful in the housing sector, which in many cities is nonunion.

Training is a more effective solution to the problem in the case of affirmative action plans, which sometimes overlook training and focus on the employment of journeymen. These plans are well meaning but of questionable effectiveness due to the availability of many expedient ways of temporarily achieving goals. Of course, affirmative action plans that are aimed at apprentices and trainees should be beneficial in the long run.

The problems of minority contractors have been less well identified. Although minority contractors face serious difficulty, there is little evidence that they encounter greater problems in construction than in other industries. Minority contractors have difficulty obtaining financing, insurance, reliable labor, and "know-how" but so do minority firms in all other industries. The one distinguishing factor is that there are fewer minority employees in the industry who might eventually utilize their accumulated knowledge as managers and employers. But this difference eventually will be eliminated through training programs.

In the above sense, the problems of minority craftsmen and contractors can be separated. Government may wish to provide preferential treatment to minority construction firms as part of a general attempt to rectify the impact of past discrimination, but this author sees little reason to focus on construction uniquely. In particular, as we discussed earlier in this paper, it does not necessarily follow that increased assistance to minority contractors will directly aid minority craftsmen in the near future. Without a major expansion in training, minority firms often will be forced to hire white skilled labor.

Repeal of the Davis-Bacon Act will aid minority labor and contractors by loosening the monopoly power of unions. Maintenance of a generally prosperous and growing construction sector will make integration more palatable to unions and hence more successful.

Carefully conceived subsidies to minority training and upgrading programs seem to me to be the natural and direct approach to the problem. The more general housing subsidy plans such as the National Housing Act are too indirect to be the major weapon in the battle against discrimination in construction labor markets. They may be a helpful complement in a balanced attack against such discrimination or may be quite appropriate for other purposes. But in my opinion, housing subsidies cannot be justified primarily as a weapon to fight discrimination against minority construction workers and contractors.

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Background Paper on Housing Market Discrimination and Its Implications for Government Housing Policy

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Summary

This paper outlines the nature, causes, and the direct and indirect effects of racial discrimination in urban housing markets and identifies the implications for government housing policy.

Negro Americans are intensely segregated in U.S. metropolitan areas. There is ample documented evidence that all levels of government at times have sanctioned private market discriminatory practices and have enacted official policies which contributed to segregated housing patterns.

Substantial research evidence indicates that because of housing market discrimination:

1. Blacks must pay more than similar white households for housing of comparable size, quality, and neighborhood amenity.

2. Blacks less often consume high quality bundles of housing attributes than similar white households.

3. Blacks are less likely to be homeowners than white households of similar income and family structure, and therefore do not obtain the benefits of this important form of investment, tax shelter, and inflationary hedge.

4. Blacks spend a smaller fraction of their income on housing than whites of similar incomes and family structure because of the higher relative prices of good quality housing and the restricted supply available in the ghetto.

In addition, housing market discrimination produces a number of indirect effects whose adverse consequences may be even greater than its direct effects.

If the ghetto is allowed to continue its rapid expansion, land and housing prices in central cities will remain at high levels, the expectation that the city will become a lower class slum will persist, and government programs aimed at reversing these trends will fail.

The major implication of these findings for public policy is that the Federal Government should make major efforts to open suburban housing to minority households. All HUD programs should encourage minority households to locate and to secure housing outside of established minority neighborhoods. The Department should vigorously enforce requirements that builders, developers, and leaders pursue aggresive open occupancy policies as a condition for participation in Federal programs.

Housing allowances presumably are being considered in the Department's review of current and potential housing programs. Because of the severe restrictions on the black housing supply in many metropolitan areas, a general income transfer would be more effective than allowances tied directly to housing. Housing allowances are preferable to production subsidies, however. Furthermore, a housing allowance program that provided greater subsidies to minority households who obtain housing outside of minority neighborhoods could be a powerful instrument to foster greater racial and economic integration.

The overwhelming evidence that discrimination decreases the opportunity of black households to be homeowners provides a powerful rationale for a special minority mortgage loan program. Such a program could favor applications by blacks who wish to purchase outside of the ghetto.

Policies to insure that minority households have access to the entire metropolitan housing market on an equal basis with the white majority will be difficult to formulate because of the persistence and subtlety of racial prejudice. The task is demanding, but the benefits to the entire population are inestimable.

Introduction

The direct and indirect effects of racial discrimination in urban housing markets on the welfare of white and black Americans, on the efficiency of metropolitan growth, and on the effectiveness of other government programs are numerous and difficult to describe. Some of them are well established and uncontroversial. Others are poorly documented and are subject to considerable debate. Moreover, much of the highest quality research that investigates the effects of racial discrimination on urban housing markets is recent and remains nearly inaccessible in preliminary reports, in draft manuscripts, or in professional journals.

It is important to articulate these effects because discrimination, along with poverty, is largely responsible for the unsatisfactory outcomes produced by urban housing markets and provides the major justification for government intervention. There are, of course, other justifications for government intervention in predominately private housing markets: to stabilize the economy, to stimulate research and development, to insure health and safety, and to correct market imperfections resulting from neighborhood effects. These concerns, however, are minor considerations when compared to the adverse effects stemming from discrimination and poverty.

Other authors have primary responsibility for tracing the effects of poverty and its implications for government housing policy. Therefore, this paper examines the impact of racial discrimination in urban housing markets, and considers policy prescriptions suggested by that perspective. The empirical studies summarized in this paper and much of the analysis of housing market discrimination and segregation refer to Negro Americans. Other minorities unquestionably experience similar forms of discrimination and comparable welfare losses. In some areas these groups may be numerous enough to cause distortions in metropolitan growth and development similar to those ascribed to the Negro populations of large cities. Because of the limited research that has been done on the effects of discrimination on other minority groups, however, the analysis in this report is based on the experience of black Americans.

Racial Discrimination, Segregation, and their Direct Effects

Policymakers responsible for the formulation and administration of housing and urban development programs should consider the following findings about the nature and effects of housing market discrimination:

1. Negro Americans are intensely segregated in U.S. metropolitan areas. Existing patterns of segregation have existed for decades, and—unlike the experience of other immigrant groups—blacks have become increasingly segregated over time (Taeuber and Taeuber, 1964; Taeuber and Taeuber, 1965; Lieberson; McEntire). Only a fraction of existing patterns of segregation can be explained by the low incomes and other characteristics of Negro households (Taeuber and Taeuber, 1965; Pascal; Kain and Persky, 1969). Moreover, what little attitudinal information exists indicates that most black persons would prefer to live in integrated rather than in segrated neighborhoods (Brink and Harris).

2. Governments, including the Federal Government, are deeply implicated in creating and in maintaining existing patterns of segregation. Early Federal housing policy accepted prevailing private practices of racial exclusion and discrimination (U.S. Commission on Civil Rights; National Committee Against Discrimination; Abrams; McEntire). FHA, for example, not only acquiesced in the discriminatory private practices, but encouraged them to the point of recommending a model racially restrictive covenant to insure against "inharmonious racial groups." The Federal Home Loan Bank Board and the Home Owners Loan Corporation openly espoused policies favoring racial residential exclusion. In recent years, Federal, State, and local governments have less often actively supported discriminatory practices, but they have not been forceful in their efforts to overcome decades of government inaction or outright support of racial segregation. Local governments today seldom pursue policies whose avowed effects are to exclude minority households. Race, however, is often a factor in the resistance of local communities to subsidized and low income housing. The exclusionary policies of local governments cannot explain either the segregation of black households or their concentration in central cities. However, zoning and similar policies do support existing patterns of segregation by income and race and make it more difficult to develop polices to overcome these patterns.

3. As a result of discriminatory practices in urban housing markets and the intense segregation of Negro households in most U.S. metropolitan areas, blacks must pay more than similar white households for housing of comparable size, quality, and neighborhood amenity. A recent high quality study by Robert Gillingham using BLS and census data for 1960–61 provides the best and most extensive systematic evidence on the magnitude of discrimination markups for

rental properties (Gillingham). Of the 10 large SMSA's included in his study, Gillingham found evidence of discrimination markups in all but one, San Francisco (Table 1).

There is some reason to believe these discrimination markups may have declined somewhat in the past 13 years as the rate of growth of urban black populations has declined. Analyses by King and Mieszkowski and by John Quigley and me using more recent data indicate, however, that comparable differentials remain (King and Mieszkowski; Kain and Quigley, 1972a; Kain and Quigley, 1972b). The King-Mieszkowski study obtained a discrimination markup of 18 percent for rental units in New Haven, Connecticut, in 1968–69. John Quigley's and my analysis of 1,500 households in St. Louis (1967) obtained a markup of 9 percent for rental units and 5 percent for owner-occupied units.

These analyses of discrimination markups implicitly assume that housing is a homogeneous good and that housing in the ghetto is the same as housing outside the ghetto, except for price. The facts are quite different. Housing is a collection of heterogeneous attributes; the characteristics of housing bundles vary in major ways between the ghetto and the rest of the metropolitan housing market; and the discrimination markups of the numerous housing attributes are not uniform (Kain and Quigley, 1972b; Straszheim; Apgar and Kain). Larger price differences arise if the different price structures of the ghetto and nonghetto housing markets are taken into account. Quigley's and my analysis reveals that the typical ghetto rental unit could be obtained for 13 percent less in all white areas. Similarly, the typical nonghetto rental and owner-occupied units would cost 14 percent and 15 percent more, respectively, in the ghetto than in the nonghetto housing market. The difference in the average weighted and unweighted markups, of course, reflects the tendency of both ghetto and nonghetto households to buy less of those housing attributes which are relatively more expensive.

These findings are consistent with earlier investigations based on aggregate census data by Muth for Chicago in 1950 and 1960; by Ridker and Henning for St. Louis, in 1960; and by numerous others (Muth 1969; Becker; Haugen and Heins; Duncan and Duncan, 1957; Duncan and Hauser; McEntire; Ridker and Henning; Tilly, Jackson, and Kay; Rapkin; and Rapkin and Grigsby). For example, Richard Muth obtained estimates of discrimination markups of approximately 30 percent for owners and 5 percent for renters in Chicago in 1960 [Muth, p. 239]. Similarly, Ridker and Henning obtained discrimination markups for owner-occupied units in St. Louis of 20 percent. Indeed, of the large number of studies that have examined the problem only two, one by Martin Bailey (South Side of Chicago) and the other by Victoria Lampman (Houston), find no evidence of discrimination markups (Bailey, Lampman). The methodological difficulties of Bailey's study are too numerous to discuss at this point; those of Lampman's are obvious. Lampman considers no neighborhood characteristics, even though Gillingham's and numerous other studies have shown them to be as important as structure attributes in determining housing prices and rents.

Table 1. Estimated Discrimination Markups for Nonwhite Renters, 1960–61

City	Percent
Chicago	20.4
Los Angeles	9.5
Detroit	9.6
Boston	3.1
Pittsburgh	16.9
Cleveland	12.6
Washington, D.C.	3.0
Baltimore	17.4
St. Louis	13.4
San Francisco-Oakland	–0.1

Source: Robert F. Gillingham, "Place to Place Rent Comparisons Using Hedonic Quality Adjustment Techniques," Research Discussion Paper No. 7, March 1973, U.S. Bureau of Labor Statistics, Research Division, Office of Prices and Living Conditions, Washington, D.C., p. 60.

4. As a result of a price structure that is unfavorable to the consumption of high quality units and of more subtle supply restrictions, blacks less often consume high quality bundles of housing attributes than similar white households. Many kinds of housing are scarce or completely unavailable in the ghetto. To consume these desirable kinds of housing, Negro households often must move to neighborhoods not sanctioned for Negro occupancy. To obtain housing in these neighborhoods, they must, without guarantee of success, devote inordinate amounts of time and money to househunting, and subject themselves and their families to humiliation and harassment. As a result, most blacks limit their search for housing to the ghetto.

Housing market discrimination operates to restrict black access to the newest, highest qual-

Table 2. Estimates of Housing Consumption by St. Louis Households [1]

	Actual Black	Est. Black Consumption	Actual White Consumption
Dwelling Quality	9.10	20.53	24.52
Interior space	55.03	55.07	58.10
Neigh. Qual.	42.21	48.08	49.84
Exterior Space	5.42	6.21	11.03

[1] Estimates of the four housing bundle components shown in Table 2 were obtained by weighting the quantities of a large number of housing attributes by the price of these attributes outside the ghetto and aggregating them into the four housing bundle components shown.

Source: John F. Kain and John M. Quigley, *Discrimination and a Heterogeneous Housing Stock: An Economic Analysis* (New York: National Bureau of Economic Research, 1972).

ity housing in the best neighborhoods. As a result, black households consume less of both neighborhood and dwelling unit quality and exterior space than would be expected on the basis of their incomes and other characteristics (Kain and Quigley, 1972b). Quantitative estimates of these effects for St. Louis households, summarized in Table 2, illustrate how these supply restrictions affect Negro consumption of four housing bundle components: dwelling quality, interior space, neighborhood quality, and exterior space. Recent analyses by Mahlon Straszheim indicate a similar situation exists in the San Francisco-Oakland housing market (Straszheim).

5. Discriminatory practices and resulting supply restrictions insure that blacks are much less likely to be homeowners than white households of similar income and family structure. Table 3 provides some estimates of actual levels of Negro homeownership in 18 large SMSA's in 1960 and of the levels of homeownership that might exist if blacks did not encounter housing market discrimination.

The restrictions of Negro homeownership opportunities suggested by the statistics in Table 3 have far greater ramifications than may be evident at first glance. Estimates prepared by John Quigley and me indicate that an effective limitation on homeownership can increase Negro housing costs by over 30 percent, assuming no price appreciation. Moreover, calculations by Quigley and me show that, given reasonable assumptions about the appreciation of single family homes, a Negro household prevented from buying a home in 1950 would have out-of-pocket housing costs in 1970 more than twice as high as the costs would have been if the family had purchased a home 20 years earlier (Kain and Quigley, 1972a). These increases in housing costs are in addition to any price markups.

Table 3. Actual and Expected Proportions of Negro Households Who Are Homeowners by SMSA

SMSA	Actual	Expected
Atlanta	.31	.52
Boston	.21	.43
Chicago	.18	.47
Cleveland	.30	.58
Dallas	.39	.54
Detroit	.41	.67
Los Angeles/Long Beach	.41	.51
Newark	.24	.50
Philadelphia	.45	.66
St. Louis	.34	.55
Baltimore	.36	.61
Birmingham	.44	.56
Houston	.46	.56
Indianapolis	.45	.58
Memphis	.37	.50
New Orleans	.28	.40
Pittsburgh	.35	.59
San Francisco-Oakland	.37	.51

Source: John F. Kain and John M. Quigley, "Housing Market Discrimination, Homeownership, and Savings Behavior," *American Economic Review*, June 1972.

Much of the savings from homeownership results from the favorable treatment accorded homeowners under the Federal income tax. These tax provisions favoring homeowners are widely recognized and well documented (Aaron; Shelton). Quigley's and my findings suggest that Negro households at all income levels are impeded by housing market discrimination from purchasing and owning single family homes. As a consequence, Negro households are prevented from taking full advantage of these tax benefits. Since tax savings from homeownership increase with income, this aspect of discriminatory housing markets cuts most sharply against middle and upper income black households.

6. Racial discrimination in urban housing markets is an important part of the explanation for the smaller quantity of assets owned by Negro households at each income level. It has been well established that Negro households at every income level have less wealth than white households (Terrell). Current and historical limitations on homeownership are an important part of the explanation. A simple example is useful in demonstrating the substantial effect of homeownership on capital accumulation by low and mid-

dle income households. The average house purchased with an FHA 203 mortgage in 1949 had a value of $8,286 and a mortgage of $7,101 (FHA). Assume this house was purchased with a 20-year mortgage by a 30-year-old household head. If the home neither appreciated nor depreciated, the purchaser of this unit would have saved more than $7,000 and would own his home free and clear by his 50th birthday.

But the postwar years have not been characterized by price neutrality. The average appreciation of single-family houses during the past 20 years must have exceeded the 100 percent increase in the Boeck composite cost index for small residential structures. Use of this conservative estimate of appreciation would mean that the typical FHA-financed homeowner would have accumulated assets by age 50 worth at least $16,000, a considerable sum that he could use to reduce his housing costs, to borrow against for the college education of his children, or simply to hold for his retirement. The mean wealth accumulation of white households in 1966 was only $20,000 (Terrell).

7. Blacks spend less on housing than whites of identical incomes and family structure. Some earlier studies of housing markets indicated that blacks spent a larger fraction of their income on housing than whites at each income level (Muth). More recent studies, based on more adequate data, have established that blacks spend a smaller fraction of their incomes on housing than whites of similar incomes and family structures (de Leeuw; Kain and Quigley, 1972b; Straszheim, 1972). This result is a completely rational response to the higher relative prices of good quality housing in the ghetto and to the inferior selection of housing available to them (Kain and Quigley; Straszheim). There is no evidence to suggest that black households would spend less than comparable white households if a similar range of housing were made available to them at prices equivalent to those prevailing outside the ghetto. This inability to consume high quality housing, which largely explains their lower expenditures, is, of course, a major welfare loss for black Americans.

Indirect Effects of Housing Market Discrimination

The full effects of housing market discrimination extend far beyond housing and include additional, more subtle costs and welfare losses for both nonwhites and whites. Segregated housing patterns create unequal educational opportunity, increase insurance and other living costs, and contribute to employment discrimination for blacks. Discrimination also results in higher commuting costs for whites and distorts the overall pattern of metropolitan growth and development.

De facto segregation, rooted in racial discrimination in urban housing markets, has displaced de jure segregation as the principal cause of segregated education and the inferior quality it typically signifies (U.S. Commission on Civil Rights, 1967; Hanushek). Again, it is middle class and upwardly mobile blacks who wish their children to have the best education possible who suffer most from existing patterns of segregated education.

Blacks who buy homes in the ghetto must pay more for theft and fire insurance than the cost of similar coverage in suburban communities or are unable to obtain them at all (Holshouser, et al.). Mortgage financing will be more difficult to obtain and often will be obtained only on less favorable terms than in the suburbs. These premiums will be in addition to the discrimination markups and homeownership considerations discussed previously. Ghetto residents, moreover, will usually pay more for auto insurance than will suburban whites.

Housing segregation and discrimination reinforce more direct forms of employment discrimination. Geographic limitations on the residential choice of nonwhites insure that blacks can reach many jobs only by making time-consuming and expensive commutes (Kain, 1968). If nonwhites seek, obtain, and accept these distant jobs, their real wages (money wages minus the money and time outlays for commuting) will be less than those of comparable white workers. Often they will not even learn of available jobs far from the ghetto or will not bother to apply because of the cost and difficulty of reaching them. Faced with these difficulties, they may accept low paying jobs near the ghetto or no job at all, choosing leisure and welfare as rational alternatives to low pay and poor working conditions.

Racial discrimination imposes costs on the majority white population as well as on minorities. Commuting costs of centrally employed whites are appreciably higher than they would be if housing market discrimination and segregation did not exist. The steady growth of central city ghettos has forced centrally employed high and middle income whites to move farther and farther from their places of employment, increasing commuting time and costs. The intense pressure for expensive high speed highway and transit links to declining central employment areas is one of the consequences (Kain and Persky, 1969).

Racial discrimination and the steady growth of central city ghettos have seriously distorted the patterns of urban growth and development in recent decades. If racial discrimination had not existed in urban housing markets, private location decisions would have produced a far different geographic distribution of the low income, black population. If the suburbs had been open to middle and low income blacks, many would have moved to suburban areas along with their jobs, much in the fashion of whites of similar socioeconomic status. This would have affected the central city housing market in two ways. First, central cities would have had a very different image. A slower rate of growth of the poverty population would have affected the prestige of central city residential areas. If more middle and high income families had remained in the central cities, the quality of public schools and of other public services would have been maintained. Similarly, the quality of neighborhood environments would have declined less often. Second, a larger number of black suburban residents would have increased the competition for, and prices of, suburban housing. The competition for, and prices of, central city properties would have been correspondingly reduced. The exact magnitudes of these price changes are difficult to predict, but their direction is indisputable. Given these changes in relative housing prices, many more centrally employed whites would have decided to live in the central city. Similarly, few blacks employed at suburban workplaces would commute long distances back to the central city core to pay more for housing. Increased Negro residence in the suburbs also would have reduced under-representation of blacks in suburban plants.

The relative and often absolute dispersal of employment, rising incomes, and declining real transport costs would have decreased the demand for, and price of, dwelling units in central residential areas (Kain, May 1969). Centrally employed middle and high income households would have been encouraged by bargain prices to buy and renovate central city residences. In neighborhoods where individual units were structurally unsound and unsuitable for renovation by individual buyers, still lower prices would have encouraged private developers, perhaps assisted by government programs, to carry out more comprehensive renewal schemes.

But the poverty of entrapped minority and other disadvantaged populations insured that central city housing would deteriorate. The result has been a steady expansion of slum housing, deterioration of urban services, and an expectation that the process would continue until the entire central city became a black slum. This pattern of urban development presents us with the current policy dilemma: Can these historical trends be reversed, or is the economic, physical, and social decline of our great cities inevitable?

Implications for Government Housing Policy

A major emphasis of Federal urban development programs has been to arrest the physical and economic decline of central cities. These programs have been unequal to powerful market and nonmarket forces that operate in the opposite direction and thus have not been particularly successful. Discriminatory practices in urban housing markets and the resulting rapid growth of central city ghettos are the most important of these countervailing forces.

As long as the ghetto continues its rapid growth, land and housing prices in central cities will remain at high levels, the expectation that the city will become a lower class slum will persist and government programs aimed at reversing these trends will fail. If the growth of the ghetto could be arrested, positive programs to make the central city attractive to middle income families, either white or black, would have a chance. Without this change in the dynamics of metropolitan development, trends outlined in this paper cannot be reversed. The first objective of Federal housing policy should, therefore, be to open suburban housing to minority households.

The Department of Housing and Urban Development should review its existing programs and policies to insure that to the maximum extent possible they encourage individual minority households to consider housing outside of established minority neighborhoods and that they facilitate minority groups in locating and securing housing throughout the entire metroplitan housing market. In particular, if the numerous interest and construction subsidies to builders and developers are continued, the Department should make an even greater effort to insure that these agents pursue active open occupancy and equal opportunity programs as a condition for continued Federal subsidy.

If current Federal responsibilities for housing and urban development are transferred to State agencies, it is imperative that adequate safeguards be developed to insure that active open occupancy policies are developed and carried out. A policy to combat racial discrimination and segregated living patterns may be the strongest rationale for a major Federal role in housing. There is considerable evidence that Federal officials, who are insulated from local pressures, are able to take a longer view of urban development trends than local officials and are more willing and successful in pressing for reductions in discriminatory practices.

The Department also should evaluate the indirect effects of all of its programs to insure that they do not operate to maintain and to support existing patterns of racial segregation. Finally, it should make every effort to obtain a similar review of all other Federal programs. For example, a racial segregation impact statement similar to the environmental impact statements might be required of all Federal programs. Such a provision might encourage policymakers to consider explicitly the indirect effects of their actions on the patterns of racial segregation in American cities.

As long as minority households do not have access to the entire metropolitan housing supply, measures to increase the amounts available for them to spend on housing will be far less effective in reducing the housing deficiency of minority households than similar measures would be for the majority. If these minority households are given the freedom to spend the increased purchasing power in the manner they deem best, they will spend less on housing then would white households of similar incomes and circumstances. If they are forced to spend all of the increased resources on housing, they will obtain less housing than similar white households.

Even if there is no reduction in housing market discrimination, increases in black expenditures for housing undoubtedly would induce some additional housing investment and improve housing conditions somewhat within the ghetto. But the improvement obtained in this way would generally be much smaller than that which would be achieved if blacks had free access to the entire metropolitan housing market, where the possible supply responses are more variegated.

Because of the severe restrictions on the black housing supply in many metropolitan areas and the past reluctance of state and local governments to provide subsidized housing outside of low income neighborhoods, a general income transfer would be more effective than allowances tied directly to housing. Black households would benefit even less from a housing allowance than white households; Quigley's and my analysis suggests that low income black households would obtain about two-thirds as much housing per housing subsidy dollar as whites. Moreover, they would typically be unable to obtain the kinds of housing they prefer. Nevertheless, subsidies tied specifically to housing production are likely to be an even less effective means of increasing the supply of good quality housing available to minorities. There is little evidence that state and local governments are more inclined to build subsidized projects outside of low income neighborhoods today than they were a few years ago. Therefore, it is likely that such projects will continue to be built in high-cost, central locations with unfavorable neighborhood environments. Because of the high land costs, the required subsidy per assisted unit would be quite large. Moreover, these heavily subsidized units, in general, will not be the kinds of housing in strong demand by black households and in limited supply in the ghetto: single family units, in quality neighborhoods, suitable for homeownership.

To encourage racial integration in urban housing markets some economists have proposed the use of payments to encourage whites to move into predominately black neighborhoods and to encourage blacks to move into all or predominately white neighborhoods. The size of the payments would be scaled to the degree of integration existing in the neighborhood. No payments would be provided to blacks who wish to live in all-black neighborhoods or to whites choosing all-white neigborhoods. Although simple incentives of this kind are hard to fault on grounds of narrow economic efficiency, they have little chance of gaining public acceptance. Still, a number of more modest plans in the spirit of this proposal may be worth considering.

The Department currently has a large-scale experiment underway to evaluate the efficacy of housing allowances, and, presumably, programs of this kind are being considered in the Department's review of current and potential housing programs. A housing allowance program could be designed to encourage greater racial and economic integration and, more importantly, to discourage the intense concentration of black and poverty populations that produce unfavorable neighborhood effects in urban housing markets. Specifically, allowances either could be scaled to the social and economic concentration of particular neighborhoods, or quotas could be employed. In the first instance, housing allowance recipients would be given larger allowances for housing in neighborhoods where few allowance recipients currently resided. A quota system might operate with a uniform allowance, but refuse to approve units in neighborhoods once the number of recipients reaches a certain prescribed level. Quotas and sliding subsidy scales might be justified as a way to spread the burden, to insure that no community or neighborhood is forced to accept a disproportionate number of disadvantaged households, and to minimize the likelihood of adverse neighborhood effects.

A housing allowance program also could provide attractive opportunities to aid minority households in locating housing outside the ghetto and to monitor the activities of lenders, builders, and housing suppliers. The success of such measures, of course, depends on adequate and sympathetic staffing and on high level support for the aims of the program. Extreme care would have to be taken to insure that these information and counseling programs did not operate in precisely the opposite way, i.e., to discourage black households from searching for housing outside the ghetto and to channel them into the ghetto housing supply.

The overwhelming evidence that discrimination decreases the opportunity of black households to be homeowners provides a powerful rationale for a special minority mortgage loan program. The large impact of this impairment on Negro housing costs and on the ability of black households to save and to accumulate wealth justifies a special effort to insure that the mortgage applications of black households receive sympathetic review, regardless of the location of the properties concerned. A minority mortgage loan program should give full credit to the earnings of black females in the assessment of the financial strength of potential black borrowers. Female earnings are, of course, far more important for black households. Unfortunately, the effectiveness of such a program would be appreciably diminished by the limited supply of suitable housing in existing black neighborhoods.

HUD in particular, should insist on rapid and sympathetic review of mortgage applications by blacks wishing to buy properties outside of established minority concentrations. In addition, the Department might consider developing legislation that would enable FHA to give more favorable terms (lower interest rates, smaller downpayments, and longer terms) to minority households purchasing properties in areas distant from the ghetto.

Negro households are a large potential market for homeownership. As Negro incomes continue to increase, this potential demand will grow. It is well to emphasize, however, that these higher levels of homeownership will not be realized unless Negro households gain access to a supply of suitable housing. A combination of favorable terms, good service, and aggressive marketing by FHA would be a powerful force to loosen the barriers to Negro entry into middle and high income neighborhoods. Such policies would enable black households to obtain the higher quality housing that existing patterns of discrimination and segregation now appear to prevent them from consuming. A minority mortgage loan program would help redress the effects of earlier FHA policies that made it difficult or impossible for minorities to acquire housing in white residential areas, policies that were among the most effective instruments for maintaining segregated living patterns.

In the aftermath of the Detroit and Watts riots a number of banks and insurance companies instituted minority mortgage loan programs. Valuable lessons in how not to design a minority mortgage loan program can be gleaned from this experience. The BBURG (Boston Banks Urban Renewal Group) program was typical. It provided mortgages on more favorable terms to minority households. Unfortunately, eligibility for BBURG loans was limited to a few neighborhoods adjacent to Boston's ghetto. The consequences were completely predictable. Black demand for homeownership was channeled into these few neighborhoods accelerating the process of racial transition and consolidating Boston's black ghetto. Racial antagonism in the neighborhood was heightened, and many white occupants who might have remained in an integrated neighborhood were forced out. A minority mortgage program should be designed to reduce the pressure on transitional neighborhoods in the path of ghetto expansion rather than to exacerbate it. At minimum, it should be neutral in terms of residential location. Preferably, it should encourage minority households to seek out housing in predominantly white middle and upper income neighborhoods distant from existing minority concentrations.

Government price guarantees for properties located in the path of ghetto expansion should also be considered. It is widely believed that racial integration causes property values to decline. This belief would appear to be inconsistent with the evidence that housing prices and rents are higher in the ghetto than outside.

A number of studies of the trends in housing prices in transitional neighborhoods have identified a pattern of shortrun price movements that may explain this apparent contradiction (Karlin; Phares; McKenna; and Werner). White demand for properties in threatened neighborhoods may suddenly fall off in anticipation of their transition to Negro occupancy. Although prices are eventually reestablished at an even higher level, they may reach quite low levels during the hiatus between white flight and large-scale black entry. Owners who panic and sell their properties during this period may suffer large capital losses. Even a few experiences of this kind, no matter how atypical, may be sufficient to perpetuate the myths about the effect of integration on property values. If a program could be designed to support prices during these critical periods in transitional neighborhoods, it would remove a source of racial hostility, inhibit panic selling, and perhaps help stabilize neighborhoods in the path of ghetto expansion.

It would be difficult to design a program of this kind because of the complexity of urban housing markets and the difficulty of disentangling the shortrun dynamics accompanying racial integration from longer-run influences in housing markets. Even so, the feasibility of such a program should be investigated. Extreme care should be taken, however, to insure that the program does not encourage more rapid transition.

The evidence that housing market discrimination significantly reduces Negro homeownership, supports the case for revision of the current treatment of homeownership expenses under the Federal income tax. Several researchers have demonstrated that existing provisions of the Federal income tax benefit high income homeowners far more than low income ones and, of course, provide no benefits to renters (Aaron; Shelton). These provisions, which encourage high income households to increase their housing consumption and which provide far fewer benefits and inducements to low income households, cannot be justified either in terms of equity or efficiency. They are even more difficult to justify when the differential access of black households to homeownership is recognized. If there is a strong policy preference to encourage homeownership, a simple tax credit would be far more effective.

Some Concluding Observations

Rapid expansion of the Negro ghetto into good quality neighborhoods adjacent to the ghetto is the most likely way in which black housing conditions would be improved under current market circumstances. In some metropolitan areas, a large increase in Negro purchasing power would cause relatively large amounts of good housing to be added to the ghetto fairly quickly. In other metropolitan areas, where the supply of appropriate housing on the boundaries of the ghetto is less plentiful, rapid peripheral growth would do little to improve Negro housing conditions. But if the social costs of continued peripheral expansion of massive central city ghettos are as high as I believe, these desirable short term improvements in black housing conditions may exact a very high longrun price in adverse impacts on metropolitan growth and development.

Although black Americans remain intensely segregated, there are some indications that increasing numbers of black households are moving to the suburbs (Birch). A full evaluation of these changes and their implications must await a careful analysis of changes over the last decade based on 1970 census data. The limited analyses available suggest that the forces of housing discrimination in a number of metropolitan areas are waning. At the same time, other metropolitan areas, particularly those in the South, may be becoming more segregated. Historically, southern metropolitan areas, particularly older ones, did not exhibit the massive concentration of black households that characterized northern ones. Unfortunately, they appear to be developing patterns of racial segregation similar to those found in large northern metropolitan areas.

Qualitative changes in recent decades in the nature of the forces that maintain housing market segregation provide more basis for optimism. A few years ago, government actively supported and maintained segregated living patterns. The most effective weapons to maintain segregation —for example, racial covenant and FHA mortgage loan policies—are no longer available. Racial discrimination in urban housing markets is now unlawful and the Federal Government and numerous State and local governments have promulgated a number of important regulations that would limit the ability of lenders, brokers, sellers, property owners, and developers to discriminate against minorities. These changes in law and government policy and practice in turn reflect long term trends in the attitudes of the American population toward racial discrimination (Sheatsly). Where a short time ago an individual who would openly discriminate in housing could expect strong and vocal approval from his neighbors, today he may not receive their support and in many communities will feel increasingly the need to hide his actions and motives from his friends and neighbors.

Brokers who once openly refused to serve blacks must now disguise their discriminatory actions. Because of changes in law and community attitudes, brokers are increasingly willing to show property in white neighborhoods to black households.

Because racial prejudice persists and because discriminatory acts in urban housing markets are so difficult to detect and prove, policies that insure that minority households have access to the entire metropolitan housing market on an equal basis with the white majority will be very difficult to formulate. It would be irresponsible to design and implement housing programs and policies that depended on minority access to the entire housing market without a sober evalution of the likelihood of breaching the barriers which currently limit the housing choices of these households. The task is clearly a difficult and demanding one. But it is not hopeless, and the benefits to the entire population of the successful eradication or even significant amelioration of existing discriminatory practices are inestimable.

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Metropolitan Employment Suburbanization as a Rationale for Housing Policy Interventions: A Statement of the Argument and Review of the Evidence

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Introduction

Over the last quarter century, the great bulk of the new metropolitan housing units constructed have been located in the suburban rings that surround the Nation's central cities. These "suburban" rings have come to be characterized by low density, generally newer and more expensive housing occupied, in the main, by more affluent persons; while the inner, "central city" area has come to be characterized by generally older, denser, less expensive housing occupied, in the main, by less affluent persons.

Over the past few years, it has also become increasingly apparent that, in addition to containing most of the new housing, suburban areas are also accounting for an ever increasing fraction of the total metropolitan employment. Coupled with the reputation these suburbs have acquired for providing housing in the main to only the more affluent, white segments of the metropolitan population, this trend has given rise to the following fear: That the movement of jobs to the suburbs has created a geographic mismatch between the location of the metropolitan employment centers and the location of certain of the residents of central cities; and that, as a consequence, the economic well-being of these central city residents is being artificially decreased by their inability to compete effectively for jobs that are available elsewhere.

Those who believe that employment suburbanization is having the impact feared usually suggest as a corrective the adoption of one or more of three types of public policy interventions: [1]

[1] For a list of options almost identical to this one, see Kerner, p. 392–3. See, also, Cassidy, Davidoff, and Kain.

1. Policies aimed at increasing the number of jobs which are "appropriate" for the central city households in question and are located in close proximity to their present residential location.

2. Policies aimed at improving the transportation network connecting central city residential neighborhoods to suburban work places.

3. Policies aimed at facilitating the greater movement of the particular group in question into suburban neighborhoods.

In this paper we are concerned with only the third of these policy intervention types, those policies designed to facilitate the greater movement of the particular central city residents in question into suburban neighborhoods. Our objective is to test proposals for this type of intervention against the evidence currently available; to determine whether or not that evidence suggests that the great movement of these particular central city residents into the suburbs will, in fact, enhance their employment prospects.

The remainder of this paper is divided into three major sections. In the first of these, we shall be examining the assumptions implicit in arguing for the adoption of this particular type of policy. In the second, we shall be examining the evidence currently available to see how accurately these assumptions appear to describe current metropolitan labor and housing markets. And, in the third, we shall draw the public policy conclusions that seem to be justified by the discussions contained in the preceding two sections.[2]

[2] It must be noted that throughout this paper the terms "central city" and "suburban" will be employed as if they described two separate, relatively distinct, and relatively homogeneous portions of a metropolitan area. Obviously, for virtually all purposes, this usage will be, at best, only an approximation.

As far as residential patterns go, by many standards there are neighborhoods in most central cities that would appear more "suburban" than most neighborhoods located in the suburbs, just as there are neighborhoods in the suburbs that would appear more "central cityish" than most portions of the central city. Moreover, in terms of employment location, there are undoubtedly many "central city" locations that are less accessible to the central city poor than are a good number of "suburban" locations. Such might well be the case, for instance, for a person living in the Bronx and facing the choice of working either in "suburban" Yonkers or in Queens Village section of the "central city."

The ideal way to go about studying job location and job accessibility would be to look at which particular locations are accessible and which are not, without regard to their particular location within or outside the boundaries of the central city. Given the present data limitations, however, such a study is not generally possible, so that we are forced to lump all central city locations into one set and all suburban locations into another set and proceed from there.

The Logic of the Argument

The Assumptions Behind the Argument

The argument that policies aimed at facilitating the movement of certain central city residents to the suburbs can be expected to enhance their employment prospects rests on the following five assumptions about current conditions in metropolitan housing and labor markets:

- Assumption (1): That the geographic location of a metropolitan employer affects the ability of at least some metropolitan residents to obtain employment from him; and, specifically, that his location outside of the central city restricts the ability of certain households now living in the central city to gain employment at his firm.
- Assumption (2): That a significant number of the metropolitan jobs these households might want to obtain are now located in the suburbs.
- Assumption (3): That, whatever is the barrier now preventing the particular central city residents in question from competing for jobs in the suburbs, it would not exist if these people occupied suburban residential locations.
- Assumption (4): That these people are now effectively prevented from securing such suburban residences.

And, finally, either:

- Assumption (5a): That, whereas the movement of these persons to the suburbs would remove the barrier which previously prevented them from competing for suburban jobs, it would not at the same time create a similar barrier to their continuing to compete for central city jobs; or
- Assumption (5b): That, relative to its supply in each place, the demand for the kind of labor supplied by the central city poor and minority group households is greater in the suburbs than it is in the central city.

The Necessity of Making These Assumptions

The first of these assumptions concerns barriers that now prevent certain central city residents from competing for suburban jobs. The assumption is necessary because, if there are no such barriers, then it clearly makes no difference where people live or where the jobs are located, and the whole discussion becomes moot.

The traditional assumption about metropolitan areas has always been that they constitute, for all intents and purposes, one labor market.[3] Those who are concerned about the impact of employment suburbanization are implicitly arguing that this traditional assumption is in error, and that certain barriers prevent particular central city residents from competing for suburban jobs.

Let us note two things at this point. First, to be persuasive, the argument requires one to be fairly specific about what the barriers are that he assumes exist. For, as we see in assumptions (3) and (5), in order to argue for the policy in question, it is also necessary to make certain additional assumptions about how the particular barriers will be affected by a move to the suburbs.

Secondly, one may note that the discussion has heretofore been rather vague about just which central city residents are the ones whose employment prospects would be enhanced by a move to the suburbs. That has been intentional, for the proponents of this type of policy intervention do not themselves agree.

I believe that all proponents argue that central city minority group households—and, in particular, blacks—would benefit from the policy intervention. There is some disagreement, however, about whether such intervention is also required on behalf of lower income whites. Some authors are silent on the question;[4] some argue that intervening is required;[5] and some imply that it is not.[6] We shall examine the evidence on possible suburbanization victims in the next section.

The second of the assumptions listed above is that metropolitan employment has, in fact, suburbanized. This assumption has been included in the list solely to give the argument a logical completeness. To the best of my knowledge, this particular assumption is not an issue

[3] This "traditional" assumption lies behind many of the recent econometric studies in labor economics. See, for instance, the literature on labor force participation rates.
This "traditional" assumption is also one of the assumptions upon which the whole concept of "metropolitan area" is built. One of the most important determinants of which community should be linked to which other community in constructing a "metropolitan area" is patterns of intercommunity journeys to work.
None of this should be taken as evidence, though, that this "traditional assumption" necessarily holds for particular central city residents.

[4] See Kain, Kerner, and Mooney.

[5] See ACIR, Burt, Cassidy, Davidoff, and Gooding.

[6] See Kain-Persky.

in the suburbanization debate because nobody argues that employment has not suburbanized.

If one can accept these two assumptions as being accurate descriptions of current conditions in metropolitan labor markets, one can conclude that employment suburbanization may well have harmed the central city residents in question and that policy interventions of the first type—those to increase the fraction of metropolitan jobs that are located in the central city—can have a beneficial impact on the employment prospects of these particular people.[7] To argue for either of the other two types of intervention, however, requires one to make additional assumptions about metropolitan housing and labor markets.

The first of these additional assumptions, and the third of the assumptions listed previously, concerns the particular barrier that now prevents these central city residents from competing for suburban jobs.[8] The assumption is that, whatever this barrier is, it will be removed (or substantially reduced) if the particular central city residents were to live in the suburbs. The assumption is necessary because to the extent the barrier would remain even after such a move, the move itself is not going to do much to improve the access these people have to the suburban jobs, and cannot, therefore, be expected to enhance their employment prospects.

As we shall see, those who have expressed concern with the impact of employment suburbanization have focused on several potential barriers which they feel prevent persons now living in the central city from competing effectively for jobs located in the suburbs. Not all of these hypothesized barriers would be removed if these people were moved to the suburbs, though; and, as a consequence, not all of the persons who have expressed concern about the impact of employment suburbanization have been supporters of this third type of policy intervention.[9]

[7] That is to say that if there is a barrier preventing certain central city residents from competing for jobs located in the suburbs, then employment suburbanization has reduced the number of such jobs for which these central city residents can compete. Thus, by seeking to increase the number of jobs available for these people, policy interventions of the first type may indeed enhance their employment prospects.

[8] The second type of policy intervention, that of improving the transportation system connecting central city residential neighborhoods with suburban work-sites, is predicated on the assumption that this barrier is, purely and simply, transportation availability. To the extent that this is the case, improving the transportation network would then provide access to suburban jobs without diminishing the present access to central city jobs, thereby leading to a definite increase in the jobs potentially available to the central city residents in question.

[9] One example of such a nondisappearing barrier is the lack of public transportation at a suburban worksite. As will be discussed later, it is not clear that a change in the residential location of a given household would do much to remove this barrier.

The fourth assumption is that the particular central city residents in question are, for one reason or another, now effectively prevented from obtaining suburban housing. Obviously, it is necessary to make this assumption in order to argue that some sort of public policy intervention is necessary in order to make such housing available.

In a sense, the thrust of these first four assumptions is that public intervention is called for and that such intervention in the form of encouraging certain central city residents to move to the suburbs can be expected to produce certain employment benefits for them. Specifically, it is assumed that after such a move, these people would be able to acquire jobs which they could not have acquired were they still living in the central city.

It is entirely possible, however, that in the process of moving to the suburbs, these people will lose access to certain of the jobs for which they could previously compete. To the extent that this happens, the move to the suburbs may well be detrimental to their employment prospects. The "cost" in terms of job opportunities lost may exceed the "benefit" of the job opportunities gained.

The fifth assumption is, in essence, a statement to the effect that the benefits of such a move (stated in terms of newly accessible jobs) are greater than are the costs (stated in terms of jobs no longer accessible). It is actually two assumptions, of which only one need hold. Either (1) the move does not prevent these former central city residents from continuing to compete for central city jobs, in which case there is no "cost," so that if there is any benefit, it will be greater than the cost, or (2) relative to the supply of workers in each place, there are more of the types of jobs these people need located in the suburbs, which is to say that there are costs but that the benefits are greater than the costs.

The Particular Lines of Arguments and the Evidence

Aggregate Trends in Metropolitan Job Location

As noted previously, there does not appear to be any dispute about the general trends in employment location. All observers seem to agree that in most metropolitan areas, employment has been growing more rapidly in the suburbs than it has in the central city, with the consequence that the fraction of metropolitan jobs

Table 1. Estimated Average Annual Employment in Six Metropolitan Areas, 1957 and 1967 [1] (000)

Industry	1957 Central City	1957 Suburban Ring	1957 Total	1957 Percent C.C.[5]	1967 Central City	1967 Suburban Ring	1967 Total	1967 Percent C.C.[5]
Agriculture, etc.[2]	3.1	4.2	7.3	42	2.4	8.2	10.6	23
Mining	8.6	7.4	16.0	54	11.2	8.4	19.6	57
Construction	141.4	110.2	251.6	56	133.8	134.0	267.8	50
Manufacturing	759.7	793.7	1553.4	49	705.5	904.8	1610.8	44
Railroads	59.1	22.9	82.0	72	33.3	18.3	51.6	65
Public Utilities [3]	241.1	88.1	329.2	73	232.5	107.9	340.4	68
Wholesale Trade	242.4	63.5	305.9	79	228.1	107.9	336.0	68
Retail Trade	404.9	280.4	685.3	59	383.5	451.7	835.2	46
Finance, etc.[4]	201.0	54.1	255.1	79	224.8	82.1	306.9	73
Services	449.0	199.3	648.3	69	568.5	395.2	963.7	59
Local Government	151.3	144.8	297.9	51	181.1	254.3	435.4	42
State Government	30.0	29.6	59.6	50	59.4	56.8	116.2	51
Federal Government	157.9	66.0	223.9	71	176.8	93.0	269.8	66
TOTAL	2851.3	1864.2	4715.5	60	2940.9	2622.6	5563.5	53
POPULATION	5728.1	7216.0	12944.1	44.2	5546.9	9287.6	14834.5	37.4
JOBS/100 RESIDENTS	49.8	25.8	36.4		53.0	28.2	37.5	

Notes:

[1] The six metropolitan areas covered are Baltimore, Boston, Denver, New Orleans, Philadelphia, and St. Louis.

[2] Includes Agriculture, Mining, and Fisheries.

[3] Includes transportation except railroads.

[4] Includes insurance and real estate.

[5] Percent of total located in central city.

Sources and Procedures:

1. Total metropolitan employment in each industry is the estimate reported in Bureau of Labor Statistics, *Employment and Earnings.*
2. Each industry's employment total was divided between central city and suburb on the basis of an estimate of the fraction of employment in each industry which was located in each place.
3. Estimates of the fraction of employment in each industry located in each place were derived from the following sources: "Railroads" from unpublished data supplied by the Railroad Retirement Board; "State and Local Government" from the Census of Governments, "Federal Government" from unpublished data supplied by the U.S. Civil Service Commission; and all other industries from Bureau of the Census, *County Business Patterns.*
4. Population estimates are geometric interpolations.

that is located in most central cities has declined.[10] The only issue with respect to aggregate trends about which there is any dispute seems to be the question of just how great the difference between the central city and its suburbs has been.[11]

[10] For instance, Rosenthal reports on Census data which show that the central city share of the total employment in the fifteen largest metropolitan areas declined from 63 percent in 1960 to 52.4 percent in 1970. Fairly comprehensive estimates of employment trends in selected large metropolitan areas can also be found in Fremon and Lewis. My own estimates of trends in six large metropolitan areas are shown in Table 1.

[11] There are some rather significant differences among authors in the reported magnitude by which suburban job growth has exceeded central city job growth.

Some of the difference can be ascribed to the completeness with which a given set of employment estimates covers the industrial structure. Earlier studies (e.g., Meyer-Kain-Wohl and Mooney) focused on the more readily available data for the manufacturing and trade sectors; however, later studies suggest that looking only at these sectors tends to overstate the problem, since manufacturing and trade appear to be two of the most extensively suburbanized industries. (See, for instance, my estimates of employment by industry contained in Table 1.)

Another discrepancy recently uncovered is between the estimates generated by the Census Bureau and those generated by either the Bureau of Labor Statistics or the Social Security Administration. The former generates estimates by asking people where they work; the latter two generate estimates by asking employers how many people work for them. For March 1970, the BLS reported some 321,000 more jobs in New York City and 51,000 fewer jobs in the New York suburbs than does the Census Bureau. To my knowledge, nobody has yet adequately explained the reasons for this discrepancy.

Potential Barriers to Suburban Employment

As noted previously, though, justifying any sort of intervention requires more than just proving employment locations have changed. For one thing, it also requires one to assume that there exists some set of forces that now prevents the central city residents in question from competing for jobs in the suburbs.

The suburbanization literature contains several lines of argument in support of the proposition that such forces exist. Though differing in some of the details, these arguments all seem to have two common elements: (1) That, for some reason, the central city residents in question cannot obtain adequate housing in the suburbs; and (2) that without obtaining such suburban housing, they cannot adequately compete for the jobs that are located in the suburbs.

Housing Barriers: There are two factors commonly cited as preventing certain central city residents from obtaining suburban housing. One is racial discrimination, which, it is alleged, prevents blacks of all income levels from moving to the suburbs.[12] The other is "fiscal zoning," a form of economic discrimination, which, it is alleged, keeps poor and working class families of all races out of the suburbs by maintaining artificially high prices on newly constructed housing.[13]

There can be no question about the fact that blacks living in metropolitan America reside, overwhelmingly, in central cities.[14] I also would doubt that anybody would seriously dispute the contention that past and present patterns of racial discrimination have played a major role in producing this pattern. As a consequence, I think it would be difficult for one to take issue with the assumption that blacks have, in general, not been able to gain access to suburban housing as readily as have whites.

The proposition that lower income whites are also denied access to suburban housing is less generally accepted than is the proposition that minority group families are denied such access.

To my knowledge, nobody involved in the suburbanization debate has ever done a very detailed study of suburban housing availability for such lower income whites. The evidence cited in support of the contention that these people are excluded from suburban housing usually consists of either a recitation of a few examples about individual plant moves or a computation of the percentage of the currently vacant land in the New York area that is zoned for single family houses on relatively large lots.[15]

There is one fact, however, which casts considerable doubt on the contention that, in general, lower income whites are not able to secure housing in the suburbs. The fact is that, by and large, a majority of them already live there.

Kain examined the residential location of the white and black poor in the ten largest metropolitan areas, and concluded that:

> . . . the poor are found less frequently in the central city; it is mainly the Negro poor who are found there. The inference is inescapable, *central cities are poor largely because they are black, and not the converse.*[16] (Emphasis in original.)

For my own work, I examined data showing the 1971 residential location of both black and white families living in the 33 largest metropolitan areas. Those data suggest that in 1971, 53 percent of the white families having incomes below $3,000 and 55 percent of the white families having incomes below $8,000 already lived in suburban areas.[17] By comparison, the fraction of all white families that lived in the suburbs was a little less than 65 percent of the total. It may be that there are serious shortages of low or moderate income housing in certain areas, which shortages may prevent some white families from living relatively close to some particular suburban worksite; it may be that there is a general shortage of such housing for whites in the suburbs of a particular metropolitan area; and it may be that in many metropolitan areas there is more of such housing needed everywhere, both in central cities and in suburbs. But this evidence suggests that, as a general proposition, low or moderate income white families can find housing in the suburbs. Therefore, it is far less clear why public policy intervention might be required to correct for the impact of employment suburbanization on those white families.

Barriers Preventing City Residents from Securing Suburban Jobs: The second element of the argument is that without obtaining housing in the suburbs, the particular central city residents in question are at a disadvantage when competing for suburban jobs. There are two general factors which are usually cited as creating this disadvantage: Transportation problems and racial discrimination in employment.

Transportation: It is useful, at this point, to divide the central city population in question into two groups: (1) Those who do not now own an

[12] See Kain.

[13] See, for instance, Cassidy and Davidoff. At least in this regard, "fiscal zoning" refers to requirements that new housing on currently vacant land be on lots of a (large) minimum size or of a minimum aggregate value.

[14] For example, the 1970 Census showed that central cities housed 78 percent of the metropolitan black population. By comparison, they housed only 41 percent of the metropolitan white population.

[15] See, for instance, Cassidy, p. 22.

[16] Kain-Perskey, p. 75.

[17] See Table 2.

Table 2. 1970 Residential Location of Families Living in the Thirty-three Largest Metropolitan Areas (000)

TOTAL 1970 FAMILY INCOME	ALL RACES No. of Families	ALL RACES % in C.C.[1]	WHITE No. of Families	WHITE % in C.C.[1]	NEGRO No. of Families	NEGRO % in C.C.[1]
Less than $3,000	1,038	58.0	711	46.3	299	85.6
$3,000 to $5,999	2,307	55.7	1,763	47.5	503	85.1
$6,000 to $7,999	1,824	48.7	1,483	41.0	311	81.0
$8,000 to $9,999	2,164	43.4	1,786	35.3	276	81.1
$10,000 to $11,999	2,825	39.5	2,097	35.3	246	82.9
$12,000 to $14,999	2,843	34.8	2,765	35.3	223	77.6
$15,000 to $24,999	4,095	32.1	3,822	29.5	244	70.1
$25,000 to $49,999	1,162	30.3	1,212	29.3	37	70.2
$50,000 and over	143	30.8	134	31.2	3	—
TOTAL	17,882	41.0	15,532	35.3	2,145	81.1

Source: 1971 Current Population Survey.
[1] Percent of total located in central city.

automobile, and would find that the purchase of one imposes an unreasonable financial burden, and (2) those who either own an automobile now or could reasonably be expected to be able to afford to purchase one.[18]

Most of those in the first of these two groups, the nonowners, must rely on public transportation in order to get to work. Several authors have argued that current public transportation systems are organized primarily to get workers into and out of the central business district, and that, if they serve suburban worksites at all, they do so so poorly as to make it virtually impossible to use them to get to work there.[19]

As far as I know, nobody has ever taken issue with this argument, and I see no reason why anyone should. Thus, it seems reasonable to conclude that employment suburbanization has, indeed, been detrimental to the employment prospects of those central city residents who cannot commute to work by car.[20] And, further, it seems reasonable to conclude that consideration of policy interventions of either of the first two types—either those to increase aggregate central city employment or those to improve the transportation—is justified.[21]

However, at least with respect to this group of non-automobile-owners, it does not seem reasonable to argue that a movement to the suburbs would be beneficial, since the same inadequacies of public transportation would still prevent these people from having access to suburban jobs; the barrier to their employment would remain after their move. Indeed, since public transit is generally far more adequate in central cities than it is in suburban areas, it would seem that the moving to the suburbs of people who must rely on such public transit would actually be doing them a disservice.

With regard to the second group of central city residents, the group that either now owns or could afford to purchase an automobile, the argument that they do not have access to suburban jobs, is a little more subtle. For this group the argument is that the distance involved in commuting from the central city to the suburbs imposes a cost high enough to make the suburban jobs, for all intents and purposes, unavailable. The subtleness comes in a need to distinguish between residents of the central city and residents of the suburbs, for while it is hypothesized that central city residents cannot commute

[18] One survey of the poor showed that in 1968, 15.4 percent of the poor families headed by white males and 56.6 percent of the poor families headed by black males owned no car. Among families with female heads and children present, 63.2 percent of the poor white families and 90.6 percent of the poor black families had no car. These figures are national averages, and no breakdown by central city or suburbs was available from the source I found them in. See Benus.

[19] See Cassidy, Gooding, and Kain.

[20] Although the conclusion appears logical, I must also report that the only study of this kind of which I am aware found no significant relationship between the unemployment rates for particular groups and the availability of good public transportation. See Benus.

[21] Whether any particular policy having either of these two objectives would, in fact, succeed in enhancing the employment prospects of central city residents is quite another question, and one outside of the scope of this paper. Indeed, several attempts to provide public transportation to suburban worksites have not appeared to have much impact. See Kalachek and Goering.

to the suburbs, there appears to be nothing that is preventing suburban residents from commuting to the central city.

Since the distance of an inbound commuting route is presumably as great as the distance of an outbound commuting route, and the time required for inbound travel is presumably as great (if not greater), the cost of the inbound commuting must be as great as the cost of the outbound commuting. However, it can be argued that this constant commuting cost looms proportionately larger for lower income workers than for higher income workers; and that, as a consequence, it is not a barrier to higher income residents of the suburbs, whereas it is a barrier to lower income residents of the central city. This is the argument which has been made, either explicitly or implicitly, by several of the authors who are concerned about the impact of employment suburbanization.[22]

There is evidence that lower income metropolitan workers do not normally commute as far as do higher income metropolitan workers,[23] and there is also evidence that metropolitan black employment tends to decrease the farther one moves from areas of black housing.[24] None of this evidence necessarily shows that black and/or lower income workers cannot commute further if they must,[25] but it is at least consistent with the argument that the relationship between the costs of automobile transportation and the income of different workers may be a factor which prevents certain central city employees from competing for jobs in the suburbs.

Let us note, however, that to the extent that one is willing to assume that these commuting costs are an effective barrier for these lower income individuals, then wherever the individuals live, they will be restricted in their job search activities to jobs located nearby. Thus, if they live in the central city, they will be able to search for jobs only in the central city; and if they live in the suburbs, they will be able to search for jobs only in the suburbs. We shall see the importance of this in the next section.

Racial Discrimination: It is appropriate here to note that one prominent author has argued that a second factor, racial discrimination by suburban employers, has also worked to prevent greater employment of blacks in the suburbs and to prevent some people from competing for suburban jobs while they are residing in the central city. The argument is made by John Kain, and will be examined in greater detail in the next section.

[22] See Davidoff, Gooding, and Kain.
[23] See, for instance, Rees and Shultz.
[24] See Kain (1968). Kain's work will be examined in more detail in a subsequent section.
[25] For instance, evidence from studies of rural labor markets suggest that blue collar workers are willing to commute extremely long distances, say 50 miles one way, in order to obtain manufacturing jobs.

Supply and Demand for Labor in Central Cities and Their Suburbs

In the discussion thus far, we have seen that there is no reason to dispute the assertion that metropolitan employment has suburbanized. We have also seen that, at least with respect to the black population, the assertion that the population seeking employment has not also been able to suburbanize their residences seems to have validity; but that the validity of the proposition with respect to the lower income white population is far less clear.

I have argued that it is difficult to justify a movement to the suburbs of the residential location of those poor households not now owners of automobiles, since the public transportation networks in most suburbs are far less adequate than those in the central city. And I have also argued that with respect to those families having access to an automobile, the argument that a central city residential location prevents one from competing for a suburban job is, in essence, a two-edged sword. For, if it is accepted, it argues with equal force that residents of the suburbs are prevented from competing for jobs in the central city. Thus, before one can conclude that the employment prospects of these central city automobile owners would be enhanced were they to move to the suburbs, one must show not only that there are jobs in the suburbs, but that, as far as these people are concerned, there are more jobs per resident seeking these jobs in the suburbs than there are in the central city. This is the assertion which we shall now examine.

The data currently available do not allow us to estimate directly either labor demanded in or labor supplied to a particular part of a metropolitan area. Thus, although a good deal of effort has been devoted to analyzing this question, all of it has been spent conducting indirect tests.

Among these indirect tests are the following:

Employment-Population Ratio Calculations: One approach taken by several researchers has been to compare estimates of the employment located in each section of a metropolitan area with the population residing there. In employing this procedure, the researcher is assuming that the demand for labor relative to its supply in each location can be approximated by this employment-population ratio.[26]

Aggregate Ratios: Researchers exploring the ratio between the total employment located in central cities or their suburbs and the total population of each respective metropolitan sector, have found there are more jobs per resident in the central city than in the suburbs. Moreover, they have generally found that trends over time have not caused a significant erosion in the margin held by most central cities.[27]

If one accepts the proposition that residents of one jurisdiction are at a disadvantage, when they must seek employment in another, the greater ratio of aggregate jobs to aggregate population in central cities would suggest that, from the standpoint of finding employment, the most advantageous residential location is in the central city—and, as a consequence, that policies aimed at suburbanizing the poor would not enhance their employment prospects.

Most of the persons who are concerned about the impact of employment suburbanization argue, however, that ratios of aggregate employment to aggregate population do not correctly approximate relative demand for the type of labor supplied by central city poor and black households. They argue that aggregate employment is not a valid proxy for the demand for the labor of these particular central city residents, and that aggregate population is not a valid proxy for the supply of labor to the jobs most appropriate for these people.

Adjustments in Labor Demand Estimates: Several of the authors who are concerned about the impact of employment suburbanization have argued that even though aggregate central city employment may not be falling, there has been a decline in those jobs most "appropriate" for many of the central city's poor and minority group households. Specifically, it has been suggested that central city employment demand has "twisted" in one or both of the following manners: (1) That jobs for women are growing while jobs for men are declining, making it increasingly difficult for central city male family heads to work their way out of poverty; [28] and (2) that, to the extent that central city jobs for men are not declining, those jobs available in the central city are increasingly jobs not appropriate for the particular central city households about which we are concerned, because they are either high wage, white collar jobs requiring a relatively high level of skill or education or because they are unskilled, high turnover, low-paying, dead-end jobs.[29]

Two researchers have addressed this "twist" issue, and, although neither was able to conduct as conclusive a test as one might like, neither found evidence that a "twist" was invalidating the results indicated by a comparison of aggregate employment to aggregate population.

Fremon estimated the skill requirements associated with the net job growth occurring in eight large metropolitan areas between 1965 and 1967, and concluded that the skill requirements associated with new central city jobs were not significantly different from those associated with new suburban jobs.[30]

In my own work, I tried to examine the possibility of a "twist" by dividing all nongovernment employment in six large metropolitan areas according to two attributes: first, whether they were held by a man or a woman, and second, whether they were "appropriate" for relatively low-skilled persons.

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[26] This, in turn, requires the folowing assumptions:

a. That the market segmentation tenet discussed previously does hold, at least with respect to some workers. (Otherwise it would make no sense to compare the number of jobs located in one place only to the number of workers living in that place.)

b. That observed employment represents a valid proxy for the quantity of labor demanded in each location (which is to say that the unobserved unfilled vacancies are everywhere proportional to the observed employment).

c. That in each section of the metropolitan area, the population estimates employed represent a valid proxy for labor supply (which is to say that to the extent adjustments are not made, the distribution of workers by skill type and the labor force participation rates are the same everywhere, and that all workers offer themselves first to local employers).

[27] For instance, Fremon found that jobs had not suburbanized more rapidly than the population in eight of the Nation's largest cities. She found them to contain, on average, 44.8 jobs for each 100 residents in 1959 and 50 jobs for each 100 residents in 1967. My own estimates of 1957 and 1967 employment in six large metropolitan areas showed that the ratio of employment to resident population was significantly higher in central cities than in their suburbs, and that over time the margin held by the central cities was not being eroded. Specifically, they showed the 1957 ratios to be 49.8 jobs per each 100 residents in the central cities and 25.8 jobs per each 100 residents in the suburbs. They showed the 1967 ratios to be 53 jobs per each 100 residents in the central cities and 28.2 jobs per each 100 residents in the suburbs. See Table 1.

[28] See, for instance, Mooney, p. 310.

[29] See, for instance, ACIR, p. 58.

[30] Fremon's estimates were that central cities accounted for 44 percent of the metropolitan increase in all jobs, 41.7 percent of the metropolitan increase in semiskilled jobs, and 41.2 percent of the metropolitan increase in unskilled jobs. Thus, although central city job growth appeared to be slightly more highly concentrated in the more highly skilled jobs, the difference between the trends in all jobs and trends in only the semiskilled or unskilled jobs was not very significant.

Table 3. Persons Finding Employment in Six Major Metropolitan Areas Divided According to Sex and Annual Wages, 1957 and 1967[1] (000)

	1957		1967	
	Central Cities	Suburbs	Central Cities	Suburbs
All Jobs:				
(1) Persons Finding Employment:				
Males	1,809	1,249	1,851	1,673
Females	1,118	644	1,315	1,061
Total	2,927	1,893	3,165	2,734
(2) Ratio: Persons Finding Employment Per 100 Residents of Each Sex:				
Males per 100 males	66.8	36.0	72.6	36.9
Females per 100 females	36.8	16.9	45.4	22.7
Total per 100 residents	51.1	26.2	57.1	29.4
All "Appropriate" Jobs [2]				
(1) Persons Finding Employment:				
Males	977	746	892	839
Females	261	137	492	341
Total	1,238	883	1,384	1,180
(2) Ratio: Persons Finding Employment Per 100 Residents of Each Sex:				
Males per 100 males	36.1	21.5	35.0	18.5
Females per 100 females	8.6	3.6	17.0	7.3
Total per 100 residents	21.6	12.2	25.0	12.7

Notes:

[1] Data applies to the following six metropolitan areas: Baltimore, Boston, Denver, New Orleans, Philadephia and St. Louis. Data excludes government employment.

[2] "Appropriate" jobs are those in which the occupant earned more than the poverty line for a family of four but less than the BLS medium standard budget. All cutoff lines were adjusted across cities and through time for any differences in the cost of living.

Sources and Procedures:

1. Employment totals for each industry in each location and in each metropolitan area were taken from the data standing behind Table 1.
2. These totals were adjusted to produce an estimate of total number of persons finding employment in each place by multiplying them times the national average ratio of persons whose major employment was found in each industry in each year to the average annual employment in each industry in each year.
3. This estimated total number of persons finding employment in each place, in each industry, and in each year were then divided by sex of the occupant and the level of annual earnings he received on the basis of the employment information in the Social Security One Percent Continuous Work History File.
4. Population estimates are geometric interpolations.

To obtain a proxy for the type of employment "appropriate" for the unskilled central city labor force, I excluded two categories of employment from consideration, those jobs in which the occupant earned "too much" and those in which he earned "too little." [31]

My estimates of trends in the metropolitan location of these "appropriate" jobs, divided by the sex of the person holding them, indicated that a twist may well have occurred prior to 1957, for by that time the central cities' share of the "appropriate" jobs for men was somewhat lower than their share of all jobs: Central cities accounted for 60.7 percent of all employment and only 56.7 percent of the "appropriate" jobs for men. Between 1957 and 1967, however, I found no evidence of a continued twist; indeed, it appears that the central cities' share of the "appropriate jobs for men" declined less rapidly than did their share of all jobs. By 1967, the central cities accounted for 51.5 percent of these

[31] "Too much" was defined as being greater than the BLS Medium Standard Budget in each area, about $9,200 a year in 1967. "Too little" was defined as being less than the poverty line for a family of four. Both cutoff lines were adjusted through time by each city's consumer price index. The jobs in which the occupant earned "too much" were excluded on the assumption that their education or skill requirements were greater than those possessed by that segment of the labor force with which the hypothesis is interested; the jobs in which he earned "too little" were excluded because they would not lead the occupant out of poverty.

"appropriate" jobs for men and 53.6 percent of all jobs.

As can be seen from the estimates noted above, the central cities' share of total metropolitan employment did decline in these 10 years, and their share of the "appropriate" jobs for men was smaller than was their share of all jobs. However, when one compares the 1967 ratio of employment to resident population in the central cities to the ratio of employment to resident population in their suburbs, one finds far higher ratios for jobs of all types in the central cities. Thus, central cities housed 35 "appropriate" jobs for men for each 100 resident males, while their suburbs housed only 18.5 such jobs for each 100 resident males. For each 100 resident females, central cities housed 17 "appropriate" jobs for women, and their suburbs housed 7.3 such jobs.

Moreover, because resident population also suburbanized in these 10 years, one finds that the declining central city share of metropolitan employment did not cause an erosion in the margin by which the central city employment-population ratio exceeded the suburban ratio. For instance, between 1957 and 1967, the ratio of "appropriate" jobs for men to resident males declined by 1.1 percentage points in central cities (from 36.1 per 100 in 1957 to 35 per 100 in 1967) and by 3 percentage points in their suburbs (from 21.5 per 100 in 1957 to 18.5 per 100 in 1957).[32]

Adjustments to Labor Supply: A potential criticism of using this employment population ratio as an index of relative labor demand is that the denominator—population—does not accurately describe the quantity of labor being supplied to the "appropriate" jobs located in each place. Specifically, if the type of labor supplied by residents of the suburbs is primarily higher-skilled, then the argument would be that even though there are fewer "appropriate" suburban jobs per capita, there are more "appropriate" suburban jobs per resident supplier of unskilled or semiskilled labor.

In order to test the impact of considering differences in the structure of the central city and suburban resident labor forces, I used 1970 census data to prepare two estimates of the supply of unskilled labor in the central city and suburban areas of the six large metropolitan areas.

The first approximation that I employed to the unskilled labor force residing in each place was the number of persons aged 25 or more who had not graduated from high school. Division of the estimated 1967 number of "appropriate" jobs in each location by the estimated 1970 number of such high school (or earlier) dropouts living in each location produced the following estimated demand-supply relationships: The central cities averaged 1.13 "appropriate" male jobs to each resident male without a high school diploma, while the suburbs averaged .92 "appropriate" jobs for each such resident male; the central cities averaged .52 "appropriate" jobs for women to each resident woman without a high school diploma, while the suburbs averaged .32 "appropriate" jobs for women for each such resident woman.[33]

The second approximation to the unskilled labor force living in each location which I employed was the number of persons aged 16 or more who were either employed in an "unskilled" job or, if unemployed, has last been employed in an "unskilled" occupation.[34] The division of my estimates of 1967 private sector employment in each location by those estimates of the 1970 unskilled labor force living in each location produced the following results: That the central cities averaged an estimated 3.4 "appropriate" jobs for men to each male resident in the "unskilled" labor force, while the suburbs averaged an estimated 2.9 "appropriate" jobs for men for each such male resident; and that the central cities averaged an estimated 2.3 "appropriate" jobs for women for each female resident in the "unskilled" labor force, while their suburbs averaged 1.5 "appropriate" jobs for women for each female resident in the "unskilled" labor force.

Employment-Population Ratios: Summary: The results of the employment-population ratios seem to indicate that, relative to resident labor supply in each place, there were significantly more jobs located in the central cities studied than in their suburbs. The conclusion held even after adjustments were made for whether or not these jobs were "appropriate" for the poor, after the jobs were divided according to whether they were held by men or women, and after resident population was adjusted to reflect only that portion of the resident population of each place that might be considered to be part of the unskilled labor force.

[32] These results are based on data presented in Table 3.

[33] These calculations, as well as those reported next, can be found in Table 4 on the following page.

[34] "Unskilled" occupations included "laborers, except farm," "service workers," and "private household workers."

Table 4. Comparison of Estimated Total Number of "Appropriate" Jobs in 1967 to Various Measures of the 1970 Unskilled Labor Force, Six Major Metropolitan Areas[1] (000)

	Central Cities	Suburbs
(1) "Appropriate" Jobs, 1967		
Held by Males	892.5	839.5
Held by Females	491.8	341.0
Total	1384.3	1180.5
(2) Unskilled Resident Labor Force,1970 [2]		
Males	261.9	316.4
Females	212.2	249.0
Total	474.1	565.4
(3) Ratio: Jobs to Unskilled Resident Labor Force [(1) ÷ (2)]		
For Males	3.41	2.65
For Females	2.32	1.37
Both Sexes	2.92	2.09
(4) Unskilled and Semiskilled Resident Labor Force, 1970 [3]		
Males	657.0	892.6
Females	680.9	951.8
Total	1337.9	1844.4
(5) Ratio: Jobs to Unskilled and Semiskilled Labor Force [(1) ÷ (4)]		
Males	1.36	0.94
Females	0.72	0.36
Total	1.03	1.56
(6) Residents Over Age 25 Without High School Diploma, 1970:		
Males	772.6	1,002.0
Females	946.1	1,121.2
Total	1718.7	2,123.2
(7) Ratio: Jobs to Residents Without High School Diploma [(1) ÷ (6)]		
Males	1.16	0.84
Females	0.52	0.30
Total	0.81	0.56
(8) Family Heads Under Age 65 Living in Poverty, 1970:		
Males	56.4	55.9
Females	79.8	48.4
Total	136.2	104.3
(9) Ratio: Jobs to Poor Family Heads [(1) ÷ (8)]		
Males	15.8	15.0
Females	6.2	7.0
Total	10.2	11.3

Notes:
1. Data apply to Baltimore, Boston, Denver, New Orleans, Philadelphia, and St. Louis. In Boston, all of Suffolk County is considered to be the central city. Data on jobs exclude employment by all governments.
2. Includes those persons employed in or, if unemployed, last employed in the following occupations: Laborer, except farm; Service Worker; and Private Household Worker.
3. Includes, in addition to those in "unskilled" occupations, those persons employed in or, if unemployed, last employed in the following occupations: Operatives and Clerical.

Sources:
Employment Data is that from Table 3.
Labor Force and Poverty Data from *1970 Census of the Population,* General Social and Economic Characteristics.

These calculations suggest, then, that if one's job search is restricted to the jurisdiction in which he lives, he will find more jobs per resident jobseeker in the central city than in the suburbs, and he is, therefore, better off living in the central city.

Wage Relationships: A second way of testing the proposition that there is a greater relative demand for labor in the suburbs is to look at the wage rate paid in the central city and that paid in the suburbs for a given unskilled or semiskilled job.

If, as has been hypothesized, workers would prefer to work (or, because of transportation problems, are better able to work) at locations close to their homes, then we should expect that, at a given wage rate, more workers will offer themselves to employers located in the area having the greatest relative supply of workers, and fewer will offer themselves to employers located in the area having the greatest relative demand. As a consequence, those employers located in the area having the greatest relative demand for labor will have to raise their wages to "bribe" nonresidents into commuting in (or out, as the case may be), while those employers located in the area having the greater relative supply of workers will be able to pay lower wages due to their relative ease in attracting workers.

If, therefore, the demand for labor, relative to its supply, is greater in the suburbs, one would expect that for similar jobs, wages in the areas of labor shortage—suburbs—would exceed wages in the central cities—areas of labor surplus.

In order to conduct a test of such a proposition, Noll compared central city wage rates to suburban wage rates for five different types of retail trade establishments in 30 different metropolitan areas.[35] Of the 129 comparisons he was able to make, he found the central business district wage rate higher in 101 cases and the suburban wage rate higher in 21 cases.[36] He also conducted such a test for 11 types of nondurable manufacturing plants in two metropolitan areas, finding that of the 20 comparisons possible, the central city wage rate was higher in 17 cases.[37] Both of these comparisons would suggest that, relative to supply, the demand for workers at a given wage rate was greater in the central city than in the suburbs.

[35] The five types of establishments examined were automobile dealers, dimestores, shoe stores, restaurants, and women's ready-to-wear stores.
[36] Noll, p. 499.
[37] Ibid, p. 500.

Although undertaken for a different purpose, a second test of this type was conducted by Rees and Shultz in their study of the Chicago labor market. They divided metropolitan Chicago into three zones: The central business district; a "South and East zone" containing the South Chicago Ghetto and the neighboring Hammond-Gary Steel Complex; and a "North West Zone" containing most of the higher income suburbs of Chicago. When they then tried to "explain" statistically the wages of individual workers in Chicago, they found that after controlling for such factors as age, sex, race, experience, occupation, industry, and union status, in most cases workers employed in the North and West Region received lower wages, and those employed in the South and East Region received higher wages. They concluded that:

> The whole wage pattern described by the regional variables might be roughly described as a wage gradient that is lowest in the northwest corner of the Chicago area and highest in the southeast. This gradient is related to the pattern of location of employment and residences, since the North and West region has a heavier concentration of residential neighborhoods and the South and East Region has a heavier concentration of nonresidential areas.[38]

They seem to be saying, then, that relative to the supply of workers, the demand for labor in Chicago is greatest in that portion of the metropolitan area which is located closest to the major ghetto.

Statistical Correlations: A third method that has been employed to answer the question of relative demands for labor in center city and suburb has been to examine various statistical correlations between employment or wage level and job location. Perhaps the two most prominent articles written on the topic of employment suburbanization, those by John Kain and Joe Mooney, both employed this technique, as have several others. All have been addressing the question of the impact of employment suburbanization only with respect to the black population.

Kain's Work: Using 1952 Detroit and 1956 Chicago data, Kain correlated the percentage of black employees working in a given location with two variables: (1) The percentage of the residents in the same location that were black, and (2) the distance in miles between the location in question and the boundary of the nearest ghetto. His results suggested that there was a significant positive relationship between the percentage of black employees working in a given location and the percentage of black residents of that location, signifying, Kain believes, that racial discrimination reduced black employment opportunities in predominantly white neighborhoods (and that discrimination in favor of blacks increases black employment opportunities in predominantly black neighborhoods). They also suggest a significantly negative relationship between the percentage of black employees working in a given location and the distance between that location and the nearest ghetto boundary—a finding, he believes, which shows that blacks cannot compete as effectively for jobs located a long way away from the ghetto.[39]

Kain goes on to assert that these results can be used to show that blacks in Chicago would have had some 9 percent more jobs if their residences were to be spread equally across the metropolitan area rather than concentrated in a few major ghettos. He reaches this conclusion by assuming that the residential location of blacks is altered so that their percentage in any location is equal to their percentage of the total metropolitan population; that the location of jobs is not altered; and that his equation will continue to predict black employment in each location under the altered distribution of resident population.[40]

Kain's results can be (and have been) attacked on two grounds. First, his procedure for estimating aggregate employment under an alternative distribution of residences seems to make the rather strong assumption that nothing affects aggregate black employment except ratios of black to total population, and distances between job location and black residence locations—specifically, that such factors as the number of blacks looking for jobs and the skills they possess have no impact.

Secondly, in addition to the assumption that these two variables are the only two which enter into the determination of aggregate black employment, this procedure also requires one to assume that the Kain equation represents the best possible estimate of the impact that these two variables have. Two authors, while them-

[38] Rees and Shultz, p. 179. Data employed in their study were collected from employers in June 1963.

[39] Kain (1968). These conclusions are based on results such as Kain's Equation (1). That equation is:

$$W = \underset{(10.7)}{9.18} + \underset{(15.6)}{0.458R} - \underset{(4.3)}{0.521d} \qquad R^2 = 0.78$$

Where:
W = Percentage of zone i's workers who are black
R = Percentage of zone I's residents who are black
d = Airline distance in miles to nearest boundary point of a Negro residence area
Numbers in percentages are t-ratios.

[40] By a similar procedure, he estimates that distributing black residences equally across metropolitan Detroit would have led to a 4 percent increase in aggregate employment.

selves disavowing the assumption that these two variables could accurately predict aggregate employment under different distributions of black population, have also questioned the assumption that the Kain formulation is the "best estimate" of their impact.[41] Specifically, they reestimated Kain's equation and found that a slightly different formulation, with the same base data, produced a slightly superior statistical correlation.[42] Further, if one wished to assume that either of these equations could accurately predict the impact of a massive change in black residential patterns on aggregate black employment, these two authors show that their equation produces a result in direct contradiction to the result obtained by Kain. Specifically, they show that the proposed shift to an even distribution of black residences across the metropolitan area would be expected to reduce aggregate black employment in Chicago by some 13 percent.[43]

Employment Rates and Employment Suburbanization: A third statistical study is that undertaken by Mooney.[44] For each of the 25 largest cities, Mooney correlated the fraction of the males and females who were employed and living in predominantly black central city poverty tracts with the metropolitan unemployment rate, a measure of the extent of employment suburbanization and a measure of black access to suburban worksites.[45] His results were consistent with the assertion that employment suburbanization had "harmed" central city blacks (i.e., reduced the fraction of them that were employed), and that greater access to suburban jobs could offset this harm.

Mooney's results do not speak to the question of whether these blacks would be better off living in the suburbs; they speak only to the question of what impact suburbanization has had. Moreover, he himself cautions against expecting too great an impact from changes in access or in the rate of employment suburbanization. For instance, at one point Mooney says:

> . . . the reader should not lose sight of the fact that the size of the coefficient of the unemployment rate is substantially higher than the size of the coefficients for either of the other variables. Thus, although the geographic separation of the central city Negro from the metropolitan fringe areas reduces to some extent his employment opportunities, relative to aggregate demand conditions in a particular metropolitan area . . . , the factor of geographic separation does not seem to be too important.[46]

And at another point, in relationship to demonstration projects aimed at improving the public transit connecting the central city residential neighborhoods to suburban worksites, he says that:

> The preliminary findings of this study would seem to indicate that major increases in total Negro employment should not be expected from these experiments.[47]

Policy Conclusions

We have been examining the evidence relative to whether, in general, we could expect that the employment prospects of certain central city residents would be enhanced by the adoption of policies designed to encourage the greater movement of these particular residents to suburban residential locations.

We have seen that all of the available evidence suggests that metropolitan employment locations have suburbanized. I have argued, however, that the position that policies such as that described above can be expected to enhance employment prospects requires that certain additional assumptions be made about metropolitan housing and labor markets. These include the assumption that those persons cannot now obtain suburban housing; that without obtaining such suburban housing, those now living in the central city cannot adequately compete for jobs in the suburbs, whereas with such housing, they could; and that, relative to its supply, the demand for labor is greater in suburban locations.

Based upon the evidence that was reviewed here, it seems reasonable to conclude that central city blacks have, in general, been denied access to suburban housing; but it is not at all

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[41] See Offner-Saks.

[42] The Offner-Saks formulation added a quadratic term to the "R" (percent of residents that were black) term, justified, they argue, under the assumption that discrimination in favor of blacks in neighborhoods with a high percentage of black residents would cause an unusually high percentage of black employment. The Offner-Saks formulation of Kain's Equation (1) was:

$$\underset{(12.8)}{W = 10.84} + \underset{(0.6)}{0.049R} + \underset{(4.8)}{0.005R^2} - \underset{(5.9)}{0.67d}$$

with the symbols having the same meaning as those appearing in Kain's equation (footnote [39]). Offner-Saks reports that the adjusted coefficient of determination on Kain's equation was .77 and that the adjusted coefficient of determination on their equation was .82.

[43] Offner-Saks claim that their result is not intended to be a prediction of the consequence of complete residential desegregation, but rather to show that predictions such as Kain's are virtually worthless because they are so sensitive to the way in which one formulates the equation.

[44] See Mooney.

[45] The measure of access was the number of central city blacks already working in the suburbs divided by the number of central city blacks working in the central city.

[46] Mooney, p. 308.

[47] Mooney, p. 311.

clear that low or moderate income whites have, in general, also been denied access to such housing. Thus, while the proposition that public sector intervention is required to facilitate the finding of such housing seems justified with respect to central city blacks, it does not seem justified with respect to central city whites.

I have argued that most suburban jobsites are not served by adequate public transit, and that, as a consequence, a public policy of encouraging persons who cannot commute to work by automobile to move to the suburbs makes no sense. Proposals to enhance employment opportunities by encouraging residential suburbanization must then be aimed primarily at those central city residents who either now own or could afford to purchase an automobile.

There is evidence that in metropolitan areas, lower and middle income workers do not, on average, commute as far to work as do higher income workers. It is possible to use this as evidence to support the contention that those central city residents who own automobiles would not want to, or be able to, compete for jobs in the suburbs without having residences there. However, such an argument also requires one to assume that suburban residents would not want to, or be able to, compete for jobs in the central city. Thus, even granting the assumption about the inability of those persons to commute across the city boundary, the question of whether or not a suburban residential location is more advantageous than a central city residential location appears to depend on the question of which location has the most potential jobs relative to its resident jobseekers.

The preponderance of evidence suggests that, relative to resident supply, the demand for virtually all kinds of labor is not greater in the suburbs—that, in fact, it is greater in the central cities than it is in the suburbs. Thus, it would appear that, even if it is granted that certain central city residents cannot now find housing in the suburbs, and even if it is granted that without such housing they cannot now adequately compete for suburban jobs, there is no reason to believe that, as a general proposition, their moving to suburban residential locations would enhance their employment prospects.

The evidence on employment locations suggests that if one assumes that certain residents of one metropolitan jurisdiction are unable to compete effectively for jobs located in the other, then these persons would be worse off living in the suburbs than in the central city. I, for one, do not believe that either. My own feeling is that, with the possible exception of the three or four largest metropolitan areas in the country, persons who commute to work by automobile are perfectly capable of commuting to most major job locations in the metropolitan area, regardless of where they live. As a consequence, my own opinion is that moving such persons into or out of suburban areas would probably have little impact on their employment prospects.

This paper has not taken issue with the assertion that metropolitan employment suburbanization may have had an unfavorable impact on the employment prospects of certain central city residents. It is entirely possible that it has, especially on those residents who do not own automobiles.

This paper has not examined the potential impact on the employment prospects of particular central city residents that other policy options might be expected to have—policy options such as the encouragement of an increase in jobs located in the central city or the improvement of metropolitan public transportation systems. It, therefore, offers no conclusions about their potential.

Much of the analysis contained in this paper relates to housing and labor markets in only a few selected metropolitan areas. I believe that conditions in these areas are representative of conditions in all metropolitan areas, but there may be a few metropolitan areas for which they are not representative. Moreover, much of the analysis is based on data aggregated over an entire suburban area or over an entire central city, and it may be that a suburban "average" does not correctly portray the situation in one particular piece of the suburbs of a particular metropolitan area, or that a central city "average" does not correctly portray the situation in a particular neighborhood of a particular central city.

With this in mind, then, let us carefully state just what we have concluded. This paper has concluded that, as a general proposition based upon the currently available evidence, policies designed to encourage the greater movement of particular central city residents to the suburbs cannot be expected to enhance the employment prospects of these residents.

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A Rationale for Government Intervention in Housing: Impact of Government Nonhousing Policies on the Housing and Mortgage Markets

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Summary

On balance, the nonhousing decisions considered below favor the rich and work against the poor. Not only are the poor at an inherent disadvantage in obtaining housing, but they are handicapped as well by the bulk of the considered nonhousing decisions. The major reason for this relatively favorable treatment of the rich over the poor can be traced directly to the Federal income tax. This situation could only be justifiable, in terms of housing goals, if it could be conclusively shown that the "extra" units constructed by the rich filtered down to the poor. In the absence of such data, it seems reasonable to conclude that, although a higher stock is encouraged by such policies, its overall quality is probably not higher, nor are lower income families benefited. HUD, therefore, with the bulk of its housing policies aimed directly at the poor, finds its efforts frustrated.

Stabilization Policies: There is general agreement that rising interest rates reduce housing starts. Fiscal policy should be improved so that monetary policy can be used in moderation. The investment tax credit probably has little impact on total investment but affects its composition by reducing housing starts and encouraging equipment purchasing. There is growing empirical evidence that strongly suggests that the credit and financial policies of the Federal Government are ineffective in stabilizing housing demand because the demand for housing is only slightly affected by the stock of mortgages.

Federal Tax Policies: The Federal tax laws grant substantial subsidies to homeownership which accrue almost entirely to middle and upper income families. Recent changes in the tax laws have had both positive and negative impacts on housing; the 7-percent investment tax credit reduces housing starts and increases equipment purchases. Adoption of a negative income tax would substantially improve the quality of housing demanded by the poor.

Labor-Manpower Policies: There is substantial agreement that construction unions have been able to maintain higher relative wage rates; eliminating this differential would permanently raise annual housing starts. The impact on housing prices would be insignificant according to one view, but another study indicates that a 1-percent reduction in wages would reduce housing prices by 1.45 percent.

Timber Industry Policies: Even though the industry gets favorable tax treatment, its impact on the housing market is likely to be very small. The impact of the Jones Act is minimal.

Transportation: Subsidization of highways accrues mainly to the nonpoor and contributes to the existence of many suburban local governments.

Urban Renewal: Urban renewal, at best, is neutral in its impacts on housing. Its probable impacts were to reduce the supply of slum housing causing slum relocation and increases in slum rents.

State and Local Governmental Policies: The major impact of these governments on housing is transmitted via the property tax and made worse by the existence of many small local governments within metropolitan areas. Its impact is to constrain the supply of housing and worsen its quality in the central city. The adverse impacts of the property tax are increased because of the current Federal tax treatment of housing-related income and expenditures.

Conceptual Problems

The Federal housing goal is to provide "a decent house and a suitable living environment for every American family." To achieve this goal, 26 million housing units are to be constructed by 1978, 20 million of these are to be provided by the private sector, and 6 million by the public sector. Whether this is a realistic goal or not, its achievement will be affected to a certain extent by governmental decisions that are not related to housing at all. In fact, any governmental decision that adversely affects the supply and demand for housing will make the achievement of this goal less likely.

The multiplicity of Federal goals requires the use of many policy instruments. The manipulation of one set of instruments or policy variables to achieve a certain set of goals may affect another set of goals either adversely or beneficially. This occurs when some second set of goals depends on the values of the first set of instrument variables, some of which are beyond the control of the agency responsible for the second set of goals. If the decisionmakers who attempt to achieve the second set of goals cannot affect the behavior of decisionmakers who control the first set of instruments, then their ability to achieve their stated goals is diminished. This problem is especially hard to resolve unless the sources of conflicts are budgetary in nature. One approach around this problem is to create special purpose agencies in an attempt to insulate and offset the adverse impact of other decisions. The establishment of Federal credit agencies is, perhaps, an example of this.

The creation of mechanisms to resolve these inherent "side effects" is difficult because of so many interactions. Effective management practices, however, require that decisionmakers responsible for, say, housing goals should have some control over the policy variables that affect housing goals, where conflicts arise some method for resolving conflicts at least should be available.

The purpose of this study is to identify these policy variables that influence housing goals and to specify the impacts that nonhousing policies have on those instrument variables and ultimately on the impacts of Federal housing goals.

Federal Government Policies

Stabilization and Credit Policies

The Federal Government has several stabilization goals, the basic two being full employment and price stability. In terms of familiarity or perhaps professional acceptance, the other goals are "adequate" growth and balance of payments equilibrium. Interest rate stability has also been suggested as an appropriate goal. Not all of the above goals are mutually consistent or compatible—the most important being price stability and full employment as reflected by the controversial Phillips curve. To achieve these goals (target variables) requires the manipulation of certain policy instruments such as changes in the rate of change of the money supply, changes in tax rates on provisions of the tax laws, and so on. Thus, the achievement of these multiple stabilization goals requires the use of many policy instruments.

If there were only two goals, price stability and full employment, many different mixes of monetary and fiscal policy could be used to achieve them simultaneously. The selection of the monetary-fiscal mix, however, affects the extent to which other stabilization goals can be achieved. To achieve a given decrease in the unemployment rate, either a "tight" monetary and "loose" fiscal policy can be used, or a "loose" monetary and "tight" fiscal policy. Typically, the first alternative is associated with high or rising interest rates, whereas the second alternative is associated with low or falling interest rates. Concern over the balance of payments would probably lead policymakers to choose the first alternative over the second. In the same way, nonstabilization goals—particularly housing goals—can be affected by the monetary-fiscal mix. To the extent that housing starts are inversely related to interest rates, stabilization policies which affect interest rates will have an impact on the achievement of federal housing goals.

If one accepts the position—as most economists do—that monetary and fiscal policies are both effective in terms of achieving full employment or price stability, then other goals or targets must be considered in choosing the appropriate monetary-fiscal mix, otherwise the mix would not matter.[1] Furthermore, if stabilization policymakers do not consider other objectives, including nonstabilization goals, then other policy instruments will have to be devised to counteract the unfavorable effects of the monetary-fiscal mix. In fact, this is part of the rationale for Federal credit agencies, for policies designed to insulate savings and loan associations from fluctuating interest rates, and so on. The conduct of monetary and fiscal policy requires that nonstabilization goals be the basis for the choice of the monetary-fiscal mix. In particular, the efficient achievement of housing goals, whatever they may be, also requires that the impacts of stabilization policies on housing be considered by the formulators of stabilization policy.

[1] Lags are being ignored here. One of the virtues of monetary policy is that it can be implemented immediately upon recognition that some change in policy is appropriate. Fiscal policy, on the other hand, cannot be implemented as quickly because of the political process involved in changing tax rates and expenditure levels.

One rationale often given for the existence of Federal housing policies is that stabilization policies—especially monetary policies—cause fluctuations in housing starts. A tight monetary policy causes high or increasing interest rates; this reduces availability of mortgages and allegedly causes a reduction in housing starts. A less restrictive monetary policy causes low or decreasing interest rates; this increases the availability of mortgages and, ostensibly, stimulates housing starts. Thus, the residential construction industry bears a more-than-proportional share of the burden of stabilization. This generates wide fluctuations in the residential construction industry that probably raise the cost of housing construction. Thus, the achievement of housing goals is more expensive and less predictable in the presence of such policies.

Of course, this occurs only to the extent that the above is an accurate description of the economy. As will be shown later, there is convincing and growing evidence that this is not an accurate description of the housing and mortgage markets. On both theoretical and empirical grounds, however, there is near-unanimous agreement that there is an inverse relationship between rising interest rates and housing starts; the divergence of views centers primarily on the "transmission mechanism."

In response to the existence of the inverse relationship between rising interest and housing starts, many proposals have been made to guide the formulation of stabilization policies so that housing would be insulated from these adverse affects. Arthur Okun has formulated perhaps the best recent set of stabilization rules.[2] In his framework, full employment and price stability are the basic goals, and the subsidiary economic targets are: (1) The composition of final output, (2) stability of interest rates and asset values, (3) minimizing financial dislocation, (4) balance of payments equilibrium, and (5) adequate growth. The basis for choice of the monetary-fiscal mix to achieve the basic goals rests on the subsidiary economic targets. His rules for stabilization policy are:

1. Monetary policy should follow the middle of the road, i.e., it should be neither too loose nor too tight. Tightness or looseness must be interpreted in terms of interest rates and credit conditions.

2. Fiscal policy should be conducted to avoid either a "tight" or "loose" monetary policy.

3. The fiscal policy variables that should be manipulated first are the timing of new spending or tax programs, but if these do not provide the desired effect, personal income tax rates should be charged.

4. To avoid lasting impacts on future budgets, an expansionary fiscal policy should be temporary and self-terminating.

5. It should be recognized that stabilization policies must be made on the basis of a forecast, but this should not inhibit decisive action when the forecast calls for it.

6. "*Presidents should listen to the advice of their economists on fiscal policy and so should the Congress*"[3] (Emphasis his).

7. "*The makers of monetary policy should be guided by both aggregate quantities and interest rates and by the present and prospective state of aggregate demand; they will serve the Nation best by using fully their capability to make small and prompt adjustments in light of the best current evidence and analysis*"[4] (Emphasis his).

The net effect of following Okun's rules would be to stabilize interest rates within a narrower range than in the past. This would minimize the impact of stabilization policy in those sectors, especially housing, which move inversely to interest rates. To the extent that fluctuations in residential construction are due to fluctuating interest rates, these fluctuations will be minimized. The striking thing about Okun's rules is that they are essentially a reform of fiscal policy and not monetary policy. The usual prescription to minimize the adverse effects of monetary policy is a reformation of monetary policy or an attempt to insulate the adversely affected sectors from the impacts of monetary policy by making monetary policy less potent in those sectors. This approach has led to a proliferation of agencies whose primary task is, in effect, to conduct offsetting monetary operations for the benefit of specific institutions. The Federal Home Loan Bank Board is an example of such an agency. If Okun's approach is correct, it is fiscal policy, not monetary policy, that is long overdue for reform.

[2] Arthur M. Okun, "Rules and Rules for Fiscal and Monetary Policy," *Issues in Fiscal and Monetary Policy: The Eclectic Economist Views the Controversy*, edited by James J. Diamond, (DePaul University, 1971) pp. 51-74.

[3] Ibid., p. 69.

[4] Ibid., p. 71.

The Board of Governors of the Federal Reserve System has also made some recommendations that would help moderate fluctuations in the construction industry.[5] The board recommended a heavier reliance on fiscal policy; that is, of course, consistent with Okun's rules. They also state that improvements in federally sponsored credit agencies, while helpful in the past, probably should not be explored any further. Recommendations to eliminate ceiling rates on FHA-insured and VA-guaranteed loans, as well as encouraging State governments to remove usury ceilings and certain changes in the Federal banking laws, would help to insure more even flows of mortgage funds. Recommendations are also offered to improve the functioning of depository institutions. Their recommendations for improving fiscal policy offer a more active use of the investment tax credit. Recommendations such as Okun's, they state, are not likely to be accepted by Congress. It is argued that outlays on machinery and equipment are large and especially volatile and that if these outlays could be stabilized, their growth in production and employment would also be more stable. Thus the investment tax credit could be lowered when aggregate demand became excessive, or raised when demand became deficient. This would smooth variations in business' external financing so that fluctuations in interest rates and mortgage credit—and fluctuations in housing construction as well—would be minimized. This recommendation clearly depends on the effectiveness of the investment tax credit.

What have studies shown about the efficacy of using the investment tax credit? A simulation study of impacts of the Tax Reform Act of 1969 and the Revenue Act of 1971 shows that the composition of fixed investment is strongly influenced by the investment tax credit.[6] Repeal of the tax credit yields substantial increases in residential construction primarily at the expense of equipment purchases, whereas reinstating the tax credit decreases residential construction. Harberger argues that, because of the savings constraint, tax stimuli cannot increase overall investment in relation to GNP; thus, only the composition of investment will be affected by variations in the investment tax credit.[7] To what extent the recent boom in residential construction is due to the repeal of the investment tax credit is difficult to say, and to what extent housing construction will be adversely affected by its reinstatement is just as difficult to predict.

In light of this evidence, the recent declines in housing starts and the substantial growth in unfilled machine tool orders suggest that the composition of investment is shifting away from housing toward equipment. Thus, flexible use of the investment tax credit may stabilize the individual components of fixed investment, but the choice about the composition will be difficult. In fact, Harberger argues that shifting the composition of investment from housing to any of the other components represents a gain because the marginal productivity of capital in the nonresidential sector is substantially higher than in the residential sector. This is primarily due to the existing tax provisions that substantially subsidize housing. To determine the impacts of a more flexible use of the investment tax credit, more study is required.

One striking feature of residential construction cycles is their persistence both in the United States and other industrial countries. The report of the FRS Board of Governors states: "There is no evidence that short term fluctuations in traditional types of residential construction are moderating with the passage of time." [8] Andrew Stern, in a study which utilized the techniques of spectral analysis, compared residential construction cycles for the periods 1857–1926 and 1901–70 and concluded that there was little evidence that a structural change had occurred, and that the cycles in the two subperiods had essentially the same characteristics even though the financial structure of the 1901–70 period was seemingly stacked in favor of residential construction.[9] He also stated: "Fluctuations in the financial variables do not appear to bear a systematic relationship of any significance with movements in residential construction." [10] According to his analysis, housing is related to demographic variables over the long run, and the cost variables, including the interest rate, in the short run. His financial variables included bank loans and mortgages. O. H. Brownlee argues that

[5] "Ways to Moderate Fluctuations in the Construction of Housing," Report of the Board of Governors of the Federal Reserve System—March 3, 1972. *Federal Reserve Bulletin*, March 1972, pp. 215-25.

[6] Henry J. Aaron, Frank S. Russek, Jr., and Neil M. Singer, "Tax Changes and Composition of Fixed Investment: An Aggregative Simulation," *The Review of Economics and Statistics*, LIV (November 1972), pp. 343–56.

[7] Arnold C. Harberger, Chapter VII of *Tax Incentives and Capital Spending* edited by Gary Fromm, (The Brookings Institution, 1971), pp. 256–69.

[8] Ibid., p. 215.

[9] Andrew Stern, "Fluctuation in Residential Construction: Some Evidence from the Spectral Estimates," *The Review of Economics and Statistics*, LIV (August 1972), pp. 328–32.

[10] Ibid., p. 331.

the interest elasticity of demand for housing is relatively high primarily because of its long life and also indicates that financial constraints have not significant impact on residential construction at least until mid-1967.[11] A recent article by Arcelus and Meltzer,[12] which is bound to be controversial, rejects the view that the availability of mortgages is a primary determinant of housing starts.

It was indicated above that two views are emerging concerning how housing markets are affected by monetary policy. By far the more popular view (the conventional wisdom) is that increasing interest rates reduce the rate at which deposits at mortgage institutions grow, which causes a decrease in the rate at which mortgages increase; this finally causes a decrease in the demand for housing.[13] The policy implications derived from this view are twofold: (1) Monetary policy should steer a middle course, and (2) credit or financial policies that increase the supply of mortgages can be effective in negating the adverse affects of a tight monetary policy or in insulating the housing sector from generally tight credit conditions. It is this view which serves as the rationale for virtually all Federal credit agencies and policies with respect to housing. The major support for this view is the observation that housing starts and the stock of mortgage credit are positively related and that both are negatively related to the interest rate.[14]

An alternative view is that because housing is a durable asset, its interest elasticity is relatively large, so that rising interest rates reduce housing starts, and falling interest rates increase starts.[15] Concomitantly, rising interest rates on securities increase net withdrawals from thrift institutions; this also reduces the rate at which their assets can grow. The policy implications of this view also call for moderation in the conduct of monetary policy, but no credit policies are implied at all; they show that the availability of mortgage credit has little or no effect on the demand for housing.

Huang also finds that housing starts are independent from savings and loan liquidity.[16] Thus, the credit policies of the Federal Government are ineffective, and to the extent that they impose costs and affect interest rates in an adverse way (Kwon and Thornton give evidence to support this view [17]) these policies should be discontinued.

On the basis of the evidence presented by Arcelus and Meltzer, the composition of credit has no impact on residential construction. The basis for their conclusions rests on a three-equation model of the housing market, demand for housing services, and the supply of and demand for housing. Their empirical estimates indicate that the principal determinants of housing starts are relative prices, interest rates, and income and real wealth including equity in homes. The authors fail to find any significant influence of mortgage credit on the demand for housing. The demand for housing starts has an interest elasticity of -1.75, and the interest elasticity of the supply of housing starts is about -2.0. Thus, rising interest rates reduce housing starts, not because of lack of availability of mortgages, but directly because of the interest elasticity of supply and demand functions.

The evidence presented by Arcelus and Meltzer is convincing. Their analysis is corroborated by others and is firmly based upon good economic theory. Their analysis, however, will have to stand the test of professional scrutiny which, we are sure, will be forthcoming. As indicated above, their view, as well as the conventional wisdom, can still be interpreted as implying moderation in the conduct of monetary policy. It does, however, reject Federal credit policies because of their ineffectiveness.

Tax Policies

The provisions of the Federal personal income tax have substantial impacts on the supply of and demand for housing. In fact, the income tax laws probably have an impact on housing that is greater than any other Federal regulations except perhaps those at the Federal Reserve Board. Included in this section is a description

[11] O. H. Brownlee, "The Effects of Monetary and Credit Policies on the Structure of the Economy," *The Journal of Political Economy,* 76, Part II, (July/August 1968), pp. 786–95.

[12] Francisco Arcelus and Allan H. Meltzer, "The Markets for Housing and Housing Services," *Journal of Money Credit and Banking,* V, Part I, (February 1973), pp. 78–99.

[13] Many references could be cited here; some of the more recent and representative ones are: Sherman J. Maisel, "The Effects of Monetary Policy on Expenditures in Specific Sectors of the Economy," *The Journal of Political Economy,* 76, Part II, (July/August 1968), pp. 796–814, and Leo Grebler, "Discussion," *The Journal of Finance,* XXVII (May 1972), pp. 224–26.

[14] Arcelus and Meltzer, p. 79.

[15] This is the approach of Arcelus and Meltzer.

[16] David S. Huang, "Effect of Different Credit Policies on Housing Demand," Irwin Friend (editor), *Study of the Savings and Loan Industry,* (Washington: Federal Home Loan Bank Board, 1969), Vol. III, p. 1236.

[17] Jene K. Kwon and Richard M. Thornton, "The Federal Home Loan Bank and Savings and Loan Associations: An Examination of the Financing of Federal Home Loan Bank Advances," *The Review of Economics and Statistics,* LIV (February 1972), pp. 97–100.

of the favorable benefits to homeownership bestowed by the Internal Revenue Service, an analysis of recent tax changes, and the likely impacts of the negative income tax on housing quality.

Tax advantages accrue to homeowners because (1) imputed rent is not taxed, (2) mortgage interest payments are deductible, and (3) property taxes are deductible. These provisions of the federal personal income tax law mean that for two identical families—except that one is a renter and the other a homeowner—the income tax paid by the homeowner is lower than the income tax paid by the renter. In 1966, the loss in revenue was about $7 billion, assuming unchanged tax rates.[18] However, if tax rates were reduced so that tax collections remained unchanged in 1966, a 12 percent reduction in income tax rates would have been possible. Renters would have gained by the 12 percent reduction in tax rates (assuming no increase in rents due to elimination of tax advantages), whereas homeowners as a group would have lost.

The value of these tax advantages varies directly with tax rates and hence income, i.e., higher incomes and hence higher tax rates make these tax advantages more valuable. Households earning less than $5,000 in 1966 received only about 8 percent of the $7 billion subsidy contained in the income tax loss.

These tax benefits to homeownership have several impacts: (1) They encourage homeownership over renting; (2) they encourage consumption of housing services relative to nonhousing services (20 percent more was demanded in 1966 than would have been in the absence of tax subsidies) [19], and (3) they encourage investment in housing relative to nonhousing. Of course, these incentive effects are directly related to a family's income. Thus, in terms of HUD's concern over the size of the housing stock, these regulations are consistent with this goal. But to the extent that HUD's direct programs focus on lower income families, these tax provisions work contrary to the housing goals of HUD.

Renters do receive a slight break, although indirectly, via income tax laws. Investors in rental property are permitted to deduct depreciation for tax purposes in excess of true rates of depreciation. Taxes are deferred, or rental property is sold for capital gains income that is taxed at a lower rate. If rental markets are competitive, the benefits of excess depreciation will accrue to renters if rents are reduced over time. Capital will also be attracted into rental properties, and more rental housing will be constructed relative to owner-occupied housing. The percentage of reduction in rentals, however, can vary from 0 to almost 20 percent, and it is extremely difficult to estimate with any precision just what these impacts will be.

The Internal Revenue Code thus gives substantial subsidies to housing, most of which accrue to upper income homeowners. In terms of most redistribution goals, it is extremely difficult to justify these subsidies. In terms of housing, if these subsidies were eliminated and the extra tax revenue used to subsidize, in some way, the consumption of housing services by low income familes, this would be a more efficient way of achieving the Nation's housing goals. This would leave the total housing subsidy constant, but the net effect would be to upgrade the quality of the housing stock. To be sure, the quality of housing services demanded by upper income families will fall in the long run, but the quality of that stock would not fall below minimal standards. The quality of the housing stock available to lower income families would certainly rise. The extent to which it would increase depends partly on the form in which housing is subsidized.

Recent changes in Federal income tax laws also have had an impact on housing. The Tax Reform Act of 1969 repealed the 7-percent investment tax credit, disallowed certain forms of accelerated depreciation, increased capital gains rates, tightened recapture provisions on excess depreciation, and introduced a minimum tax on certain incomes. The Revenue Act of 1971 restored the 7-percent investment tax credit in a slightly modified form and permitted businesses to reduce depreciable lives up to 20 percent. Simulating these impacts based on the investment sector of the 1969 FRB-MIT model yielded the following results:

1. The net effect of both changes on housing was negative, i.e., the changes tended to reduce housing starts.

2. Repeal of the investment tax credit favorably affected housing, and its reinstatement adversely affected housing. The impacts were substantial—as high as a 5 percent change in expenditures.

[18] Henry J. Aaron, *Shelter and Subsidies, Who Benefits From Federal Housing Policies?* (Washington, D.C., The Brookings Institution), 1972, pp. 55-56.
[19] Ibid., p. 62.

3. Reducing depreciation allowances shifts the composition of investment from plants to housing.[20]

Thus, changes in tax provisions in the Internal Revenue Code since 1969 have tended to affect housing adversely. These results may be interpeted with some care and should only be considered as very rough approximations. The point is that tax laws are changed and these changes potentially affect housing. Certainly, HUD should involve itself, at least to some extent, in tax changes that adversely affect its housing goals.

Another proposed tax change which has received much attention is the negative income tax. The negative income tax means simply that families earning below some minimum, based on deductions and exemptions, receive a benefit equal to 50 percent of the difference between their income and the minimum. Hugh Nourse has estimated that for 1960 there would have been 857,000 fewer substandard housing units if the negative income tax had been in effect.[21] This amounted to about 8 percent of the substandard stock of housing. Compared to the number of public housing units constructed, this is a substantial figure. Public housing units constructed until about 1968 only amounted to about 850,000 units.

The tax laws are, and could be even more of, a powerful tool to accomplish the Nation's housing objectives. These objectives, however, must also be considered in light of other goals such as equity in taxation and the equitable distribution of income.

Labor and Manpower Policies

There has been increasing interest in wage determination in the construction industry. The size of wage settlements in this industry has been rising more rapidly than for other industries. For example, in 1970 the average wage settlement in construction involved a 15 percent wage increase.[22] Professor D. Quinn Mills [23], in analyzing the determinants of wages in contract construction, has found that a number of factors significantly contribute toward the rise in construction wages. Some of his results are briefly summarized: (1) Wage settlements tended to be higher where demand has been most expansive and supply of construction workers has been most limited; (2) there is a positive influence of strikes on the size of the settlement; (3) unions tend to compete against each other in order to get the highest wage settlement; and (4) the general state of the economy is positively correlated with the magnitude of wage settlements.

Employment in the construction industry is seasonal, uncertain, and cyclical. Unions play a significant role in modifying the uncertainties of construction employment by controlling the supply of labor through the operation of hiring halls and through the apprenticeship system. The ability of unions to achieve monopolistic control over the supply of labor is facilitated by the fact that they are highly organized into 18 major crafts and deal with contractors that are usually small and fragmented into numerous, and often competing, associations.[24] Recently, the Government has attempted, somewhat successfully, to modify the wage effects of the unions' monopolistic-like control of construction labor by initiating the Construction Industry Collective Bargaining Commission and the Construction Industry Stabilization Committee. These organizations apparently had some success in reducing the rate of wage increases and have reduced the number of strikes by 50 percent.[25]

There still remains much to be done. A few improvements in the construction labor market might include the following:

1. Increasing the scope of bargaining to reduce competition for wage increases among crafts and areas.

2. Development of vocational education programs with a strong link to the unions' apprenticeship programs in order to increase the supply of construction labor.

3. Vigorous enforcement of equal employment opportunities, especially for nonwhites seeking to enter apprenticeship programs.

Another factor that affects construction wages is the Davis-Bacon Act. This act specifies that for every Federal construction contract in excess of $2,000, each class of labor will receive, at a minimum, the prevailing or average

[20] Aaron, Russek, and Singer.

[21] Hugh O. Nourse, "The Effect of a Negative Income Tax on the Number of Substandard Housing Units," *Land Economics*, XLVI (November 1970), pp. 435-46.

[22] Report by the Construction Industry Collective Bargaining Commission, October 29, 1970.

[23] "Wage Determination in Contract Construction," *Industrial Relations*, Vol. 10, No. 1, February 1971.

[24] See Michael H. Moskow, "New Initiatives in Public Policy for the Construction Industry," *Proceedings of the Twenty-Fourth Annual Winter Meeting* of the Industrial Research Association, New Orleans, December 1971.

[25] Ibid.

wages in the area.[26] The minimum wage determinations for each area are made by the Labor Department. Perhaps because of limited staffing and a heavy reliance on published union wage scales, the Labor Department's wage determinations have exhibited a large and persistent upward bias. As examples of this bias, Damodar Gujariti [27] has cited numerous cases in which the prevailing wage determinations were inappropriately high. In some cases the rates have been so high that nonunion contractors will not bid on contracts for fear that their employees will resist working for lower wages after the completion of the Federal project. This, of course, increases the appeal of unions to more workers and strengthens the unions' bargaining power. Because of the numerous cases of overestimating the prevailing wage, upward pressure is placed on construction wages. But even if prevailing wages were not overstated, the act would tend to increase wages. Ronald Ehrenberg, Marvin Kosters, and Michael Moskow [28] suggest that the structure of the industry is changed due to the wage inelasticity of the Government's demand. Since the contractor is not legally permitted to pay wages below the "prevailing rate," the employer must sacrifice much bargaining power.

In testing this hypothesis, Ehrenberg, Kosters, and Moskow found that if unionization and construction growth are held constant, an increase in the proportion of publicly financed construction in an area will increase construction wage rates relative to manufacturing wage rates. Furthermore, they find that an increase in the proportion of Federal construction increases apprenticeship wages to a greater extent than the wages of journeymen. This latter effect tends to discourage the use of apprentices on public construction projects.

Although it seems rather certain that the Davis-Bacon Act exerts upward pressure on wage rates and increases the bargaining power of unions, the precise magnitude of the effect is difficult to specify. Some preliminary results are available from Ehrenberg, Kosters, and Moskow, however. They regress relative wages of unionized construction workers on the extent of unionization in nonresidential construction, on the proportion of nonresidential construction which is publicly supported, and on a measure of growth in the construction industry. Although the authors caution the readers about implications to be drawn, their results are interesting. They find that when the proportion of publicly supported construction increased by 1 percent, the relative wage rates increased by 0.68 percent. This type of relationship between wages and publicly financed construction could seriously inhibit the benefits of governmental participation in the housing industry.

One would suspect that the monopolistic practices of unions and the Davis-Bacon Act, by increasing relative construction wages, will have the effect of limiting the supply of housing and increasing the price of housing services. Theoretically, the effects of high wages will be greater the less the elasticity of factor-substitution in the construction industry.

Before considering the effects of wages on housing prices, we will make a brief digression to consider the housing market. At any point in time, there is an existing stock of houses that yields housing services. In the short run, these housing services are fixed, and their price is determined by demand.[29] This stock of housing is influenced, in the long run, by the annual volume of new construction, which is approximately 3 percent of existing stock. The dominant forces in explaining the price of housing services are the existing stock and the demand for the stock. Since purchasers of housing services may opt for either new housing or existing housing (because the stock of housing and the flow of new housing are close substitutes), the two markets are integrally related.

For example, if demand for housing services increases, rental prices rise. This increase in rent encourages the consumer to purchase new houses (a close substitute), and the higher prices of new houses encourage an increased supply of this product. The increase in supply of houses adds to the stock of existing homes and thus offsets part of the initial increase in rental prices. Any consideration of the effects of unions on the housing market should attempt, therefore, to include estimates of their impact on the cost of new houses, the supply of new houses, and rental rates for housing services.

Recent empirical estimates of the effect of increases in wages on the cost of new houses suggest that labor costs are presently much less

[26] The discussion of the Davis-Bacon Act relies heavily on John P. Gould's "Davis-Bacon Act: The Economics of Prevailing Wage Laws," American Enterprise Institute, Special Analysis Number 15, November 1971.

[27] "The Economics of the Davis-Bacon Act," *Journal of Business*, Vol. 40, July 1967, pp. 303-16.

[28] This is an unpublished paper referred to by Gould, op. cit.

[29] See Richard F. Muth, "The Demand for Non-Farm Housing," in Harberger (ed.), *The Demand for Durable Goods*, Chicago: University of Chicago Press, 1960, pp. 29-96.

influential than they were 15–20 years ago. Joseph T. Finn,[30] for example, shows that onsite man-hours per $1,000 of contract cost have declined by more than 2 percent annually over the period 1960–68. Sara Behman and Donald Codella [31] show that the importance of carpenters' wage rates (used as a proxy for labor costs) has declined significantly over the period from 1950 to 1967. Their findings suggest that in 1950, labor costs had a significant effect on housing costs and that this effect was about two-thirds that of the land cost or site cost. For 1967, levels of wage rates did not account for differences in final house prices, suggesting that the influence of labor costs was virtually zero.

Francisco Arcelus and Allen Meltzer [32] also calculated the effects of wages on prices and supply of housing services. Using a system of equations to explain the demand for housing services and supply of new housing, the authors conclude that their data cannot be used to support any generalizations about the effect of labor union monopolies on the relative price of housing. They argue, however, that their equations do provide a basis for distinguishing some of the factors affecting housing prices if one is willing to make some assumptions. Assuming that (1) real wages of construction workers are entirely a result of productivity changes and increases in the unions' monopoly power, (2) that all increases in wages due to monopoly power increase the relative price of housing, and (3) that all increases in labor productivity in homebuilding either increase the quality or reduce the relative price of housing, they conclude the following:

> A 1 percent increase in the real wage of construction workers has much less effect on housing starts and rental prices than on the index of housing prices. Equilibrium housing starts decline 0.06 percent and rental prices rise 0.13 percent with each percentage point increase in real wages. Housing prices increase by 1.45 percent.[33]

There is obviously some difference in the estimates of the effects of wages on housing prices. It is beyond the scope of this report to determine which estimate is more accurate, but it is informative to note that the Arcelus and Meltzer estimates include all types of housing, whereas the Behman and Codella estimates include only single family dwellings.

We might conclude that wage rates may contribute toward higher rental and new housing prices while limiting housing supply. Using the Arcelus and Meltzer estimates, a reduction in real wages of 5 percent, due to the repeal of the Davis-Bacon Act or to some reduction of labor costs in the housing industry, would lead to an increase of 3 percent in the supply of new housing, a .65 percent decrease in real rental prices, and a decrease of 7.25 percent in housing prices.

One potential determinant of housing prices not previously referred to in this report is land or site costs. According to the President's Committee on Urban Housing (The Kaiser Committee),[34] and the work by Behman and Codella cited above, land cost has been a key variable in the rising prices of new homes. In each of 4 years studied (1950, 1955, 1960, 1967) the site price was the most influential variable accounting for interarea house price differences. Through the time period from 1950–1967, the site cost variable became more influential in explaining price differences.

Policies Related to the Timber Industry

Through forest and transportation policies, the Federal Government has had some effect on the timber industry. Because this industry is a supplier of an important input in the production of housing, some of these effects will be analyzed. The three significant areas to be considered are: (1) The Federal tax treatment of the industry, (2) the Jones Act as it affects the transport of timber, and (3) other transportation policies that influence the industry.

The Federal tax system's treatment of the timber industry extends a subsidy to the industry. The tax subsidy consists of three components: (1) The capital gains treatment of income derived from the increase in the value of standing timber, (2) the overstatement of costs charged against ordinary income, and (3) the conversion of ordinary income into capital gains.[35]

As a result of the tax laws, virtually any income derived from the increase in the value of

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[30] "Labor Requirements for Public Housing," *Monthly Labor Review,* April 1972, pp. 40-42.

[31] "Wage Rates and Housing Prices," *Industrial Relations,* Vol. 10, No. 1, February 1971, pp. 86-104.

[32] Ibid., pp. 78-99.

[33] Ibid., p. 96.

[34] *The Report of the President's Committee on Urban Housing: A Decent Home,* Washington, D. C.: U. S. Government Printing Office, 1969.

[35] See Emil M. Sunley, Jr., "The Federal Tax Subsidy of the Timber Industry," In *The Economics of Federal Subsidy Programs, Part 3,* U. S. Joint Economic Committee, G.P.O., July 1972, pp. 317-342 and Walter J. Mead, "Effects of Capital Gains Taxation on the Timber Industry," *Proceedings of the Fifty-Eighth Annual Conference on Taxation,* National Tax Association, New Orleans, 1965, pp. 342-360.

standing timber qualifies for the preferential capital gains tax rate. A second feature of the tax laws allows the timber industry to apply many expenses of growing timber against current income rather than against income derived from the increase in the value of standing timber. The effect of this mismatching of income and expenses is to underestimate current income (which is taxed at the higher rate) and to overstate income that qualifies for the lower capital gains tax.

Together, these three components of the timber tax subsidy lead to significantly higher rates of return in the industry. A second consequence of the tax law is to encourage more integrated timber industry ownership. In order to take maximum advantage of the income-shifting potential arising out of mismatching income and expenses, the firm must have a stable and sizable income from sources other than capital gains. The tax treatment, therefore, encourages the formation of larger firms and influences the structure of the industry toward a more oligopolistic and less competitive product markets. In this sense, the subsidy would tend to limit supply and raise the price of timber.

On the other hand, increased profits in the industry encourage more capital investments and thus stimulate more intensive and extensive forest land use. Increased profits, therefore, have the effect of increasing supply and reducing the price of timber products. According to Emil M. Sunley,[36] the tax subsidy is expected to reduce Federal revenues by $130 to $140 million per year, an amount equal to one-fourth of the Federal Government's direct subsidies to the industry. The difference between the two subsidy programs is that the tax subsidy accrues to large, integrated firms, whereas the direct subsidies accrue to small timber owners.

It is difficult to calculate the effects of the tax subsidy on housing prices. As an extreme overestimate of the effects, one can assume that all subsidies to the industry are realized in lower housing costs. Using this assumption, Sunley estimates that the tax treatment of the timber industry reduces the price of housing by less than .5 percent. Using the same extreme assumptions, we find that all subsidy programs reduce housing prices by approximately 12 percent, at the most. In reality, of course, it is doubtful that all subsidies are passed on to the consumers of timber products—much less to the consumers of housing services.

[36] Op. cit., p. 317.

A second governmental policy affecting the timber industry centers on the Jones Act. This act limits the water shipment of timber produced in the United States to carriers under the jurisdiction of the Interstate Commerce Commission (ICC). Published rates applicable to firms affected by the Jones Act were equivalent to $27 per thousand board feet.[37] However, firms not under ICC regulation (the relevant firms in our case are located primarily in British Columbia) pay approximately $10 per thousand board feet less than U.S. water transportation rates. The higher shipping rates paid by U.S. firms give Canadian firms an obvious advantage in shipping and marketing timber products. This advantage explains, in part, why 70 percent of timber purchased in the Northeast (the major destination of timber shipped from the west coast by water) comes from Canadian firms.

Our immediate interest is the effect of the ICC regulation of timber shipped by water on the housing market. To estimate this effect, consider the following: Water transportation accounts for twice the amount of lumber shipped from British Columbia coastal mills to the Northeast, Southern, and Western States than by other modes of transportation. If American firms, given the same water rates as British Columbian firms, used water transport in the same two-to-one ratio, they would have shipped, in 1970, 5.4 billion board feet by water and 2.7 billion board feet by other modes. If it is assumed that rates would be reduced by $10 per thousand board feet, and the total amount were passed on in the form of reduced timber product prices, total savings would be $54 million. Once again we use the extreme assumption that the entirety of these savings would accrue to the housing market in the form of reduced prices. The $54 million reduction accounts for between .1 and .2 percent of total expenditures on new housing. Although these estimates overestimate the influence of timber policy on the price of housing, the effects are still very small. If the trend towards multiple dwellings and mobile homes continues, the influence of timber costs on the housing market will be even smaller.

An implicit assumption of the above estimates is that the supply of timber products is constant; however, there are Governmental policies which affect this supply. Because more than

[37] The numbers referring to the Jones Act and shipment of timber by water are taken from a Department of Transportation memo for the CEA Interagency Committee on Lumber and Plywood, entitled "Transportation and West Coast Lumber Availability," April 6, 1971.

22 percent of the total supply of softwood timber is taken from national forests, policy affecting the Forest Service, which manages national forest, will affect total supply of timber produced and delivered to the market.[38] In addition to pressures from environmental and conservation groups (e.g., the Sierra Club) to alter the method of cutting timber and limit the total cut of timber, the Forest Service faces a severe limitation of funds. Although private firms pay for the timber cut—$321 million in 1971—almost all of it goes to the Federal Government's general funds, not to the Forest Service. The result is that as the cost of cutting timber increases, the Forest Service, which faces limited budgets and is little affected by the revenues it generates, must reduce the amount of timber it sells. In 1970, for example, the sale of timber was down by about 8 percent from the previous year.

Transportation policies also affect the amount and cost of timber placed on the market. Perhaps the two most influential factors are the shortage of rail cars and the difficulty of truckers in obtaining "authority" to haul timber as part of a return trip from the east coast to the west coast.

Rail car shortages, even under normal operations, have been a persistent problem, according to C. R. Allenwood of the American Plywood Association. These problems have been exacerbated recently by the increase in demand for cars as a result of huge shipments of grain to foreign countries. Other factors that have aggravated the problem are the collapse of Penn Central and the bankruptcy of five other northeast lines. In addition, rail car manufacturers have delayed producing large quantities of cars because of anticipation of the passage of Federal legislation to finance the production of railroad equipment.[39] This legislation is still pending in Congress. Some of these problems are temporary and should dissipate as the supply of cars increases. But a general shortage of railroad cars, if it exists, is a symptom of some failure of the market or regulatory bodies in allocating resources.

A second problem faced by the timber industry is the difficulty experienced by truckers in obtaining ICC authority to haul timber on the return from a trip which originates in the East and involves another commodity. To send back empty trucks from the West to the East is an obvious waste of resources.

Finally, the timber industry faces some problems in transporting timber products because of limitations on the width of trucks. Many products are commonly cut in 4-foot by 8-foot sheets. The maximum width of trucks permitted by the Federal Government is 8 feet, leaving approximately 7′8″ in a covered trailer for the commodities shipped. Obviously, to increase the width by 6 to 7 inches would greatly facilitate transport by truck. Since size regulations were set over 25 years ago, it is possible that our present highway system could accommodate wider trucks. It seems that this regulation deserves some attention.

Lacking empirical estimates on the severity of the aforementioned problems and the price elasticities of demand and supply for timber products used in the housing industry, it is difficult to predict the effects of these policies on the housing markets. On the one hand, they may partially explain the substitution of other inputs for lumber in the construction industry. On the other hand, these effects may be rather insignificant because of the trend to substitute other materials for lumber.

Transportation Policies

The availability of transportation facilities has had a significant effect on the spatial patterns of economic development. As such it has influenced land and housing markets. The single most important type of transportation is commuting—that is, the transportation of people for the exchange of labor services. This section will center on the impact of transportation's policies (especially policies affecting commuting) on the housing market.

To a very large extent, the supply of transportation is a responsibility of the public sector. Streets and highways are constructed and maintained by public agencies. Public transportation is usually owned or regulated by governments. However, the demand for transportation services is basically private in nature, and the consumer, in maximizing his welfare, chooses among different modes of transportation. But since supply is controlled by the public sector, governments through public policy affect the consumers' choice concerning the preferred mode of transportation.

It is rather clear that the popularity of auto travel has increased significantly over the last several decades. From 1940 to 1967, for exam-

[38] See "The Timber Industry's Struggle for Wood," *Business Week*, November 25, 1972.
[39] See "Freight Car Shortage," *Barron's*, May 7, 1973.

ple, urban auto travel more than tripled, but use of public transportation declined. The substitution of public transit for automobiles can be explained by improvements in auto travel and a growing preference for its convenience. An additional explanation of the increasing popularity of the auto is based on the underpricing of automobile services.

The most serious case of underpricing occurs on congested roads. Alan Walters [40] has argued that at some point the number of cars on a stretch of highway will be large enough so that when another vehicle uses the same section of the road, all cars must slow down in order to maintain the same degree of safety. The entry of this last car increases the cost for all drivers (if time is considered a costly input of transportation) because it has necessitated reduced speeds for everyone. Thus the average cost of travel has increased for everyone and each driver assumes the cost. If average cost is increasing, marginal cost must be greater than average costs.

Since all drivers perceive only their own costs (equal to the average cost), the number of users of the road can be illustrated by the intersection of the demand curve for auto services and the average cost curve. According to traditional price theory, this allocation represents an inefficient use of resources in that too many people use the road. Efficient use of the road would be at the intersection of the demand curve with the marginal cost curve. William Vickrey [41] has estimated that during rush hours the marginal cost to all drivers on an expressway is 4.3 times the average cost incurred by the driver imposing those costs.

These external costs (the difference between marginal and average costs) that an additional driver creates are also imposed on public transit if public transit utilizes the same roads as the auto. The most familiar type of public transit so affected is the bus.

Auto transportation also is underpriced in the sense that it contributes to air and noise pollution—costs not fully borne by the drivers but imposed in part on city residents. The construction of highways creates additional costs when it removes land from tax rolls. To maintain tax yields, the remaining property owners must bear higher tax burdens.

Another factor contributing to the inefficient pricing of automobile transportation is the pricing of parking facilities. Parking officials often see their duties as making parking facilities as abundant and as cheap as possible. Even if these policies are not followed—but parking officials seek to maximize profit or simply break even—little thought is given to coordination of parking with transportation. Municipal parking areas remove land from tax rolls and compete with housing for use of available space. The usual practice is to ignore social costs created by the auto; this further exacerbates the underpricing problem of auto transportation. Thus a large cost element (e.g., parking spaces, traffic signals, etc.) of transportation is not incurred by the individual commuter. Although there are no precise estimates of these costs borne by society over and above the costs borne by individual commuters, William Vickrey has estimated that in Washington, D.C., the societal cost is $25,000 for each additional car entering the center city during rush hour. At 250 round trips per year, the carrying charges on such an investment equal approximately $3 per round trip for each auto, or, on a 1-year basis, $9 per round trip.[42]

The underpricing of automobile travel has encouraged greater use of the car and has facilitated the movement of households to the suburbs. Thus subsidies to automobile travel encourage the consumer to forsake public transit and drive his own car. But the effects are cumulative, for public transit is severely damaged by heavily subsidized competition, and in the long run by the fostering of a land use pattern too dispersed for mass transit to serve.

The immediate effects on the housing market are summarized below. First, the construction of roads, which use increasingly more valuable land as road systems are expanded, competes with housing for available land. Because of this effect alone, the reduction of the amount available for housing increases the price of land and the cost of housing services. On the other hand, expansion of highway systems facilitates the dispersion of the population and of firms in the city, and thus reduces the demand for land and housing services in the city. This decrease in the demand for land and housing in the center city (and a concomitant increase of demand in the suburbs) reduces rents in the center city and creates a flatter rent gradient curve.

[40] "The Theory of Measurement of Private and Social Costs of Highway Congestion," *Economica*, October 1961.
[41] "Pricing in Urban and Suburban Transport," *American Economic Review*, Vol. 53, May 1963, pp. 452-465.

[42] Ibid.

Although the effects of an expansion of roads is not obvious with respect to housing prices, there are two effects which are almost certain to materialize. First, public transit will suffer. Second, those families that commute by car will benefit from low-priced auto transportation, but families without a car will not be able to take advantage of the subsidy. To a large extent, the low income family is not able to purchase cars. Thus they are not able to receive the transportation subsidy and also suffer because of the diminution of public transit services caused by highway subsidies. If families without cars had access to better transportation systems, it is likely that the population would become even more dispersed and that the rent gradient would be even flatter.

It should also be noted that mass transit systems now being planned are designed to bring persons from suburbia to the central city rather than bring central city residents to the suburbs. In addition, it is clear that suburban bus systems are planning to bring suburban residents to line haul stations and not to bring central city resident from line haul stations to suburban employment centers.

It has been shown that while underpriced auto transportation may not increase the absolute cost of housing service in the city, the benefits of this pricing system accrue to higher income households rather than to low income households. One obvious method of dealing with the underpriced transportation problem is to set a price of auto services equal to the longrun marginal cost. Since highways are increasing-cost industries, transportation authorities could make a profit from auto user fees. Public transit, on the other hand, is less subject to peak-hour congestion and, because of very high initial capital costs, may be a decreasing-cost industry. Therefore, to set a price equal to marginal cost for public transit would create losses. One solution might be to price both types at marginal cost and use the profits from the highway program to offset losses from public transit.

It is likely that the policymaker does not have jurisdiction over transportation pricing. Although housing policies may not have any significant effect on the consumers' choice of transportation, it can compensate those subgroups which receive relatively few benefits from subsidies to auto transportation. Such policies might include housing subsidies based on income. Ideally, the subsidy would take the form of a lump-sum transfer payment and be granted to individuals for the purpose of purchasing housing services, but not contingent on consuming any particular amount of housing. These payments should be based on income rather than the availability of private or public transportation. To grant subsidies based on distance from transportation lines, or on the condition that the individual owns no car, may act as an inducement for him to remain in his present location or refrain from purchasing a car. Inducements of this type could be counterproductive by creating an artificial immobility of households from the center city to other areas, or by lowering a certain subgroup's demand for automobiles.

Urban Renewal

The Federal urban renewal program, started in 1949 and greatly expanded in the 1960's, has become the most ambitious effort (and perhaps the most controversial) to eliminate central city slums and decay. A large part of this program has been devoted to the improvement of slum conditions. In this section the discussion of urban renewal will be limited to the slum removal aspect of urban renewal.

In Jerome Rothenberg's [43] excellent study of urban renewal, a detailed categorization of the benefits generated by urban renewal is presented. According to Rothenberg, the elimination of slums may produce benefits in the following three ways:

1. Internalization of externalities will occur —because of the effects on the property value of other homes in the neighborhood—when a homeowner improves the value of his own property. If an individual rehabilitates his property while his neighbors fail to do so, the increase in the value of his property will be modest because the improved property is surrounded by blight. However, his neighbors will benefit to some extent from the improvements to his property. If all propertyowners invest in improvements, the returns to the investment will be considerably higher. Internalization of benefits occurs when the local urban renewal agency acquires all the property in an area, razes the existing structures, and resells the land to the highest bidder. The value of the internalized externalities is measured by the change in the value of land between acquisition and resale.

[43] *Economic Evaluation of Urban Renewal,* The Brookings Institution, Washington, D. C., 1967.

2. As a result of the internalization of externalities, there may be spillovers to land adjacent to the project area. These benefits are also measured by the change in the value of land so affected.

3. Reductions of social costs such as crime prevention, fire departments, and health services which are generated by slums can be considered benefits.

With respect to the first two benefits, Stephen Messner[44] found that changes in land values in and near the project area did not equal the dollar costs of the project. Rothenberg also concluded that in the three cases for which he presents data, changes in the value of land are less than the cost of the project.

More recently, John Weicher[45] has measured the benefits of a Chicago urban renewal project as it relates to the third category of benefits. He concludes that the reduction in slum-generated social costs accounts for approximately 8 percent of the project costs.

Given these admittedly sketchy empirical results, it appears that urban renewal cannot be justified using a cost-benefit calculus. It may be justifiable on redistributive grounds, however. That is to say, urban renewal projects may be justifiable if they are successful in providing improved housing services for the poor. But evidence suggests that urban renewal has not improved conditions for the poor; rather, it has had the opposite effect.

The reasons for this perverse effect can be stated rather simply. Physical removal of urban blight has all too often been substituted for the solution of the problem. Families with low incomes require inexpensive housing; they buy or rent blighted housing because it is inexpensive. Typical urban renewal projects improve the average quality of housing by destroying substandard dwellings and thus reduce the supply of this type of housing that the poor commonly purchase. With a decrease in supply (and no change in demand) the price of housing services will increase for the poor. The poor will not benefit even if a large proportion of those displaced find standard alternative housing. The fact that the poor who are displaced by urban renewal did not move until coerced reveals that renewal made them worse off.

Furthermore, improvements in the quality of housing services are likely to be short-lived. Edgar Olsen[46] argues that slum clearance and urban renewal merely shift the location of slums rather than reduce the number of slums. If markets are competitive, Olsen argues, owners of near-blighted housing can profit by renting their property to low income households by reducing maintenance costs. Through lack of maintenance, more substandard dwellings are created in different locations.

Another defense of urban renewal is that it attracts middle income residents back into the city. But the program attempts to make them move to the central city by providing them with publicly subsidized services which are large relative to the taxes they pay. As Edwin S. Mills[47] has stated: "If removal does not alter the proportion of public services and taxes, they will not come. But if it does alter the proportion enough to attract middle-income people, they will be a liability rather than an asset to the city government."

Mills, in commenting further, explains that one reason the projects lose money is ". . . that the public sector decides the uses to which cleared sites should be put. . . . Selling sites to highest bidders would reduce the losses to the public sector on renewal projects. If it were felt that certain institutions, such as hospitals, deserve public subsidy, it should be given to them directly so they could use it either to bid on renewal sites or for other purposes, whichever best suits their needs."[48]

Some of the failing of urban renewal in its goal to provide a decent house for all Americans is caused by the municipalities' desire to seek the return of middle and high income families from the suburbs. But this represents a fundamental conflict between national and municipal goals. There seems to be some confusion as to whether the public purpose of a clearance project is the removal of blight and slums, as specified by Congress, or the creation of a new use. Clearer guidelines and more specifically stated goals on the part of municipalities could alleviate some of these problems. It now appears that one of the unstated purposes of renewal programs is to inhibit large capital losses on downtown properties that would have occurred. These losses have been transferred from the

[44] "Urban Renewal In Indianapolis: A Benefit-Cost Analysis," *Journal of Regional Science*, Vol. 8, No. 1, Winter 1968, pp. 145–58.

[45] "The Effect of Urban Renewal on Municipal Service Expenditures," *Journal of Political Economy*, Vol. 80, No. 1, January/February 1972, pp. 86-101.

[46] "A Competitive Theory of the Housing Market," *American Economic Review*, Vol. 59, September 1969, pp. 612–622.

[47] *Urban Economics*, Scott, Foresman and Company, Glenview, Ill., p. 188.

[48] Ibid., pp. 188-89.

propertyowner to the public sector and hence to the general taxpayer. Whether one feels it is justified depends on his attitude toward the redistribution question.

Given past shortcomings of renewal programs and effects which have created greater hardships for the less affluent residents of the city, the future of the program should be carefully considered. Since the Housing and Urban Development Bill of 1965, greater emphasis has been placed on rehousing the poor. But any slum renewal program is doomed to fail if it does not increase the ability of the poor to purchase better quality housing. Unless the housing demand of the poor increases, propertyowners will, rightly or wrongly, limit maintenance of housing until the owner's capital investment is commensurate with the rent received from the poor. Thus it is imperative to link renewal programs closely with rental subsidies for the poor, or with other income maintenance programs.

The danger of dismembering the renewal program may be as great as that of continuing programs as conceived and administered during the 1960's. For example, those who feel that urban renewal should be oriented toward housing (and this view seems to be correct) conclude that downtown renewal should be stopped. But, as many have argued, the downtown section must be vital—if not for economic reasons, then for social or cultural reasons. Even severe critics of urban renewal recognize the potential for downtown development.[49] But to accomplish these objectives, more careful attention must be given to market forces as they pertain to the income constraints of the poor and the best use (in most cases, the use to which the highest bidder would put the property) of cleared property.

The new-town approach is another concept which has received considerable attention as a tool to improve housing and the general life style of Americans. The Housing and Urban Development Act of 1970 envisioned new communities as one device for achieving a more "balanced" growth, which would in turn "preserve and enhance both the natural and urban environment." There are presently four types of new towns—independent, satellite, peripheral, and in-town—recognized by HUD as eligible for various kinds of Federal assistance.[50]

[49] See, for example, Raymond Vernon, *The Myth and Reality of Our Urban Problems*, Joint Center for Urban Studies of M.I.T. and Harvard University, Cambridge, Mass., 1962, p. 42.

[50] It is assumed that the readers of this report are familiar with these categories, no elaboration will be made on the differences among these four types.

The major arguments that have been presented in support of the new town approach are: a) Relief of population pressures in central cities, b) internalization of external economies, c) elimination of diseconomies of scale, d) increase in the esthetic quality of the city, and e) development of "community." These justifications are briefly discussed below.

1. By creating new towns, some of the demand for existing urban land will be diverted to the new town. This decrease in demand for land in older cities will lower land values and therefore housing price. This reduction in demand also will relieve other congestion pressures in the central city that lead to high social costs.

2. Externalities characterize population aggregation so that the action of one decisionmaking unit affects another unit. Small-scale builders or other decision units do not internalize these externalities but equate their own, nonsocietal, marginal costs and benefits. Under these conditions, firms may continue to locate in large urban-core cities, where operations at least appear profitable, even though the net social product (taking diseconomies into account) is less than that which would have been generated by an alternative location.[51] A large-scale planned and developed unit can more easily incorporate the economies of urbanization and internalize otherwise external economies.

3. Large urban centers are believed to experience diseconomies of scale. Although there is no conclusive proof, it appears that per-capita costs of public services are substantially higher in very large cities than elsewhere. The creation of new smaller cities would reduce population growth in cities suffering from diseconomies of scale but would not be so large as to incur these diseconomies.

4. New towns, it is argued, will provide open space, greenbelts, and other esthetic amenities vital to quality neighborhoods but difficult to provide in existing cities.

5. New towns will be reasonably self-sufficient or self-contained, with shopping, homes, recreation centers, and work places located within the area. The new town will be a "social enterprise" that will facilitate a sense of community. These justifications of new towns imply certain end products which are anticipated.

[51] See Nonna Moto and Verle Johnston, "New Towns vs. Old Problems," Federal Reserve Bank of San Francisco, *Monthly Review*, July 1972, pp. 1-15.

These implications will be discussed below:

1. Relieving the demand pressures on the property of existing cities will lead to lower land prices and consequently lower housing prices. But as radical as the new town proposals seem, they will affect only a small part of our housing production. The effects on center city housing will likely be small. Moreover, if the housing markets are competitive, a diminution in rental prices will lead to a decrease in the maintenance of housing so affected. Thus the quality of housing services will also decrease.

2. As has been stated above, the question of diseconomies of scale is still unresolved. It is conceivable that new towns—through planning and controlled growth—could produce public services more cheaply than larger older cities. If new towns attract the higher income persons from the cities, however, the problems of providing public services will be exacerbated for those residents remaining (usually lower income persons) unless the cost of those services is reduced dramatically.

3. One of the strongest arguments for new towns is the potential for the internalization of externalities. But this requires unprecedented cooperation among all levels of government and the private sector. Presently, large scale construction and planning is frustrated by a fragmented governmental structure. Administrative and political constraints have tended to impede consistency in the attainment of public interest objectives. Techniques for shaping the urban region operating within these constraints have included: Extraterritorial zoning and subdivision powers and consolidation and annexation; agricultural and development zoning and floating zones; State and county zoning and subdivision regulation; purchase of scenic easements by States; purchase of conservation easements; and development rights and changes in assessment practices for taxation purposes.[52] A commission with broad coordinating powers and the use of eminent domain would help to alleviate many of these problems and would facilitate the internalization of externalities.

4. In Great Britain, greenbelt as a concept has tended to work haltingly at best. Permanent restrictions on growth are not compatible with increases in population and the economic and social advantages of the city. In the United States, the conservation of green areas is not so severe a problem. To accommodate 100 million people at suburban densities would take about 14 million acres. This represents only about one-half the decrease in planted crop acreage that occurred during the 1959–64 period. It is unlikely that new towns would use less space than a simple expansion of suburbia, but if properly planned they may offer more usable green areas than an unplanned growth.

5. The final justification for new towns is that through creation of self-contained cities the values of a "social enterprise" will be realized. But self-contained cities create many problems, especially if they are rather small. The self-contained city may be able to economize on certain resources (commuting time for example) but it is likely to result in lower per-capita income as well as the cyclical risks and instability that affect small cities. In small cities, career opportunities are far fewer, and the decline of a major firm can spell disaster. People seem unwilling to constrain themselves to the localized and small range of choices that would likely exist in smaller new towns. Furthermore, a small, self-contained town will not be able to achieve the specialization which leads to efficiency. But if the towns are not self-contained, the space that intervenes between them and other cities will lengthen travel time and create higher commuting costs.

It is not obvious that a self-contained town is the ideal community that many people have suggested. While many writers have associated large cities with alienation, others give a less than flattering view of small city life. William Alonso articulates another difficulty of new towns to those who stress the importance of ". . . participation in planning. The great problem with such participation is that several years of planning and development must take place before a new town has any residents. Except in rare cases . . . there appears to be no feasible mode of participation that would amount to more than a consumer survey. . . . This accounts for some of the tension that commonly occurs between residents and developers in some new town under way."[53] As part of a feeling of community, supporters of new towns emphasize the social balance that can be achieved. There is little hope, however, that this balance has occurred. Low income families need inexpensive housing;

[52] See Herman G. Berkman, "The New Town and Urban Change Form," *Land Economics*, Vol. 48, No. 2, May 1972, pp. 93-103.

[53] "The Mirage of New Towns," *The Public Interest,"* Vol. 19, *Spring 1970*, p. 13.

this usually is older housing. Presently, we cannot build new housing for low income families without heavy public subsidies. In Reston, Va., and Columbia, Md., there has been some success in achieving racial mix, but the median income of minority residents is well above the median income of minority groups generally. At present, the new town has not achieved social balance with respect to the inclusion of all income groups.

In spite of some of the limitations of the new-town approach, further development of the program may be justifiable on the grounds of the internalization of externalities and, to some extent, the creation of a sense of community among its residents. In addition, new towns might serve as testing laboratories for urban innovation. They provide a chance to experiment with new housing and transportation designs as well as with new methods of public administration. In the process, they may provide solutions to some of the problems of the central city. On several counts—economic, social, and purely structural—new towns can provide an experiment in stimulating urban thinking.[54]

State and Local Government Policies

The policies of State and local governments potentially affect housing supply and demand in numerous, diverse, and complex ways. Generally speaking, States establish the legal framework in which local governments operate, but do not seem actively to affect housing markets. There are significant differences among States with respect to the kinds of taxes that local units can levy, the kinds of activities that local units can undertake, the legal relationships among the various kinds of local units, etc. State-usury laws and laws governing the operation of financial institutions within States could possibly affect housing, but these do not seem too important. The significant areas in which State and local governments affect housing are the levying of the property tax, the structure of local governments, and the various regulations concerning zoning and building codes.

The importance of the property tax as a source of revenue for local governments is well known and widely documented.[55] For our purposes we will concentrate on the real property tax, neglecting only the taxation of personal property such as autos, household appliances, etc. It is important to note first that wide variations exist in the property tax laws and practices among States. Not all classes of property are taxed by every State; some classes of property are legally taxed more than others—in practice, some classes of property are taxed more than other classes even though the intent of the law is to not do so. States also determine the kinds of nonproperty taxes that local units can levy, and this seems to explain differences in property tax collections among areas and regions.[56]

The real property tax can be separated into (1) a tax on residential property, both owner-occupied and rental property, and (2) a tax on real business property, including agriculture. The tax on residential property can be considered as a sales tax on housing services because housing services are derived almost totally from the characteristics of the house, which is, of course, capital. It makes little practical difference whether the tax is expressed in terms of the input—the house—or the output—housing services—as long as all capital is taxed. Roughly half of the property tax revenue comes from taxes on housing; this was equivalent to an excise tax of 24 percent on rental value in 1962.[57] Like most sales taxes or excise taxes, the property tax is regressive.[58] The property tax discourages the consumption of housing services; this especially hurts the poor because of its regressivity, and to the extent that the production of housing services is more capital-intensive than the production of nonhousing services, investment in housing is discouraged, as well as improvements in existing properties.

The property tax by itself has deleterious effects on the quantity and quality of housing, but these negative aspects are reinforced by another phenomenon: The existence of large numbers of

[54] See Nato and Johnston, op. cit., p. 6.

[55] In the 1950's and 1960's, property taxes accounted for about 45 percent of total State and local taxes. By 1970, this percentage had fallen to 39.2 percent and is projected to fall about 35 percent by 1980. Total property tax collections are projected to increase from the $34 billion collected in 1970 to about $70 billion in 1980. See *The Financial Outlook for State and Local Governments to 1980*, Tax Foundation, Inc., New York, 1973, p. 89.

[56] Dick Netzer, "Impact of the Property: Its Economic Implications for Urban Problems," reprinted in *State and Local Finance*, ed. by William E. Mitchell and Ingo Walter, (New York: Ronald Press), 1970, p. 145.

[57] Ibid., pp. 147-48.

[58] Ibid., pp. 152-53.

small local governmental units, especially in metropolitan areas, where the bulk of the housing problem is to be found. Many explanations have been given for the growth of suburban areas; the important and relevant ones for our purposes are given below.

One reason for this growth is the intent to minimize the redistributive impacts of local government tax and expenditure programs. The most effective way to prevent redistribution is to put the "price" of governmental programs beyond the reach of the poor. This is accomplished via high property values or rents, and this is a much more effective device than zoning out the poor. Of course, the subsidization of highways made travel for the nonpoor much cheaper and permitted movement away from the rental city. The production of poor or low quality housing is also cheaper in the central city than in the suburbs. Effective property tax rates are lower in the richer suburban units, and this attracts housing capital away from the central city to the suburbs. Property tax payments in smaller, less complex units are more readily identified with expenditure programs, so that it takes on many characteristics of user-charges. This is not true for central city residents.

The net impact of the property tax, combined with suburbanization or fragmentation of local units, is to inhibit the quantity and quality of housing available to the poor. Because of the Federal tax subsidies and isolation from the poor, the nonpoor are much less adversely affected. To offset these negative impacts, States could encourage a heavier reliance on nonproperty taxes, or Federal income tax breaks could be granted to the poor based on their rents. The Federal revenue sharing program—to the extent that it reduces property taxes—will help to alleviate this situation.

Zoning laws attempt to minimize the impact of potential external diseconomies caused by the construction of properties that impose costs on individuals in surrounding properties. Zoning laws permit these problems to be handled at a cost lower than would occur if litigation were the only solution. To the extent that zoning insures against unforeseen declines in property values because of changing land use patterns, the construction of housing is encouraged [59] over what it would be in the absence of zoning. Zoning, however, must be optimal in the sense that the side effects or externalities are neither overestimated nor underestimated. If a disproportionate share of urban land is zoned for single family units, a shortage of rental units will be created, or overcrowding will exist outside the single family zone. This will tend to discourage housing construction or at least reduce the quality of the housing stock.

On the other hand, zoning might unduly limit the supply of slum housing so that slum rents are maintained at artificially high levels, or so that the slums are relocated.[60] One zoning problem that seems to be prevalent is related to mobile homes. Given the substantial increases in mobile home shipments, more and better land will have to be made available for this kind of housing unit.

Somewhat related to zoning regulations are building and maintenance enforcement codes. Inadequate maintenance by a single-property owner imposes costs on nearby properties so that it is in everybody's interest to have laws governing minimal maintenance standards. Building codes are an attempt to insure that new housing construction meets minimum standards. Just what impact these laws have had is hard to judge. To the extent that the building codes do not get revised, the cost of housing construction is higher than if the new updated production techniques and materials were used. If the codes are too severely enforced, this could result in a large reduction of slum housing, thereby driving up rents that low income families have to pay. It would also eliminate a low-cost method of providing housing for the poor.[61] Stricter code enforcement would raise the cost of poor or substandard housing.

[59] Otto A. Davis, "Economic Elements in Municipal Zoning Decisions," *Land Economics*, XXXIX (November 1963), pp. 375-86.

[60] Martin J. Bailey, "Notes on the Economics of Residential Zoning and Urban Renewal," *Land Economics*, XXV (August 1959), pp. 288-92.

[61] Richard F. Muth, op. cit.

A Rationale for Government Intervention in Housing

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Summary

The Federal commitment to housing remains poorly defined as to minimum shelter quality and the quantity or scope of the effort. Involvement has been mainly reactive to emerging special needs, rather than directed to basic reforms of the housing market.

Assistance to families displaced by urban renewal and highway programs has evolved from simple condemnation awards to provision of social casework assistance and special-purpose housing. The principal reason for this has been the local vacancy rate constraint—i.e. the failure of the local market to anticipate and accommodate relocation needs. Critical problems arise, however, when public works agencies are required to perform social casework functions and to develop special-purpose relocation housing. An alternative approach is to strengthen social assistance agencies and ordinary housing market institutions sufficiently, so that public works agencies can properly assume that assistance and facilities exist for families to be displaced.

There is evidence to suggest that the replacement rate of the U.S. housing inventory is held below a warranted level by institutional factors in the market. If true, this would help to account for the necessity of urban renewal programs and for difficulties in rehousing particular categories of displaced households. It would also suggest that governmental emphasis on basic housing sector reforms, in lieu of primarily reactive programs, would be an appropriate national housing strategy. The principal responsibility for that strategy would lie at the Federal level.

A Rationale for Government Intervention in Housing

The Concept of Adequate Housing

Minimum standards of housing in the United States have been devised and implemented, or suggested, by a great variety of public and private agencies, including the Federal Housing Administration; local planning, building, and health codes; local housing authorities and State welfare departments; and the American Public Health Association. The principal criteria employed relate to floor area, density, sanitary facilities, structural soundness, particular hazards such as infestation or faulty wiring, and exposure to various nuisances.

Locational accessibility and the quality of local public services are generally only implicit housing criteria, but nevertheless important. There is a powerful tradition which asserts that homeownership should be attainable by all families, and a less explicit tradition which asserts that the cost of housing should not exceed some fixed proportion of the household's income. Neighborhood racial composition is also of wide concern, though no clear quantitative criteria have emerged. The Federal Government has never enunciated standard criteria for judging the adequacy of housing, except insofar as the Bureau of the Census has attempted to classify components of the inventory once every 10 years. Census classification systems have been changeable and inexact, however. Neither the Federal census nor any other source provides nationwide information on the amount of distribution of housing space in areal units (e.g. square feet)—using room counts instead as a very crude approximation—nor of the amount of residential land in use. Hence, there is virtually no comprehensive data on residential density. Housing analysis in the United States would be assisted if systematic information were developed concerning:

- Areal measures—floor areas of housing units and ground area of lots or parcels.
- Housing history of individual households—longitudinal information on the changes in tenure, location, housing unit size and quality, rent or price (and financing) at each move since the household was established.
- Occupant history of individual housing units—longitudinal information on the size, income, race, employment, and other characteristics of successive occupant households over a

period of 1 decade at least, together with information about structural changes, major repair, and rent or price.

The Nation has, then, only partial, imprecise, and largely implicit ideas about what makes a family's housing adequate, and no stable statistical programs to determine whether that standard is getting closer or receding.

Reactive Strategy

This is not as strong a criticism as it might seem. Housing needs in the United States are met primarily through the private market, and this mechanism has given the American population a general standard of housing which is admired and envied elsewhere. The public sector's role in the production of housing or its distribution has been almost entirely confined to specific problems to which the marketplace seemed unresponsive, such as low income public housing and urban renewal. In only one respect—mortgage insurance—has government in the United States introduced a basic reform affecting, both directly and indirectly, the bulk of housing market activity by altering its institutional premises. (Some might argue that secondary mortgage arrangements belong in the same category.)

Various provisions of Federal income tax law have undoubtedly had major impacts on housing standards and housing construction. Accelerated depreciation and favorable capital gains treatment have been important incentives for the construction of rental housing.[1] Deductibility of mortgage interest and property taxes, and exclusion of imputed rental value of owner-occupied homes have acquired the status of politically unassailable institutions.[2] It is far from clear, however, whether these effects were consciously intended or anticipated when tax legislation was framed; at best, their impacts could be presumed only subjectively because no suitable econometric or investment model has been developed.

Government intervention in housing has been mainly reactive—responding to speical problems as they arose to claim attention. For example, interest rate subsidies have been used to stimulate the production of special types of housing, such as that for senior citizens. Relocation requirements have been written into the Highways Act. Monetary measures were taken to shore up the housing sector in the recent credit crunches.

This reactive strategy—if inchoate and cumulate responses to separate issues can be called a "strategy"—does not require complete knowledge of how the housing sector as a whole functions. A problem or complaint arises, measures specific to that condition are devised and implemented, and, after a while, the difficulty is under control. One does not need to be an automotive engineer to drive the family car to the supermarket, and in a complex field such as housing, where ultimate expertise is nonexistent, the sensible thing is often to deal with immediate problems in shortrun, reasonable-sounding terms.

The reactive strategy does not define needs, nor does it test whether the basic performance of the housing sector is all that it might be. Extensive studies made in anticipation of the Housing Act of 1968 attempted to remedy both of these criticisms of Federal housing policy formulation. It is interesting to note that the principal thrust of the studies and of the legislation itself was toward a quantitative increase in housing production—a numerical goal of about 26 million housing units in 10 years, to amortize a measured inventory of substandard dwellings while also providing for a growing population. Needs were measured with census data and definitions, crude though these are known to be. And though many questions were raised about the efficiency of the private housing industry, the only substantial structural "reform" attempted was an extension of mortgage subsidies to a wider portion of the population. We did not really learn much that helps us to identify the things that government should do and can do from that 1967–68 spate of housing studies.

The Right to Housing

Government's proper responsibility in housing remains ill-defined partly because policymakers often seem to regard it as self-evident. The 1949 Housing Act committed the Nation to ". . . the goal of a decent home and a suitable living environment for every American family. . . ." There are many ways to interpret such a statement, and one of them is the extreme notion that government guarantees that adequate housing, like schooling, will be available for all. If this were really the case, inadequately housed families could simply come to a government office and demand to be taken care of.

[1] W. F. Smith, *The Low-Rise Speculative Apartment*, Center for Real Estate and Urban Economics, University of California, Berkeley, 1964.

[2] Henry J. Aaron, *Shelter and Subsidies*, The Brookings Institution, Washington, D.C., 1972, Ch. 4.

Several important programs with almost this premise actually exist. Probably as many as one household in three qualifies on grounds of income for public housing or housing assistance under Sec. 235 or 236. In New York City, a family of four is eligible for public housing if its income is less than $9,500; about 150,000 families are on the waiting list for such housing.[3]

Categorical welfare programs and general assistance are committed to the principle of providing recipients of aid with sufficient income to obtain standard housing, though housing allowances often tend to lag seriously behind increasing market rent levels. If all qualified households sought help under these programs and were accommodated, the Nation's housing problem would already have been substantially solved. Of course, the quantities of assisted housing units actually provided or obtained fall far short of the number of theoretically qualified households. This may not be a legal dilemma, but it is a moral one, and it raises a question about the real nature of the public commitment.

Token Programs

When Robert Weaver was Secretary of HUD, he encountered strong congressional opposition to a proposal for rent supplements to "moderate income" families. Critics wanted these supplements limited to truly low income families, and the answer offered these critics was to the effect that low income families already had their program—public housing. At the time, public housing units made up scarcely more than 1 percent of the nation's housing inventory and accommodated only a small fraction of families that fell within public housing income limits.

Only a slim fraction of the Nation's "moderate income" families benefit from housing programs directed to them, and only a small proportion of the elderly population occupies senior citizen housing that has resulted from Federal efforts. For almost any group that can be said to have housing problems, there is some type of program on the books. But there is not very much of that type of housing on the ground.

This tokenism is partly explained by the reactive strategy described above. In response to a new type of need, some new vehicle is created; but there is insufficient feedback—or program evaluation—to reveal whether that vehicle is adequate for the task. Indeed, the very existence to a vehicle tends to discredit subsequent complaints from the target group. Urban renewal got rolling toward its large relocation headache by assuming that displaced low income families would be "referred to public housing"—in cities where waiting lists for public housing were already very long. These referrals are sometimes specious, but they may nevertheless meet the responsibilities of urban renewal agencies under more recent relocation laws and directives.

Urban renewal itself was initially construed by many of its advocates as a subsidized rehousing scheme—which is what "slum clearance" means in many other nations. In 1945, for example, while Congress was involved in the lengthy process of drafting urban redevelopment legislation, a spokesman for the Family Welfare Association of America expressed his support in these words:

> The basic purposes of the general housing bill . . . now under consideration in the Senate are to provide as quickly as possible adequate low-cost housing for middle-income and low-income families.[4]

When redevelopment legislation was at length introduced to the Senate by Senator Allen J. Ellender, he explained:

> The basic justification for Federal assistance in slum clearance is the serious impact of slum conditions on the lives and development of millions of American families and their children.[5]

The same Senator Ellender, however, had been told by a witness representing the National Association of Real Estate Boards (an affiliate of which played a leading role in drafting the 1949 bill) that slum clearance was not only not a subsidized housing program, but that the addition of a relocation requirement would discourage redevelopment.[6]

With the beginning of actual urban redevelopment projects, it became manifest that the program was harmful rather than helpful to families in substandard housing. In 1954, a new program of FHA mortgage insurance (Sec. 221) was introduced to remedy this problem by encouraging the provision of "low-cost housing for families displaced because of . . . urban renewal projects. . . ."[7] Once again, the slum dweller's

[3] Cited in the *Ontario Housing Magazine*, April 1973, p. 2. H. J. Aaron provides estimates of the number of households which qualify for public housing. Aaron, op. cit., p. 115.

[4] *Hearings Before the Committee on Banking and Currency*, U.S. Senate, The General Housing Act of 1945, 79th Congress, Part 1, p. 319.

[5] *Congressional Record*, 81st Congress, 1st Session, Senate, p. 4613.

[6] *Hearings Before the Committee on Banking and Currency*, op. cit., pp. 450-453.

[7] *8th Annual Report of the Housing and Home Finance Agency, 1954*, U.S. Government Printing Office, Washington, D.C., 1955, p. 90.

housing problem was "solved" by well-intentioned legislation. But mortgage insurance failed to provide anything like the deep subsidy required for effective housing help; when this at last became apparent, a new solution (Sec. 221(d)(3)) emerged, consisting of below-market interest rate mortgages with FHA insurance and FNMA market support. In its own time, this was also seen to be inadequate, so that, by 1968, another "ultimate solution" (Sec. 235–236) was proclaimed, 19 years after a bold effort which had been billed as the slum dweller's salvation. The author prefers to believe that this extended "comedy of errors" simply reflects the dismal state of the study of housing economics in the United States, rather than the perversity of legislators or lobbyists, but other views could be entertained.

Putting the Burden on the Individual

In American communities, local ordinances go far toward specifying the minimum quality of housing that a family can occupy. Construction of housing with quality lower than this is prohibited, and existing dwellings that fall short are sometimes declared "unfit for human habitation" and ordered vacated. Although code enforcement rarely puts families physically into the street, it has the effect of forcing most families to pay the market price for standard housing, whether they think they can afford it or not. In this respect, housing standards are treated somewhat like automobile standards—if you cannot afford a car that is safe to drive, you may not drive.

In the early days of urban renewal, some of its advocates took just this approach to the slum problem—the occupants would have to meet their community responsibilities by providing themselves with a higher standard of housing. This view was that slum residents were the source—not the victims—of the housing problem. Today, the great majority of U.S. households live under this budgetary rubric, laying out enough money to obtain housing that meets community expectations, whether they individually prefer it or not. There is some current criticism that the average or modal level of housing consumption—particularly as to land—is too high. But to be adequately housed is something most American families tend to feel they owe to their communities, rather than the other way around, just as personal standards of dress and cleanliness are partly a response to community expectations.

A Confusion of Aims

It is not clear, then, that government is accountable, in general, for lapses in housing standards. Where government itself is the cause of housing difficulties, the case may seem clearer for specific remedial action—to provide replacement housing for families caught up in a public works program, for example. But even here, responsibility does not define action; we can meet the responsibility in various ways.

The Case of Relocation

Households displaced by urban renewal and highway programs—and by some other forms of public action—are entitled to specific public assistance in securing replacement housing. This entitlement is recent. Prior to 1954 (at the earliest), displaced homeowners were awarded the appraised value of real property taken. Displaced families who were renting had no direct claim for compensation against the government and were probably only rarely able to recover against the landlord for loss of a valuable leasehold. Tenants even lacked legal standing to protest the taking of property in which they lived. This is the traditional and "normal" state of affairs to which right-of-way agents and urban renewal real estate officers were long accustomed. The procedure could be lengthy—if the condemnee were persistent and imaginative—but the course and the rules were clear. Payment of the appraised value of property taken satisfied the obligation of the public agency and allowed the project to proceed. Households displaced by public action had the same rights as households forced to move by decisions of private landowners—and no more.

The implicit rationale for this very narrow definition of public responsibility was the assumption that substitute housing was always readily available, and that particular households were relatively mobile within the urban community. Tenants could simply stop paying rent at one address and start paying it somewhere else; homeowners could take the cash received in condemnation and purchase a home of equal value somewhere else. If these market conditions existed, the displaced households were not much worse off than households which at the same time were changing their places of residence voluntarily—something that most households do rather regularly.

Self-relocation, whether voluntary or compulsory, requires the existence of surplus housing inventory—vacant units available for purchase or rent. Eventually, the housing construction might make up for demolition losses brought about by the public program, but displaced families are in need of an immediate recourse. Hence the local vacancy factor is an important determinant of the impact of public programs on housing conditions.

If there is a large inventory of vacant, available dwellings in the community, families displaced by small-scale public projects can be readily rehoused. If the project is large in scale but phased over a long period of time, the problems of relocation may still be minimal—if the supply of vacant dwellings is also gradually replenished at the same time. Projects that soak up substantially all of the community's vacant dwellings will make it increasingly difficult for all the households in the community to enjoy mobility, and will also make it very unlikely that displaced households will find substitute dwellings of the type, price, and location they desire.

Unfortunately, the quantity and quality of local housing vacancy data in the United States are quite inadequate for objective evaluation of relocation resources, generally speaking. There is the further substantial difficulty that we do not know the minimum vacancy rate which protects a local housing market from the condition of "scarcity" (and possible inflation). For these reasons, people who are concerned about the welfare of potential relocatees have been correctly suspicious of large-scale projects; the local vacancy rate, whatever it is, is assumed unlikely to remain at a viable level.

The "critical level" of vacancy rates—below which scarcity prices are expected to appear—is generally believed to be approximately 1 percent for owner-occupied dwellings and 5 percent for rental housing; these are subjective judgments. Statistical verification of the scarcity threshold would require disaggregated time series on both rents (or prices) and vacancy for a particular community. Suitable data are not ordinarily available, though economical methods of gathering them have been developed.[8]

Urban renewal and highway construction projects are likely to create relocation needs in excess of local vacancy resources for two reasons: They involve the removal of housing in large quantities—by the city block—in a relatively compressed period of time, and they affect a particular category of housing rather than a cross section of all the housing in the community. Thus, large numbers of quite particular types of dwellings are needed, while market-produced vacancies tend to be spread—albeit unevenly—across the board of dwelling unit sizes, prices, locations, and other significant characteristics. There is likely to be a serious mismatch between relocation requirements and vacancy resources; unfortunately for all concerned, the poor quality of local vacancy information typically obscures this mismatch.

Urban renewal relocation—and to a lesser extent that resulting from highway construction —also implies an upgrading of the displaced families' housing standards. It was a most disingenuous assumption of early relocation programs that families could be relocated from slum dwellings to standard housing without someone's having to pay a higher price; of course, there would have to be an extraordinary vacancy situation in the local market for this to happen—a surplus of standard housing sufficient to pull its price level down, but which the slum families had not themselves discovered.

Urban renewal relocatees, then, are in need of substitute housing at a market level above what they can usually afford. Not only do they look for some form of financial assistance for this upgrading of their housing standards, but they also encounter many-sided difficulties in shifting to an unfamiliar socioeconomic environment; neighborhoods where some of the required type of dwellings might be vacant resist the intrusion. Housing that seems to be suitable and vacant often is not practically available.

Not enough is known about families displaced by highway construction, but it is apparent that their relocation is not always the "lateral transfer" through the housing stock that might be supposed. If their housing is even moderately substandard to begin with, then relocation involves upgrading, and the special difficulties associated with urban renewal are encountered. Homeowner families requiring new mortgage loans in the relocation process sometimes face higher interest rates than they had been paying, and some householders—particularly the elderly —may no longer be eligible for normal mortgage loans.

Both urban renewal and (to a lesser extent) highway programs encounter families with needs for many social services besides housing assistance. One prominent urban renewal director, in an unpleasant but perceptive analogy, likened this to turning over a rock and exposing a mass

[8] For example, J. M. Carman, *Rental Housing Vacancy and Turnover*, Technical Report No. 3, Center for Real Estate and Urban Economics, University of California, Berkeley, 1969.

of loathsome insects in the decay beneath. Long-neglected needs for health care, family counseling, education, and employment guidance, as well as extreme destitution, come to the attention of public agencies that are nominally responsible for meeting these needs, when occupants of buildings to be demolished are surveyed. Alienation and occasionally criminality add to the social challenge which is revealed.

Relocation thus became a convenient point at which a full range of social services could be brought to bear. Not only is it difficult for the community to close its eyes to needs revealed in this way, but the concept emerges that social services can facilitate relocation. For example, if an elderly widow's reluctance to apply for welfare can be overcome, she may be able to afford better housing. If a man who is ill and unemployed can be given medical treatment and found a job, he may be able to fend for himself in the market for adequate housing. If "open housing" laws are scrupulously enforced, minority families may be able to move out of slum dwellings without subsidy and into a broad spectrum of available housing.

The reactive strategy to housing needs places responsibility for ancillary social casework on the public works agency engaged in demolishing housing units and therefore in relocating its occupants. Urban renewal and highway agencies build up staffs of social workers and establish complex, ad hoc liaison with numerous other public and institutional agencies, so that all the significant needs of relocated households can be met on a case-by-case basis. Since the proper performance of these functions can require lengthy time horizons, the agencies' goals are compromised, or they are tempted to give just "a lick and a promise" to these large new responsibilities.

Properly done, social casework in the relocation process increases the effective availability of vacant, standard dwellings in the community. It does not create additional housing, and it may provoke opposition in the new neighborhoods to which the "rehabilitated families" are directed. This is most significantly true in the case of racial minorities, the elderly, and fatherless households. There are quantitative limits to the relocation effectiveness of even the most comprehensive social service program, and those limits are determined by the local vacancy situation in conjunction with basic community attitudes.

Consequently, the public works agencies have become increasingly involved with the development of new, special-purpose housing for relocation, as well as with complex social casework. In one approach, local public housing authorities are persuaded to adapt their development programs to relocation needs; this is sometimes an uneasy relationship because these agencies have divergent rationales and funding —the 1949 Housing Act which inaugurated urban redevelopment specifically divorced these functions. In another scheme, the redevelopment agency encourages creation of nonprofit organizations as housing sponsors under appropriate Federal legislation. In either case, new housing units are developed which are precommitted to displaced households. Sponsored, special-purpose housing may also be developed by spontaneous groups, and the new housing from whatever source may be available to families displaced by various public programs, such as highway construction or code enforcement, as well as urban renewal.

For an urban renewal agency, the necessity to arrange for the construction of special-purpose new housing creates important operating problems. The principal land resource is that which the agency is undertaking to redevelop, and of course this is not completely available until after the land has been cleared. An intricate phasing problem is created which requires that some housholds first be relocated away from the project area, that new relocation housing be constructed on the released land, and that the next households displaced be rehoused in this new construction. A further complication is that households displaced from one block, for example, may have diverse housing needs—some may be single, elderly people and others members of large families, so they cannot all be shifted to a homogeneous new development.

It is obvious that a redevelopment agency that undertakes to rehouse displaced families within the project area surrenders important freedom concerning the reuse of that land. The central purpose of the initial urban renewal legislation in the United States was to allow slum area land to be used for some other purpose—

housing for some other socioeconomic group, or commercial enterprises, or public facilities.[9] Many of the supposed benefits of urban renewal —increase in the tax base, reduction of social service costs, attraction of new enterprises to the community—are difficult to realize when on-site rehousing becomes an operating constraint. This does not imply that these initial goals are superior, but it does mean that the cost-benefit assumptions underlying urban renewal are at least partially invalidated.

Indeed, if social casework and housing construction efforts arising out of the need for relocation are added into project cost estimates, both urban renewal and highway construction become much less attractive works of government than they otherwise appear. From the initial situation, in which perhaps too little "social cost" was charged against such projects in the planning stage, we may have moved to a situation in which too much is charged, so that essentially worthwhile efforts are curtailed.

An alternative concept—which might be called "administrative pluralism"—would place the responsibility for social casework and for the provision of replacement housing in other agencies. The work that social agencies perform should be done irrespective of urban renewal or highway building, and their costs should not be charged against those programs simply because the need for social services is revealed by them. As for new housing resources, the fact that some groups in our communities cannot obtain adequate housing through the marketplace is not something to be laid at the door of urban renewal or highway agencies.

While these programs do remove housing—some of it substandard—from the inventory, they do not diminish entrepreneurial motivation to supply other housing in its stead. They may, depending on their timing and scale, cause the marginal cost of housing to rise, and that is a social cost which, by rights, should be part of the cost-benefit judgment preceding the renewal or highway project. But if entrepreneurial responses in the housing market are sluggish and inefficient, renewal and highway programs do not make them so; the problem lies elsewhere. Renewal and highway agencies have no meaningful control over the housing economy as a whole, but simply function as additional consumers of housing space, in a very real sense. We already have a large set of agencies and institutions in the marketplace whose function it is to supply housing space in response to effective demand from all sources.

Administrative pluralism does not mean an absence of coordination among public works, social services, and housing activities, but means rather that coordination should be the responsibility of government itself at a higher level than the operating agencies. Reconciliation of disparate aims is a policymakers' function that individual operating agencies are inherently unable to perform. For example, an urban renewal director has no basis for selecting a tradeoff point between the welfare of relocated families and the benefit to his community of the proposed change in land use. If he is given responsibility and discretion in both areas, he must make arbitrary and inefficient choices, or be subjected to unmanageable pressures, or both.

Applied to relocation housing, this concept of plural agencies means that local housing inventories would be made to expand appropriately in anticipation of displacement caused by urban renewal, highway building, code enforcement, or other activities. The local housing inventory would be managed and planned, to some extent, if only in terms of a good simulation model and refined information systems. These planning tools have not been developed in the United States (although some useful preliminary work has been done).[10] Local city planning staffs sometimes use what data they have very effectively, but are handicapped by the lack of economic concepts. They, and other agencies such as regional FHA or FHLB housing economists, now rely primarily on intuitive extrapolations and implicit judgment models about how the local housing economy would respond to

[9] In Congressional hearings on early urban redevelopment proposals, the Administrator of the National Housing Agency, John B. Blandford, Jr., expressed such a view in the following words:

Up to the present time, practically all slum clearance and rebuilding of the blighted areas of our cities have been in connection with public housing. Broadly speaking, this has tended to limit the amount of slum clearance and redevelopment according to the size of the public housing program. But a broader question certainly presents itself: Does not sufficient progress in the rebuilding of blighted and deteriorated areas depend upon making it possible to reuse them for a variety of purposes—for housing for middle and upper income families as well as low income families, and for other purposes besides?

Hearings Before the Committee on Banking and Currency, op. cit., p. 109. See, also, James Q. Wilson (ed.),*Urban Renewal—The Record and the Controversy*, Cambridge, Mass., M.I.T. Press, 1965, Ch. 4. Gradually increasing emphasis on rehabilitation and on resident-oriented sponsored housing in project areas implies abandonment of this early view, but this has not deterred local agency officials from portraying their project proposals as fiscally beneficial to the city.

[10] See Douglass B. Lee, Jr., "Requiem for Large-Scale Models," *Journal of the American Institute of Planners*, May 1973, pp. 163-178.

particular exogenous events such as land-clearance programs.

Indeed, one important reason for locking housing functions into renewal and highway agencies is that these agencies have precise information about relocation needs, though it is on an extremely short time horizon. An urban renewal agency knows for a fact, for example, that today Family X must move into a 3-bedroom dwelling renting for $100 or less. If the community's housing market has not somehow anticipated this need, the renewal director will have to put Family X up in his own living room, so to speak; he may end up manufacturing something for them—which is approximately what urban renewal directors have been doing in recent years. The local housing economy has not anticipated his needs, either because these needs were not known soon enough or because the housing economy was unresponsive.

So, if relocation housing activities are to be spun off from public works programs, accurate short term forecasting of local housing market activities must be made possible. There must also be some form of public handle on changes in the nature and use of the local housing inventory—direct public construction, incentives to private investors or developers, or other devices. Such "handles" exist, in the form of numerous housing assistance laws, and powers granted for their use by public or quasi-public bodies. The information and analysis systems do not yet exist in usable form.

It can be argued that urban renewal and highway relocation problems are so localized and limited in scale that no fundamental restructuring of national housing market institutions is called for; ad hoc measures will do, in the same way that response to housing needs created by a natural disaster can only be handled ad hoc. This is an area very much deserving of careful empirical study. But it can be said that national housing market institutions and public programs relating to them exist in any case, and that these institutions may be responsible in some measure for the embarrassment that relocation has come to mean for urban public works undertakings.

Strategies for Public Involvement

Housing needs that arise from relocation can be provided for in several alternative ways. These strategy options are not applicable only to relocation, however. They pertain to the general concept of governmental involvement in housing; public responsibility for housing in particular circumstances cannot be defined until policy decisions have been taken with regard to housing as a whole, for the Nation as a whole. Thus, consideration of what should be done in connection with urban renewal and highway relocation leads directly to the question of general housing strategy.

This involved issue can usefully be simplified down to choices along three dimensions:

1. Whether to provide special-purpose housing (e.g. public housing, Sec. 235–236 projects) which directly accommodates households lacking adequate shelter, or to influence or "manage" the general housing market in such a way that adequate housing becomes available to all households.

2. Whether to rely on a single governmental agency to perform all housing-related functions, including social services, or to divide responsibility among several agencies with independent functional missions.

3. Whether to place the responsibility for housing and related functions at the Federal, State, or local level of government.

It is convenient to separate the "level of government" question for discussion in the following section. This leaves two dimensions, with two extreme positions in each. Their combinations identify four "strategy types," as in this scheme:

	Single Agency	Plural Agencies
Special-purpose housing	A	B
General-market approach	C	D

Strategy A describes approximately the position toward which urban renewal agencies have been pushed by the course of events. The agency's original public works mission becomes enlarged to include social services for families to be displaced, and efforts to provide special-purpose housing in which (some of) the displaced families can be rehoused with financial assistance in money or in kind.

Strategy B can be illustrated by the position of urban renewal agencies some years ago, and probably of highway agencies at this time. In it, the public works agency turns over caseloads consisting of displaced families to the local housing authority, to welfare agencies of various kinds, to nonprofit housing sponsors of FHA counselors, to fair housing groups, etc.

For the most part, A and B represent "reactive strategies." Concern is focused on particular households whose needs are assumed to be irrelevant to the general housing market.

Strategy C might be said to represent the original, implied mission of HUD. The aim, in this case, is merely to create circumstances in the area of housing finance and housing subsidy so that opportunities for adequate housing exist for all. By stretching the point slightly, HUD's assistance to local housing authorities can be construed consistently with this concept; local housing authorities are, in effect, surrogate households. It is interesting that local planners sometimes seem attracted to Strategy C, believing that their land-use control powers can manipulate the local housing economy so as to achieve community housing aims. Metropolitan councils of government also appear confident that local taxing powers, plus controls over community services and transportation as well as land use, are nearly sufficient to handle regional housing problems.

Strategy D involves a collection of agencies working to maintain housing adequacy in ways other than construction of special-purpose housing. Welfare agencies would be responsible for solving socioeconomic problems that deprive some households of "effective demand" for adequate housing; public works agencies such as urban renewal and highway programs would have no responsibility for the housing welfare of families displaced beyond recognition of irreducible social costs in the initial cost-benefit stages of planning; monetary and economic organizations in government would assure adequate flows of funds to meet housing construction and related urban capital needs; the principal housing agency of government would confine its activities to developing usable housing market information and forecasts in all communities and bringing cogent cases for housing-related tax legislation to the legislative body, while administering such mortgage market functions—insurance and trading, for example—as are required ancillary to the operation of the capital market.

Division of Labor in the Public Sector

The housing sector of the economy, while basically private in principle, is extensively and quite directly influenced by all levels of government. This is due more to the nature of the housing commodity and to the necessary general roles of government rather than to explicit decisions by government to be responsible for housing welfare. Much of the government's involvement with housing is thus inherited and fortuitous.

In a lengthy historical process, the Federal Government has acquired overriding responsibility for the health of financial institutions and the allocation of credit through the capital market. Hence, it affects housing, which is a major user of credit. The Federal Government is also in a strong—but not unique—position to exercise leverage upon the private use of credit by creating ancillary institutions for insuring and exchanging residential mortgages, which it has done. The massive and involved Federal tax system automatically creates additional leverage in housing finance, while on the expenditure side, virtually every Federal activity from military procurement to the payment of rent supplements has some important impact on housing, directly or indirectly.

State governments affect housing primarily by regulating housing-related businesses—land development and subdivision, construction, mortgage lending, real estate brokerage, property management, etc. They are responsible for some kinds of housing-related infrastructure, particularly highways, and they provide enabling legislation for special-purpose authorities such as local public housing agencies and transportation entities.

Local government has traditional responsibility for basic urban infrastructure (streets, schools, water, and sewage) and services (police, fire protection, sanitation, parks), all of which are components of the housing "package" and may usefully be thought of as goods or services that households elect to purchase and consume jointly. Land-use control, and control over the manner of construction and the use of buildings, are also local functions.

Federal, State, and local governments share responsibility and control with respect to welfare payments. Local governments have the option of using Federal funds for programs such as public housing, urban renewal, and sewage disposal.

In recent years, both State and local governments have experimented with "development corporations" which are authorized to build special-purpose housing or other facilities, free of some restraints (e.g., zoning) that might apply to private organizations and of some obligations (e.g., referenda) of governmental bodies per se.

Significant external (i.e., avoidable) costs are associated with special-purpose housing in the United States. Low income households bring with them needs for extensive social services and assistance. Neighborhoods resist the introduction of lower socioeconomic status households because of fears and prejudice. It is only at the community or neighborhood level of social interaction that these phenomena can be externalized. That is, some neighborhoods may be able to avoid the status and income-transfer costs of special-purpose housing programs while adjoining neighborhoods are compelled to bear them both. The residents of affluent Orinda, in San Francisco's East Bay area, for example, enjoy, at least indirectly, the benefits of low-wage labor residents in neighboring Oakland, for whom Oakland must provide assistance in housing, health, and education. In the competition not to be stuck with the "bad penny," the likely loser is the urban district whose physical and fiscal situation is already the most difficult.

Because low-priced housing is generally concentrated in older central cities where land values are high—reflecting metropolitan accessibility and encroaching commercial uses—it is particularly difficult for those communities to provide special-purpose new housing. Unfortunately, high land values in the central cities do not equate with fiscal strength, for in residential areas they reflect high density rather than high per capita income. The per capita income of many central city residents is inadequate to support normal local government services, let alone new housing on expensive land.

A neighborhood community which does not presently have special-purpose housing in its midst, and which in good conscience elects to take on its "fair share," runs the risk of overshooting the mark, as some of its affluent residents opt out. Among competing urban neighborhoods, "nice guys finish last."

It follows that many local governments tend to disdain special-purpose housing programs, even if subventions are provided for this purpose. Even in the older central city, other fiscal aid is needed along with housing assistance, if the latter is to provide, dollar for dollar, the services and amenities that housing money purchases in the suburbs. Suburban communities, for their part, may need virtual bribes as well as comprehensive subventions to be encouraged to provide special-purpose housing. To make it both discretionary and attractive for local governments to run the assisted housing "show" may be very costly for the effects achieved.

The natural and easy role for local governments with respect to housing is to keep its infrastructure healthy and growing, so that expansion and replacement of its housing inventory can proceed steadily. Then housing opportunities for all its residents can be improved progressively. This requires that local governments have good access to capital markets—which, by and large, they have in the United States—and that they do a good job of short term forecasting (of employment and housing trends) and of fiscal management.

State governments could conceivably play an important role in assuring the provision of special-purpose or assisted housing in either of two ways—imposition of metropolitan government upon contiguous communities, or establishment of powerful urban development corporations. Either of these encounters important political obstacles. Very large personal windfalls, both negative and positive, are implied in any metropolitan land use planning scheme, and this makes "objective" judgment very difficult. An urban development corporation exercises public power without public accountability; political authority is generally not strong enough to sustain major efforts, particularly because a development corporation can practically create only windfall losses for people in the vicinity of its projects. State governments have, in addition, virtually no means of improving the structure or performance of the national housing industry.

Federal Government, which is answerable to the entire national community, has both the means and the authority to engage in special-purpose housing development. In the early days of public housing (1933–37), the Federal Government backed away from direct housing development activities because of opposition on grounds of "States' rights" and "socialism." At the present time, it may be judged that both of these criticisms have weakened. The largest difficulty in direct Federal development of special-purpose housing is informational—knowing just what a particular community needs and will accept.

What Is America's "Housing Problem"?

It is possible to state a housing goal—such as "adequate housing within the means of all" —without suggesting why that goal has not yet been achieved. But the reasons for failure in the past have significance for the selection of methods for pursuit of the goal in the future. In simplest terms, a nation's housing situation can be inadequate because too little has been invested in it, or because the distribution of housing is inequitable or inefficient. In the United States, government has generally acted on the presumption that the distribution and not the quantity of housing is deficient. Another way of stating this presumption is that housing supply is elastic but housing demand is sometimes artificially constrained.

Clearly, the housing inventory of the United States has never been devastated as Germany's was in World War II. Nor has the United States seen a sudden influx of new population, in this century, as Hong Kong and Israel have. And it is self-evident that the United States does not lack the real economic resources to create an adequate housing inventory, as seems to be the case in India. The most significant suggestion that housing output in the United States has been quantitatively inadequate was developed by studies preceding the housing legislation of 1968; these studies identified a need to replace some 6 million housing units deemed substandard—about 10 percent of the occupied inventory.

Otherwise, implicit and explicit criticisms of housing in the United States clearly focus on qualitative and distribution issues. Homeownership—one form of housing tenure—has long been perceived as a social value in its own right. In the 1930's, the production of housing was thought of, at least partly, as a means of stimulating employment; beginning in that period, public housing produced is used as a welfare device for families in general economic distress.

Mortgage insurance and mortgage guarantees provided by Federal agencies were intended mainly as ways of making homeownership possible for greater numbers of families. Mortgage insurance and secondary mortgage market programs also have been introduced on the assumption that technical defects existed in the link between housing and the capital market—not that physical resources were scarce or that the housing construction industry was unresponsive to effective demand.

Urban renewal may have been understood by many as a new form of housing assistance when it was introduced in 1949, but it is now clear to most that such was not the case. Urban renewal's primary mission is to alter the use of some central city land; relocation housing now produced in the process is a distinctly secondary and inadvertent objective.

The idea that housing costs more than it need cost, because of the industry's technological backwardness, appears to have been discredited after very ambitious efforts such as Operation Breakthrough. Instead, demand for new housing has been broadened by new subsidy programs for low and moderate income families.

On occasion, the proportion of new rental units in total housing output has increased dramatically in response to special mortgage and tax stimuli, only to be choked off because of unpopular windfalls arising in the process. Housing discrimination has been deprived of legal sanction. And development of special new housing for senior citizens has been effectively encouraged.

It is fair to say, then, that Americans, through their governments, appear to judge that the housing problem is not a sheer scarcity of space, but a feeling that homeownership should be encouraged, that decent shelter should be available to families who may not be able to afford it, that overt racial discrimination is improper, that sometimes and in some places apartments are needed instead of single-family houses, and that special kinds of housing are needed by elderly people and other special groups. These are matters of distribution and quality, not quantity of housing output.

The implied assumption is that the housing industry—an umbrella term for a great assortment of interests, institutions, and enterprises—provides whatever the consumer is able and willing to pay for. Some consumers lack effective demand, for one reason or another, and they are the ones who have housing problems. The general population gets its money's worth from a reasonably efficient and responsive set of businesses, according to this image.

This assumption is open to serious challenge. There is historical evidence to support the hypothesis that aggregate housing production in the United States is limited by institutional constraints, and that housing output has been deficient and unresponsive over a very long period to real, effective demand for better housing, and that much of the perceived "qualitative" or distributional housing problem actually originates in cumulative quantitative deficiencies.

The Underlying Problem—Supply Inelasticity

A housing structure is a durable good which, even with normal maintenance, gradually becomes less serviceable as time passes. It is subject to physical deterioration and to obsolescence. We would expect houses, like automobiles, to become cheaper as they get older, and to be scrapped finally when a replacement is produced. The rate of replacement, or alternatively the average duration of use, is an index of the general quality of the inventory in use; an increase in the replacement rate is necessary if the average quality is to rise.

For American housing, the replacement process appears to be very sluggish, and subject to institutional limitations that national housing programs have done little to overcome. Based on a recent study, the average annual replacement rate of the U.S. housing inventory during the period 1889–1969 was approximately one-third of 1 percent.[11]

Figure 1
U.S. Housing Starts and Household Formation

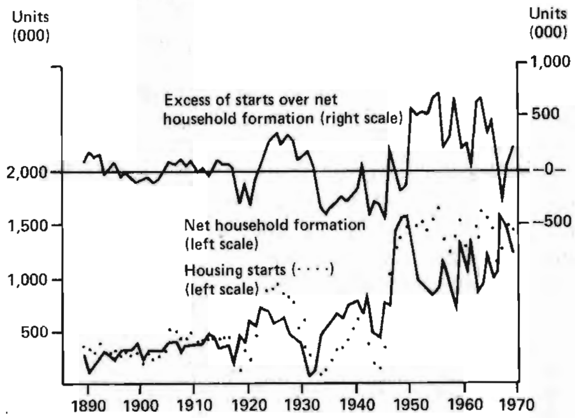
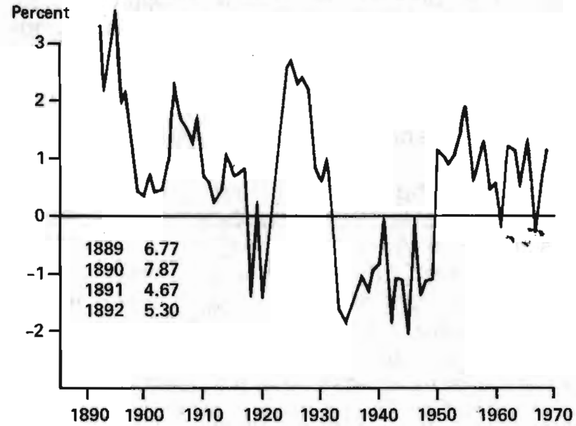


Figure 1 shows the historical relationship of housing starts to increases in the number of American households; the excess of starts is what makes replacement of superannuated units possible. Figure 2 describes a rate of inventory replacement in terms of value (rather than in numbers of units). From 1950 through 1959, the value replacement rate fluctuated generally below 1 percent, a relatively good performance. The general quality of the inventory in use, however, is the result of replacement levels over a very long period of time, and there have been prior periods of substantial replacement deficits.

These numerical estimates are important primarily for an issue they raise concerning the structure of the housing economy. Superannuated housing is made redundant only by new construction in excess of population (household) growth. The housebuilding industry and its mortgage lending affiliates traditionally respond with alarm to any suggestion of "overbuilding."

Figure 2
Value Replacement Rate — U.S. Housing Inventory



Among other reasons for this response, housing output in excess of growth requirements obviously diminishes the market value of older units in the inventory, creating windfall capital losses for particular owners and lenders. As long as older units are not made redundant by "excess" new output, their market value can be sustained even through their serviceability is falling.

Econometric studies of the housing market have been inconclusive on the subject of the income elasticity of housing supply—partly because of the theoretical difficulty of separating demand factors from supply factors by econometric techniques. A recent Urban Land Institute study concludes, for example, that "the supply of rental housing is less than perfectly elastic, even in the long run," but the argument is very indirect.[12] Richard Muth's well-known study of housing demand includes a finding that "new construction is highly responsive indeed to changes in income or in the price of housing".[13] This is not inconsistent with a longrun replacement rate which might be judged, subjectively, to be "low," because it merely correlates fluctuations in absolute increments, not in their bases; it does not indicate how rapidly the inventory as a whole is becoming either better or worse. Curiously, Muth demonstrates in the same article that "desired stock" of housing exceeded actual stock through the high construction period of the 1920's; this seems to agree with our suggestion that people were not getting as much housing

[11] A study by the author, forthcoming in *Socio-Economic Planning Sciences* under the title, "Should a House Last 300 Years?" It should be noted that special definitions are involved in this measurement, and that the accuracy of original data must be qualified in some respects.

[12] Frank deLeeuw and Nkanta F. Ekanem, *The Supply of Rental Housing*, The Urban Institute, Washington, D.C., 1971, p. ii.

[13] Richard F. Muth, "The Demand for Non-Farm Housing," in Arnold C. Harberger (ed.), *The Demand for Durable Goods*, University of Chicago Press, Chicago, 1960, p. 75.

improvement as they were willing and able to pay for.[14]

Attention has also been focused recently on housing abandonment, a phenomenon which might seem to indicate that the housing inventory is being replaced at an accelerating rate. Although it is doubtless an acute problem in particular cities, the national quantitative impact of abandonment is not clear.[15] Concern seems to center on the belief that families who could be accommodated in such housing have been "pushed" into inferior housing by something akin to a natural disaster affecting neighborhoods that have been abandoned, rather than having been "pulled" out of obsolescent areas because something better was available elsewhere. "Abandonment" today seems to mean housing discarded by its owners, not by the marketplace of users—a new form of demand for housing space not unlike urban renewal or highway building, rather than a reflection of superabundant new construction. Studies of abandonment have emphasized micro rather than macro aspects, and so the larger significance of abandonment is not clear.

At this stage, it can only be considered a hypothesis that the housing and mortgage industries in the United States discourage replacement construction, and so contribute to continuous deterioration of the real quality of the inventory. But it is a reasonable hypothesis. Indeed, the formula for Federal urban renewal subsidies worked out in 1949 (and still essentially in use) is based on the assumption that market values of slum housing need to be written down, because these substandard dwellings have not been made redundant and therefore still command a market with effective demand for housing. Figures 1 and 2 (and the material on which they are based) suggest that this resistance to replacement is characteristic of the U.S. housing economy as a whole.

Of course, resistance is a matter of degree; some replacement activity occurs more readily, no doubt, in some areas and for some types of housing than others. A far more serious look at the economic dynamics of the U.S. housing industry is warranted than has yet been undertaken, because the easy and attractive presumption of supply elasticity can be challenged.

If there is, in fact, significant institutional resistance to the replacement of older and less serviceable housing, then we may have to reinterpret the concept of special housing needs—for low income or even moderate income families, for minorities, for relocatees, for senior citizens, etc. Some of these "special" problems —situations in which the marketplace seems obviously unresponsive to effective demand—may actually be manifestations of a more general problem. In that case, the policy issues would be whether to attack the general problem by basic institutional reforms in the housing economy or to go on treating the special difficulties ad hoc.

There is an alternative and, perhaps, supplementary explanation for the low replacement rate of the U.S. housing inventory, and that concerns urban land markets. During the past 50 years, at least, general urban densities—not only residential but commercial and industrial as well—have been falling. Market pressure to reutilize the land under older housing has been weakening. The reasons for this phenomenon, in turn, include the automobile, changes in the availability of mortgage loans, and preferences or life styles as they affect housing. Thus, local land-use policy is related to the overall performance of the housing economy, partly by way of the replacement rate.

Defining the Federal Role

It now has been about 40 years since the American conscience was pricked by the phrase, "one-third of a nation ill-housed." In that time, the Federal Government has responded to the ill-defined challenge with a wide variety of efforts that have no coordinating philosophy, and the effectiveness of which has not been regularly evaluated. It has been an experimental period, perhaps not overlong, given the nature of the housing commodity. But at some point a set of clear working rules ought to emerge, reflecting the lessons of experience concerning what the Federal Government can do and should do with respect to housing, and which Federal agencies should perform which functions. That is, policy decisions of a longrun character should be made.

The preceding brief survey of some highlights of government involvement with housing supports a new definition of the appropriate Federal role. This definition is offered below in an intentionally provocative way, without excessive deference to long-established positions, in the spirit of encouraging a fresh and open consideration of fundamental policy issues.

The Federal role, as it has evolved, has three principal components:

[14] Ibid., p. 79.
[15] The National Urban League, *The National Survey of Housing Abandonment*, 1971.

1. Augmenting effective demand for housing—through welfare payments, rent and mortgage supplements, mortgage insurance and guarantees, antidiscrimination measures, etc. The basic weakness of this type of effort lies in the possibility that the supply of adequate housing might not expand in proportion to augmented demand.

2. Stimulating additions to the supply of housing—by means of tax incentives, innovations in the mortgage market such as secondary market arrangements and mortgage-backed securities, and guarantees for long term credit required by developers. The two central uncertainties about this approach have to do with the incidence of the benefit—of tax shelter, for example—and with the net effect on housing output. It has never been made completely clear that tax benefits or new secondary market facilities have caused housing output to exceed the level it would otherwise have reached.

3. Benefits-in-kind—public development or promotion of special-purpose housing allocated directly to defined categories of housing need. Public housing and sponsored low and moderate income housing fall into this category. This approach involves subsidy, the potential need for which exceeds the apparent willingness of the general public to bear; it also requires the production of new housing for income groups whose needs would be served at less cost by older dwellings if the latter were in redundant supply.

None of these three basic approaches ought to be abandoned, but the following reformulation of them is suggested:

Augmenting Demand: Assuring that families have adequate current income to afford standard housing is essentially a function of welfare and employment-related agencies of government. Antidiscrimination efforts are a law enforcement function. Federal housing responsibility in this side of the equation should be restricted to a broadened program of mortgage credit guarantees sufficient substantially to obviate personal credit screening of mortgage borrowers by lending institutions. This is really an extension of the GI loan principle to all households.

Stimulating Supply: Without discarding any of the existing tools for encouraging the production of housing, new incentives for the retirement from use of privately owned, superannuated housing should be designed and implemented. This envisages a spontaneous, continuous, private form of urban renewal; it calls for a major policy decision about the incidence of the financial cost of taking older housing off the market.

The adequacy of housing-supply responses should be measured with a carefully defined replacement-rate concept—as a social indicator.

Economic and monetary agencies of government should acknowledge a commitment to assure sufficient annual flow of mortgage funds for residential construction equal to the rate of net household formation plus at least 1 percent of the value of the existing housing inventory. In addition, appropriate new capital must be available to urban communities for infrastructure investment to meet growth and replacement requirements consistent with changes in the housing inventory. This suggestion amounts to a limited form of capital rationing.

With Federal guidance and assistance, each urban community should develop information and analysis systems sufficient to monitor housing trends, make short term forecasts of construction requirements and suitable forecasts of special needs arising from public works programs.

Federal agencies in the housing field should, in liaison with local government and housing businesses, use such information and other tools to encourage sufficient housing activity to prevent specific or general shortages from arising.

Benefits-In-Kind: Construction of special-purpose housing should be undertaken on a "last-resort" basis only; it should cease to be an open-ended commitment to large segments of the urban population.

Special-purpose housing development should be federalized—i.e., a Federal Housing Development Corporation should be the principal instrument for creating this type of housing resource in the future. Whenever such projects are undertaken, compensation should be provided to the community affected for legitimate social costs which may be created.

Again, these are sweeping and perhaps impolitic suggestions about the role the Federal Government should acknowledge in connection with urban housing in the United States. They are laid out primarily to help focus policy discussions. The author believes they are workable and promising, and that they are the implied lessons of previous efforts to define and cope with housing problems.

These general concepts have particular implications with respect to urban renewal, highway construction, and other governmental activities that cause residential displacement. One principle is that each such undertaking be preceded by a careful cost-benefit evaluation, so that the totality of likely housing consequences can be charged against the project to see if it still seems worth doing. The second principle is that if the cost-benefit evaluation is positive, the public works agencies be allowed to proceed without being obliged to operate parallel rehousing schemes.

Still more specifically, this philosophy of government's role in housing suggests following requirements in connection with a particular renewal or highway proposal:

1. A "housing impact study" as an input to the cost-benefit analysis, such study to describe the chain of moves and the pattern of inventory changes most likely to facilitate the absorption of displaced households without the need for special-purpose housing. It would also describe the requirements for social services (from all levels of government, through existing programs) incident to this absorption, and the local infrastructure needs corresponding to anticipated housing construction activity.

(This study would be quite different from the "relocation resources" study required in connection with urban renewal, which tends to focus on static vacancy levels and often misleading "turnover" rates, rather than on the dynamic adjustment of the whole local housing market to a block of additional home-seekers.)

2. Regular "housing audits" in communities with active residential displacement programs. This would be an examination of the actual response of the local housing market, with particular attention to entrepreneurs.

3. A local housing liaison service, to employ the information generated by impact studies and audits, and every permissible and appropriate incentive to stimulate suitable responses by entrepreneurs, so that housing opportunities will expand rather than shrink in the face of displacement from renewal or road construction areas.

4. A Federal housing development corporation, ready to provide special-purpose relocation housing if there is clearly no reasonable expectation of an adequate response by the local housing market to liaison efforts. Such housing would bring with it other equitable assistance to the community in which it is placed, so that standards of community services would not suffer.

This set of suggestions has a limited implication for the very large issue of revenue sharing. It says that the responsibility for the residential displacement problem arising from federally funded renewal and highway programs rests with the Federal Government; that first reliance will be placed on market institutions and the complement of existing social assistance programs administered by any and all levels of government, to see that this responsibility is met; and that if these prove inadequate in a particular situation, the Federal Government must have retained the option and the duty of carrying the ball. It is not realistic to expect that a community will feel compelled to use its "free money" from a revenue-sharing program to compensate private injuries (displacement) occasioned by activities that are conceived to be beneficial to the public (urban renewal and highway building).

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A Possible Rationale for Government Intervention In Housing: The Slow Adjustment of the Housing Market to Its Longrun Equilibrium Position

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Introduction

The purpose of this paper is to analyze the following statement, which has been offered as a justification for government intervention in housing:

> Housing is such an important part of the family budget that shortrun price and rent increases which result from the slow adjustment of housing supply to demand should not be permitted.

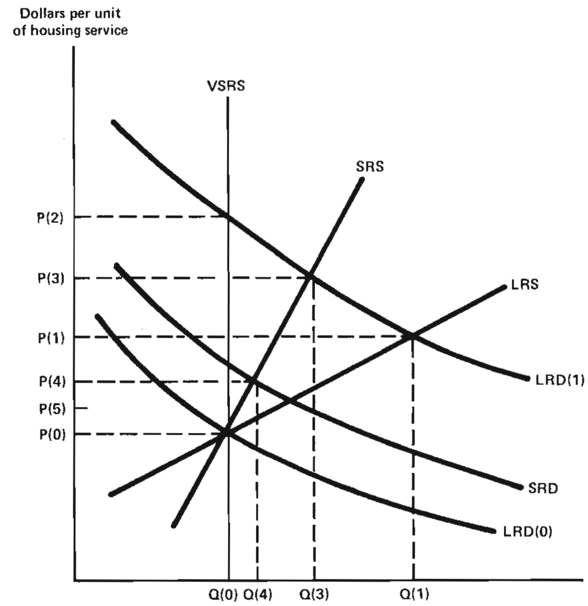
The view of the workings of housing markets that appears to underlie this statement will be presented and criticized. Some government interventions that seem consistent with this rationale will also be presented and their effects analyzed. It is concluded that the case for government intervention on these grounds has not been established.

The Incorrect View of the Workings of Housing Markets Underlying this Rationale

The following view of the workings of housing markets seems to underlie the statement to be analyzed: in the shortrun, the quantity of housing is fixed. Therefore, if there is an increase in the demand for housing, prices and rents will rise substantially above their longrun equilibrium levels, but no more housing will be available.

This view is depicted in Figure 1. For simplicity, we begin at a position of longrun equilibrium. The price per unit of housing service is

Figure 1



P(O). At this price, the sum of the quantities that households want to consume and the sum of the quantities that producers want to supply is Q(O). Now suppose that the demand for housing increases from LRD(O) to LRD(1). Since the amount of housing available is considered to be insensitive to price in the shortrun, the shortrun equilibrium price will be P(2), which is greater than the new longrun equilibrium price P(1).

This view is inconsistent with existing empirical evidence on the adjustment to longrun equilibrium in the housing market. Let me begin by explaining the theoretical defects of this argument and then cite the empirical evidence.

We should distinguish between two types of changes in demand, namely a change in the number of households that demand distinct dwellings, and a change in the quality of housing demanded by existing households. Either type of change leads to a change in the aggregate demand for housing services. It is not reasonable to expect either the number of distinct dwellings available or the quality of existing units to be insensitive to price, even over periods as short as a few weeks. At any point in time, there are houses at all stages of construction. It is possible to provide many new units in a short-period of time by speeding up the completion of these units. The higher the price of housing during a period of time, the greater the number of houses we expect to be completed during that period. Furthermore, among existing dwellings, the number of occupied units is not fixed. At any point in time there are vacancies. If the demand for distinct dwellings increases, many of these new households can be accomodated in existing vacant housing. Finally, it is not difficult to vary the quality of existing units. (How long does it take to paint a room?) Higher prices make a greater quantity of maintenance and repair activities profitable. Therefore, even in the shortrun, we expect the quantity of housing service that producers will provide to vary directly with its price. This tends to dampen the price rise accompanying an increase in demand.

In Figure 1, we expect a shortrun supply curve similar to SRS rather than one similar to VSRS. Therefore, taking into account only this objection to the analysis of those who make the statement under consideration, we expect a shortrun price of P(3) rather than P(2).

We should also distinguish between shortrun and longrun demand, just as we distinguish between shortrun and longrun supply. Suppose that there are changes in economic circumstances or tastes so that, at existing prices and rents, all families eventually want better housing. Not all families will attempt to change their housing consumption immediately in response to these changes in circumstances or tastes. It is in the nature of housing decisions that they are considered carefully, and moving into new quarters often is meshed with other events, such as children on vacation from school, marriage, and birth or death of family members. Because shortrun increases in demand corresponding to changes in economic conditions and tastes are not so great as longrun increases in demand resulting from these changes, we expect shortrun price and rent increases to be less than they would be were consumers to respond instantly to such changes.

In Figure 1, if economic circumstances and tastes change so that the longrun demand curve shifts from LRD(O) to LRD(1), then we expect the shortrun demand curve SRD to be positioned between these two longrun curves. Therefore, taking account of this and the preceding objection, we expect the shortrun price per unit of housing service to be P(4) rather than P(2).

Now suppose that economic conditions and tastes change in such a way that at existing prices some families want better housing during the next time period, while other families desire no change in their housing consumption. There is some set of higher prices that would induce sellers of housing services to upgrade their housing to the extent desired by families at these higher prices. Actual prices during the next month will not rise to these shortrun equilibrium levels, because there are lags in the adjustment of prices. One reason is that leases are often negotiated for a year or more at a time, making inevitable some delay in the response of prices to changing housing market conditions. This is yet another reason for skepticism concerning the existence of shortrun price increases exceeding increases in longrun equilibrium prices.

In Figure 1, we expect the actual shortrun price P(5) to be higher than the original price P(0), but lower than the shortrun equilibrium price P(4).

Taken together, these considerations suggest the possibility that the actual shortrun price increase accompanying an increase in demand will be less than the increase in the longrun equilibrium price. This is the case depicted in Figure 1.

Fortunately, there is some empirical evidence concerning the adjustment in housing prices and quantities from one longrun equilibrium position to another. Frank de Leeuw and Nkanta Ekanem constructed a demand and supply model of the housing market which allowed for the possibilities discussed in the preceding paragraphs. They were not able to estimate all of the parameters of their structural equations. However, using a combination of regression and simulation techniques, they were able to conclude: (1) The quantity of housing service supplied does vary directly with price even in the shortrun; (2) consumers do not try to rapidly adjust their housing consumption to changes in their economic circumstances; and (3) landlords do not rapidly adjust rents to their new shortrun equilibrium levels. The first conclusion is consistent with the earlier findings by Richard Muth and Tong Hun Lee that about 30 percent of the adjustment in the quantity of housing service to its longrun equilibrium level occurs each year. These results suggest that if the longrun equilibrium price and quantity of housing service rise, the actual price per unit of housing service will rise toward the new longrun equilibrium level, but will not overshoot this level.

An Analysis of Some Alternative Government Actions

With this evidence in mind, let us consider several alternative government actions which seem to be in the spirit of the rationale under consideration.

The government could attempt to set the price per unit of housing service at the new longrun equilibrium level. If the new longrun equilibrium price and quantity were greater than the initial ones, then the price fixed by the government would be greater than the price that would prevail in the market in the absence of government intervention. As a result, consumers would demand fewer distinct dwellings and poorer quality housing than otherwise. I take it that this is not what the people who offer this rationale have in mind.

The government could attempt to set the price at a level above the initial level but below the level that would be established in the market. This would induce sellers of housing service to provide fewer distinct dwellings and poorer quality housing than in the absence of government intervention. Because the price per unit of housing service would be lower and the quantity of housing service supplied would be less, total housing expenditure would be less than otherwise. Because total expenditure on housing will be lower, total expenditure on other goods will be greater. Therefore, the prices of other goods will be driven up. Families who spend a large proportion of their income on housing will gain; families who spend a small proportion will lose. Producers of housing will lose; producers of other goods will gain. I suspect that many people who favor this government intervention fail to recognize its effect on the price of nonhousing goods.

This rationale is usually offered by people who want to have the government set rents permanently below longrun equilibrium levels. Fortunately, there are several empirical studies of the economic effects of this type of rent control.

In a study of rent control in New York City, Edgar Olsen estimated that occupants of controlled apartments consumed 4 percent less housing service and 10 percent more nonhousing goods than they would have consumed in the absence of rent control. This change in consumption patterns is clearly inconsistent with the change implied by arguments for housing subsidies.

There is considerable variation around each of these measures of central tendency. Some families experienced much greater decreases in their consumption of housing service, while other families experienced increases. Likewise, some families experienced much greater increases in their consumption of nonhousing goods, while other families experienced decreases. The net effect of these distortions in individual consumption patterns was that the dollar value of the benefit of rent control to tenants was only half its cost to owners of this housing.

Furthermore, one can question the fairness of providing benefits to a large class of families in rental housing at the expense of the small number of owners of this housing. Although the mean income of owners of rental housing is probably greater than the mean income of their tenants, the magnitude of the difference has never been established with any great accuracy. The best available evidence suggests that the mean income of owners of rental housing is not significantly greater than that of their tenants. (See the study by D. Gale Johnson.) However, even if each owner of rental housing had an income greater than that of the richest tenant, the implicit tax inherent in rent control would be inequitable because it is borne entirely by the small subset of rich families who happen to own rental housing, and because the magnitude of the tax borne by individual landlords is not closely related to their economic position.

Olsen's study also indicated that there is a great variance in the distribution of the dollar value of the benefit from rent control among families that are identical with respect to income and size, and the age, race, and sex of the head of the household. That is, there is nothing approaching equal treatment of equals among the beneficiaries of rent control. I conclude that this type of rent control has little to recommend it.

Conclusions

After examining this possible rationale for government intervention in housing, I have found no reason to believe that shortrun equilibria in housing markets correspond to inefficient allocations of resources, or that the speed with which these markets adjust to their longrun equilibria fail to account correctly for the real costs and benefits of adjustment. I have also concluded that several possible government policies that could stem from this rationale have no merit.

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A Rationale for Federal Government Intervention in Housing: Distortions Arising from Present Fiscal Arrangements at the Local Government Level

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Summary

The principal theme of the paper is that the present structure of local government in metropolitan areas contributes non-negligibly to the housing problems of low income families. This arises from two features of the current system: (1) Property tax rates in central cities tend to be considerably higher than in their suburbs; (2) the provision of local public services entails a redistribution of income from higher to lower income groups.

While high city property taxes fall upon the housing of rich and poor alike, they tend to have a greater impact upon low income housing. This is due to the fact that higher income groups have housing opportunities in the suburbs, whereas the poor do not. It is proposed that the Federal Government provide direct housing subsidies to low income groups to offset the deleterious effect of property taxes.

While taxes vary directly with family income, most public services do not. As a result, higher income groups subsidize the public services of low income groups. For a variety of nonfiscal reasons, the suburbs tend to be populated by relatively affluent families, while the cities house the bulk of the poor. Together with the fact that public services tend to be more costly in the city, this results in greater income redistribution activity in the city. Thus, families have a fiscal incentive to leave the city. In turn, suburban jurisdictions have a fiscal incentive to exclude low income families. The joint operation of these incentives is to strip the city of its middle and upper income groups, as well as much of its business activity. This means that cities will become increasingly unable to provide services essential for the maintenance of decent housing. Furthermore, low income families will be unable to avail themselves of job opportunities that arise in the suburbs—thus heightening their housing problems.

To offset the perverse consequences of fiscal redistribution, it is proposed that the Federal Government subsidize the public service costs of low income individuals. This would take the form of a voucher which would be paid to the jurisdiction in which the individual resides. This not only will ease the fiscal crisis of our central cities, but would eliminate the penalty a suburban community faces if it admits low income families.

Introduction

The process of urbanization in the United States has continued unabated for the past 200 years. The result has been that, by 1970, nearly three out of every four Americans reside in urban areas. Few will deny the contribution of urbanization to the high living standards we enjoy today. Without it, widespread industrialization of the U.S. economy would not have been possible, since it is predicated on scale economies, which in turn require the concentration of population in space.

While urbanization has been vital to the economic development of this country, it has not been withouts its costs. High population density gives rise to problems not adequately coped with by a system of private markets. Included here are problems of transportation, environmental quality, and land use. In addition, private markets fail because of the concentration of low income residents within the urban area itself. Hence, we have the problems of urban slums—substandard housing, inadequate public health, crime, etc. While the latter problems are usually associated with poverty, wherever it may occur, they are particularly acute in our large cities, owing to spillovers that result from the clustering of poor in ghettos.

Common to each of these private market failures is the presence of externalities. That is, in pursuing their private interests, individuals do not take into account the impact of their actions upon others. As a result, we observe congestion, air and water pollution, and slum creation, among other problems.

While the problems posed by externalities are formidable and have been resolved with only a limited degree of success, they are widely recognized and are subject to intensive study. The latter cannot be said with respect to another source of resource misallocation in urban areas —those that stem from the operation of the public sector itself. Our present system for providing urban public goods and services gives rise to spatial misallocation of resources in addition to exacerbating private market externalities.

There are two principal sources of such misallocation. The major source of local government revenue is the property tax—a tax which tends to discourage investment in housing. The rapid growth of local public services in recent years has led to substantial increases in the rate of the property tax, intensifying resource misallocation in housing. Perhaps more importantly, the rate of property tax is not uniform across an urban area, being substantially higher in the central city. Because poor families tend to be concentrated in the central city, the property tax may bear relatively heavily on the supply of their housing. Furthermore, higher property tax rates tend to inhibit the growth of the city's taxable base, reducing its ability to provide public services which are highly complementary to housing for the urban poor.

The second source of resource misallocation is the result of the redistribution of income implied by our present system of financing urban public services. Since the extent of such redistribution is not uniform across an urban area, locational choice is affected. Specifically, it is more extensive within the central city. This provides incentives for people to relocate to the suburbs. For reasons to be set out in this paper, such incentives are most operative for middle and upper income groups. The result may be to strip the city of such residents, sharply curtailing the city's ability to engage in programs which enhance the quality of low income housing, and/or requiring a property tax rate so high that it greatly diminishes the quantity of housing available for the urban poor. Perhaps more importantly, the "ghettoization" of the central city intensifies the housing and other externalities generally associated with geographic clustering of low income groups.

In what follows, we shall set out these arguments in greater detail, carefully scrutinizing the assumptions that underlie them. In the last section, we discuss their implications for policy and further research.

Fiscal Redistribution

We begin the analysis with a stylized description of the mechanics of income redistribution through the public sector, and its impact upon the spatial distribution of the urban population. Then we shall examine the sensitivity of the conclusions to some of the simplifying assumptions of the model.

Responsibility for the provision and finance of urban public services generally rests with a number of local jurisdictions whose boundaries may or may not overlap. An often observed pattern is a large central city government, whose constituents comprise about half of the urban area's population, and a multiplicity of small suburban local jurisdictions who serve the remainder. Within each jurisdiction, public services are financed by taxes which tend to vary directly with income. The distribution of public services among residents, however, tends to be uncorrelated with income.[1] Unlike private goods and services, therefore, there is no correspondence between payment and benefits received. It follows that the public services of relatively low income individuals are subsidized by high income individuals. The extent of such redistribution will vary directly with the heterogeneity (with respect to income) of residents and the level of public services. If taxes are proportional to income— which approximates reality for most urban local governments—the redistribution cost (benefit) to an individual is proportional to the amount his income exceeds (falls short of) the average for the community as a whole, and to the per capita level of public expenditure.

The preceding would not create a source of resource misallocation if all jurisdictions enjoyed the same distribution of income and provided the same level of public services. This is not the case, however. In the vast majority of large urban areas, the central city houses a disproportionate share of the poor, while the suburbs are populated primarily by middle and upper income groups. Thus, central cities tend to have lower average income as well as larger variance than their suburbs. Making matters worse is the fact that locally financed public expenditure tends to

[1] To the extent that there are services directed toward the poor, e.g., public welfare, there may be a negative correlation between public services consumption and income. For the most part, however, such services are financed by grants from higher levels of government. The statement in the text and similar references thereafter are meant to apply to locally financed services. Nonetheless, if the consumption of locally financed services is negatively correlated with income, the argument which follows is strengthened.

be considerably greater in the central city. To a large measure, this expenditure differential is compensatory in nature and does not reflect true differences in public service levels. The need for compensatory expenditures arises from two principal sources: (1) Clustering of the poor in urban ghettos intensifies problems of crime, fire, public health, substandard housing, etc.; (2) service demand is imposed upon the central city by suburban commuters. From the standpoint of an individual making a residential choice, such compensatory outlays are of no net benefit to him, because they are unnecessary in the suburbs. For example, greater police expenditures are necessary in the central city to afford the same level of personal safety as exists in suburban communities.

Thus, the central city engages in substantially more redistribution through the provision of public services because: (1) Its population is more heterogeneous with respect to income than the suburbs; (2) the benefit per dollar of public expenditure is lower in the central city. It follows that individuals have a fiscal incentive to reside in the suburbs rather than in the central city. This is true for all income groups. For the well-to-do, the redistributive cost is lower in the suburbs, while for the poor the redistributive benefit is greater. However, there are reasons to believe that these incentives are an increasing function of income: (1) Because moving costs tend to have fixed elements, such costs may tend to be a higher fraction of relocation benefits for the poor than for the well-to-do; (2) the redistributive benefits to the poor have a ceiling—per capita, locally financed expenditure—while there is no such ceiling for the well-to-do; (3) the recipient suburban jurisdiction will tend to be much more receptive to high income individuals for reasons similar to those that motivate the individual to relocate in the first place. If the prospective resident's income exceeds the average for the jurisdiction, and public services can be expanded at constant cost, then existing residents will enjoy a redistributive gain. Conversely, those whose income falls below the community's mean will impose a redistributive cost on existing residents. Because local governments have instruments such as zoning at their disposal, they can successfully exclude those who would impose a fiscal burden on them.

For the preceding reasons, then, we can expect fiscal incentives to be much more operative for higher income classes than for lower income groups. To the extent that such fiscal incentives play a major role in the locational choice of middle and upper income groups, we have a mechanism that is self-reinforcing. As the well-to-do begin to leave the central city, the fiscal incentives for those remaining will increase. This will stimulate further outmigration of upper income groups. The process will not stop until all of those whose incomes are above the suburban average have departed. The city will find itself stripped of its middle and upper classes.[2]

The result is to intensify the concentration of poor within the metropolitan area, giving rise to higher public service requirements. Since the poor are confined within the city's boundaries, the city will have to make a substantial fiscal adjustment. If the city attempts to maintain public service standards, the resulting rise in its property tax rate will adversely affect housing investment, and thus increase the cost of housing to low income residents. If, on the other hand, the city chooses to reduce the quality of public services, the quality of housing will deteriorate because most city services are complementary with housing. In either event, the housing services consumed by low income groups will be curtailed. Perhaps the most important impact upon low income housing, however, is the fact that the concentration of poor within the city limits will increase the incidence of poverty. The flight of middle and upper income groups to the suburbs, and the relatively high rate of city property taxes, will encourage business and industry to relocate as well. Given the lack of adequate transportation, the city's poor will be unable to follow employment opportunities to the suburbs. Because the major cause of substandard housing is low income, the resulting unemployment or underemployment will intensify the "housing problem."

Further Consideration

The preceding argument suggests a gloomy outlook for our central cities. To what extent does it square with the facts? There are a number of issues here, including the factual basis for some of my assertions, and the validity of hypotheses concerning the motivation of individuals and local jurisdictions. In this section, I provide evidence to substantiate the model.

First of all, consider the question of city-suburban disparities. In Table 1, selected characteristics of central cities and their suburbs for the 37 largest SMSA's are shown. A cursory

[2] For an explicit model of such a process, see Oates, et al. [1971].

inspection reveals that, as of 1970, most of my generalizations concerning city-suburban differentials are valid. The proportion of poor families residing in central cities is nearly twice that of the suburbs. This is also evidenced by the difference in racial composition of the population, because race and poverty are highly correlated. The preponderance of middle and upper income families in the suburbs is reflected by the fact that, on average, the proportion of homeowners whose house value exceeds $25,000 is nearly twice as high in the suburbs than in the central city. Because homeownership is more prevalent in the suburbs, this probably understates the actual difference. The table also reveals that per capita income in the central city was, on average, 96 percent of that in the suburbs. This difference is smaller than expected. However, the newer cities in the South and West tend to enjoy higher incomes than do their suburbs. The older cities of the Northeast and Midwest, where urban problems are most severe, follow the expected pattern. In Baltimore, for example, per capita income in the central city is only 73 percent of the suburban figure.

Table 1. Central City (CC)—Suburban (OCC) Disparities: 37 Largest SMSA's

	Median 37 Largest SMSA's
Central City population as a percentage of SMSA, 1960	46.1
Central City population as a percentage of SMSA, 1970	40.4
Percent nonwhite in CC, 1970	21
Percentage of households with incomes less than $3000 CC/OCC ratio, 1970	180
Median house values, CC/OCC ratio, 1970	81
Percentage of owner-occupied housing valued at over $25,000, ratio, 1970	56
Per capita income CC/OCC ratio, 1970	96
Per capita expenditures, CC/OCC ratio, 1957	132
Per capita expenditures, CC/OCC ratio, 1970	138
Per capita tax collections, CC/OCC, 1957	152
Per capita tax collections, CC/OCC, 1970	139
Per capita noneducational expenditures, CC/OCC 1957	193
Per capita noneducational expenditures, CC/OCC ratio, 1970	212
Crime rate per 100,000 population, CC/OCC ratio, 1970	245
Percentage population growth, 1960–1970	
Central City	−2.2
Outside Central City	34.3
Central City's share of nonwhite population growth, 1960–1970	82
Percentage increase in median house value 1960–1970 CC	29
OCC	45

Source: Sacks and Callahan (1973).

That local public expenditure and taxes are considerably higher in the central city is also brought out by the table. If we abstract from educational expenditure, the average central city spends more than twice as much as its suburbs, reflecting greater demands for services within the central city. The fact that the crime rate is nearly 2½ times as great in the central city gives further support to this observation. That central cities engage in substantially more redistribution of income through the public sector is quite evident from these figures.

The table also indicates that disparities between cities and suburbs widened significantly during the recent past, corroborating the paper's thesis of central city decay. The population of large central cities has tended to decline. This was the result of a considerable exodus of whites from central cities. It is interesting to note, however, that despite an absolute decline in total population, nonwhite city residents increased rapidly during the 1960's. Indeed, although the central city accounted for less than half the urban area's population, it accounted for over 80 percent of the growth of nonwhite population during the 1960's. Race and income are highly correlated; this suggests that the economic position of central city residents declined relative to the suburbs during the 1960's. This is further evidenced by the fact that the median value of owner-occupied homes increased less rapidly in the city than in the suburbs. Finally, the ratio of city to suburban per capita expenditure widened during the 1960's, while the ratio of per capita taxes diminished. This was made possible by an expansion of intergovernmental grants. Because of the rapid rate of growth of local budgets, however, the absolute gap in per capita taxes widened over this period. Thus, central cities entered the seventies with a greater fiscal disadvantage than existed a decade earlier, and were redistributing income to a relatively greater extent.

Having established that significant socioeconomic and fiscal disparities exist between central city and suburbs, we now turn to the question of whether fiscal incentives provide a major thrust to the exodus of middle and upper income groups from the central city.

The question of residence site choice has come under very heavy scrutiny by urban economists. This work has been so voluminous that it precludes any attempt to survey it here.[3] I will restrict my attention to what I believe to be the findings of major relevance for this paper. First of all, the process of suburbanization or urban decentralization has proceeded extremely rapidly since the late 19th century. For a small sample of metropolitan areas, Mills found that the density gradient, by 1963, had fallen to one-fourth its value for 1880.[4] Much of the initial outward expansion took place within the city border itself. This was made further possible by the expansion of city boundaries. By World War II, however, the boundaries of most large cities became fixed. As a result, much of the postwar suburbanization took place outside the city limits. Indeed, as Table 1 shows, more than all of the urban growth in the typical SMSA during the 1960's occurred outside city limits. This suggests that the fiscal incentives we have discussed were not important before the postwar period, or perhaps even later. The figures in Table 1, however, support the connection that considerable fiscal incentives were present by 1960.

There is general agreement that the process of urban decentralization resulted from three major forces: (1) population growth; (2) income growth; (3) transport cost reduction. Of the three, the last is usually assigned greatest importance. By increasing the supply of accessible land at the urban fringe, transport cost reduction lowered the rent gradient, thus lowering the density gradient. Whether or not fiscal incentives exist, therefore, there are powerful forces inducing people to move to the suburbs. Furthermore, as Muth argues, it is the middle and upper income groups that are most likely to relocate.[5] If the income elasticity of demand for housing services exceeds unity, and transport costs are proportional to the wage rate, upper income groups can be expected to locate at the urban fringe. There are further reasons to believe that middle and upper income groups are relatively attracted to the suburbs. One of the most obvious is that higher income groups have stronger effective demands for lower density and the privacy it affords. Furthermore, as incomes increase over time, people will demand a greater quantity of housing services. This will require the construction of newer, larger homes for the upper income classes. Since building costs, for a variety of reasons, are lower on the urban fringe, these newer homes will be built in the suburbs. By a process of filtration, lower income groups are also able to expand their housing consumption. Because the city's housing structure tends to be older than that of the suburbs, lower income groups will tend to be concentrated in the central city.

Thus, it is clear that there are other forces at work, in addition to fiscal incentives, inducing the exodus of the middle and upper income groups from the city. Indeed, Muth concludes that ". . . the forces influencing the distribution of an urbanized area's population between the central city and its suburbs are very much the same as those which affect the spread of the population within the central city itself."[6] This would appear to contradict our hypothesis that fiscal redistribution plays a major role in residential choice. However, Muth goes on to point out an important exception to his argument: ". . . with a fall in the average income level of the central city relative to its suburbs, the central-city population tends to decline and the urbanized area's land to increase. Although there is no direct evidence, the best explanation for this phenomenon is, I believe, the increased tax burden on higher income households and business firms in the central city . . . ."[7] Apparently, then, fiscal factors cannot be dismissed as insignificant factors in locational choice within a metropolitan area. As Muth correctly points out, however, we have no direct evidence concerning this influence.

While the significance of fiscal incentives probably can be uncovered by a complete, and thus complex, econometric model of residential location, knowledge of the magnitude of fiscal redistribution would be most helpful. Unfortunately, we have little information on this, either. A crude calculation can be made from Table 1. In 1970, taxes per capita were approximately 40 percent higher in the city than in the suburbs, while per capita incomes, on average, were equal. Local tax revenues, in large metropolitan areas, average about 5.5 percent of personal income; it follows that the tax differential amounts to 2.2 percent of personal income. Because the average family tends to devote more than 20 percent of its income for housing, the tax differential amounts to approximately 10 percent of housing expenditure. This hardly would seem sufficient to induce a massive flight to the suburbs.

[3] See for example, Alonso [1964] and Muth [1969].
[4] See Mills [1972].
[5] Muth [1969], ch. 2.
[6] Muth [1969], p. 325.
[7] Ibid.

There are a number of reasons, however, to suspect that a simple comparison of city-suburban tax burdens is an inaccurate measure of fiscal incentives. First of all, it ignores any differences that may exist with respect to the quality of public services. This may be particularly significant for public education. In the eyes of many middle and upper income families, the decision to live in the city simultaneously commits them to send their children to private schools. The cost of private education is not an insignificant fraction of housing expenditure. The cost of private education is equivalent, for practical purposes, to a tax the family must pay if it chooses to reside in the inner city.

Also overlooked by the crude calculation is the fact that the tax differential between city and suburbs is reduced by the process of capitalization. Most likely, the fiscal incentive will lower city property values relative to the suburbs. This means that property tax rates in the city will have to be raised to extract the desired sum. Since the city housing stock will depreciate over time, maintenance and/or new investment outlays are required to keep it intact. Such outlays, however, are taxed at the effective property tax rate, as opposed to the average tax rate with respect to income. Since the city-suburban differential with respect to the former often exceeds that of the latter, the crude calculation above understates the difference in tax burden on investments in housing. This is brought out by an example drawn from the author's recent study of the Baltimore SMSA.[8] Local taxes as a fraction of income, in 1970, amounted to 6 percent in Baltimore City and 4.2 percent in the suburbs.[9] The major source of this difference was the property tax. In 1970, the effective property tax rate was 3 percent in the city, compared with 1.5 percent in the suburbs. If we assume a proportionate relationship between income and local taxes, a family with an income of $15,000 would pay $900 and $630, respectively, if it chose to locate in the city or suburbs. This $270 differential applies if the family lives in an existing home in the city or suburbs. However, if such a family decided to build a new home worth, say, $25,000, its property tax would be $750 in the city and $375 in the suburbs.[10] For a new home, therefore, the tax differential is $105 higher than for an existing home. This difference reflects the fact that property values of comparable existing homes are substantially lower in the city than in the suburbs, perhaps due to fiscal redistribution. Thus, there is greater fiscal incentive to locate new housing in the suburbs than a simple comparison of average tax burdens would indicate.

This discussion suggests that the magnitude of fiscal incentives to relocate to the suburbs cannot adequately be determined by a "back-of-the-envelope" calculation. Rather, it requires a careful cost and benefit accounting that takes into account the quality of public services, demographic characteristics of the potential migrant (i.e. age, family size, etc.), and the difference between the tax treatment of new and existing property. While such a task will involve many difficulties, none is insurmountable. Such estimates are necessary first steps in explaining the role fiscal incentives play in the city-suburban locational choice.

We now turn to the question of the behavior of suburban jurisdictions. It is my view that they are the key actors in the entire central city decay scenario. Recall that there are fiscal incentives for all income groups to migrate to the suburbs. Furthermore, although it has been argued that middle and upper income groups have the strongest nonfiscal incentives to move to the suburbs, it is not true that such incentives do not exist for low income groups. As the urban area becomes decentralized, job opportunities for low income groups will arise in suburban areas. Clearly, it will be in the interests of such employees to seek to reduce their transportation costs. Indeed, for many, commuting from the central city may be prohibitively costly.

The argument that the poor are best housed in the central city because its housing stock is older and easier to convert to low rent uses overlooks a number of considerations.[11] The most important is that to restrict low income groups to the central city is tantamount to perpetuating the poverty cycle and to creating conditions for the proliferation of slums. In addition, it is by no means clear that new low income suburban housing could not be a commercial success. While under current building codes and lot size restrictions, new housing for the poor may not be profitable, these restrictions need not be taken as given. Furthermore, most close-in suburban communities surrounding Northeastern cities are now old enough to provide the basis for profitable conversion of existing housing for low income uses. It is mainly restrictive cove-

[8] Oakland, et al., [1972].

[9] This includes all local taxes: property, income, sales, etc.

[10] A family of four with an income of $15,000 would tend to purchase a home worth $25,000. See Teplin [1973].

[11] An example of this line of reasoning can be found in Muth [1969].

nants, density restrictions, and racial prejudice that stand in the way of such conversion.

Whether or not the central city becomes a low income ghetto is clearly in the hands of suburban jurisdictions. Indeed, the ability of even the middle class to relocate depends upon the willingness of the suburbs to accept them. It is conceivable, although not likely, that the process of central city decay could be halted by the refusal of suburban areas to expand. In such a case, suburban land values would rise to the point where new investment by middle and upper income groups in the central city would become profitable.

It appears important, therefore, that we have a firm understanding of the behavior of local governments in urban areas, including the central city government. The model sketched earlier, although quite simple, is highly suggestive. Its major limitations are that it does not allow for intergovernmental revenues and "congestion" effects of new residents. More importantly, it overlooks other motives guiding suburban government behavior, e.g., racial discrimination. Nevertheless, it provides insight into a potentially important factor affecting the receptiveness of suburban governments to new residents.

Unfortunately there has been no attempt, to my knowledge, to test the model for predictive content. However, a recent study of Baltimore City and its principal suburban counterpart, Baltimore County, provides interesting quantitative information on the question.[12] The objective of the study was to measure the local revenues and expenditures which would result from the introduction of families of different socioeconomic characteristics. One of the principal findings was that a family of four would produce a deficit in both city and county. This was true, in 1970, for a family with an income as high as $22,600. The principal source of the deficit was expenditure upon education. Both jurisdictions appear to have incentives to zone out families with children in public school. Of greater significance, for our purposes, was the finding that the deficit decreased much more rapidly with family income in the county than in the city. Indeed, the size of the deficit in the city was almost invariant to changes in family income. Thus, the county stands to gain much more by "zoning out" low income residents than does the city. One is tempted to speculate that this consideration might have had a lot to do with the fact that the city absorbed virtually all of the increase in the area's poor during the 1960's. Finally, the study found that the deficit for low income families increased eightfold from 1960 to 1970 in the county, while increasing only half as fast in the city. Pressures to "zone out" low income families from suburban communities are evidently increasing rapidly.

The Baltimore study provides valuable evidence that the supply of housing opportunities in the suburbs may be every bit as important as demand considerations in the allocation of population in an urban area. This is of great significance fo Federal policymakers. It may be just as effective, and perhaps more feasible, to increase the supply of suburban housing to low income groups by measures which eliminate incentives for fiscal zoning, such as affecting the demand side through housing subsidies and the like. Unfortunately, this hypothesis is only tentative, since solid general evidence of its validity has yet to be developed. Further study of this question is surely in order. Research, similar to that for Baltimore, should be carried out in other metropolitan areas, and the results should be tested for predictive content.

The Property Tax

We turn next to the property tax. Although I will argue that city-suburban disparities, like fiscal redistribution, are of most importance, there is a substantial body of opinion that the property tax, per se, aggravates housing problems. My initial comments concern the validity of this view. Then I turn to what I feel to be the nub of the problem—city-suburban property tax differentials.

The property tax has received considerably more attention than fiscal redistribution as a contributing factor to housing problems. This possibly reflects the more direct relationship between property taxes and housing, because it is a tax on the value of capital and land inputs used to produce housing services. The latter has led some observers to equate the property tax with a sales tax upon housing services. Dick Netzer, the foremost authority on property taxes, has estimated that in 1962 the property tax had raised the price of housing 24 percent.[13] Since no other good is taxed at such high rates, Netzer concludes that the property tax has considerably reduced the effective demand for housing services. Furthermore, the effect is alleged to

[12] See Teplin [1973].

[13] Netzer [1968], p. 13.

be worse in central cities because of their relatively high property tax rates. Thus, the property tax affects most adversely those whose housing problems are most acute—the low income city dweller.

This view of the property tax has come under critical review in recent years.[14] It is argued that a uniform tax upon capital will not be passed on to consumers, but will be borne by owners of capital. The relative price of capital intensive goods, such as housing, will rise in the long run only if aggregate saving is reduced. Available empirical evidence, however, suggests no such response. Hence, a truly general property tax will be reflected in lower profits and not in higher prices.

The proponents of this view, however, do concede that, to the extent that capital is not taxed uniformly, excise tax effects will result. Because the property tax varies across space and exempts certain classes of real assets, relative prices will be affected. In general, owners of capital will bear the average rate of property tax, while consumers will bear (enjoy) the difference between the average tax rate and the rate of tax on the particular use to which capital is being put. In 1969, the ratio of property taxes to the total stock of privately held tangible assets in the United States was 1.33 percent.[15] On the other hand, the ratio of property taxes paid to the value of residential property was 2.25 percent. Using Netzer's estimates, this would imply an excise tax effect of approximately 10 percent ($.92/2.25 \times 24\%$). Since retail sales taxes tend to average about 4 percent, this means that the relative price of housing is raised by approximately 6 percent—a much smaller distortion than that implied by Netzer.

Even a figure of 6 percent is misleading, however. In order to calculate the excise tax on housing, one should consider all taxes on capital. Since capital is heavily taxed under the corporation and personal income tax, considering the property tax alone could seriously bias the estimates. Indeed, this is the case, since most residential property is exempt from the corporation income tax, and owner-occupied housing is exempt from the personal income tax. Even if we ignore the favorable treatment given owner-occupied housing under the personal income tax, we find that capital invested in housing is taxed less than virtually any other use.[16] Only farm capital is taxed less heavily. If we further allow for the favorable treatment of housing under the personal income tax, it is clear that housing capital is taxed substantially less than the average. Therefore, it is simply not true to say that the present tax structure discourages housing investment. If anything, the United States overinvests in housing. The mounting drive to provide general property tax relief, if successful, will only lead to greater overinvestment in housing. The "housing problem" in the United States is not one of an inadequate average level of housing, but involves the distribution of the housing stock we have. While it may be possible that, by increasing the aggregate supply of housing, we can increase the quantity of housing available to low income groups, such a policy would be a very clumsy and costly method of achieving this objective. It would be much more efficient to design policies that directly increase the supply of housing to lower income groups.

The preceding comments should not make us lose sight of the fact that there is another source of nonuniformity in property taxation—one which is spatial in nature. Thus, while it is true that investment in housing is generally favored by the present tax system, the rate of tax on housing investment varies sharply between central city and suburbs. Netzer found that in 1961, of the 38 largest SMSA's, central city effective property tax rates were higher in all but six.[17] The differences were often quite substantial. In 12 cases, tax rates were more than 25 percent higher in the central city, and in nine cases, they were 40 percent higher. Since the relative fiscal position of cities has tended to deteriorate during the sixties, there is good reason to believe that present property tax differentials are even greater now than in 1961.

The effect of city-suburban property tax differentials is to reduce the relative attractiveness of new investment—including maintenance outlays—in the central city. This might appear to be of greatest significance for the mobile elements of an urban area—middle and upper income groups and business. However, it is not the property tax per se which provides an incentive to relocate, and hence reduce investment outlays in the central city. Essentially the same incentives would exist even if local government were financed through a personal income tax. Because of fiscal redistribution, the value of exist-

[14] See for example, Mieszkowski [1972].

[15] This calculation is based upon estimates of the private capital stock made by Christensen and Jorgenson [1969] and [1972].

[16] See Rosenberg [1969].

[17] Netzer [1968], p. 24.

ing city middle and upper income housing would fall relative to that of the suburbs. This capitalization process acts as a brake on the flight of above-average income groups to the suburbs. When the time comes to replace the wornout city housing stock, however, it will have to be done on the same terms that exist in the suburbs. This means that middle and upper income groups will have to absorb the full amount of fiscal redistribution if they build in the city.[18] Hence, they have an incentive to build in the suburbs. Therefore, the dampening of investment incentives for mobile urban groups is not a unique consequence of the property tax.

The same line of reasoning does not carry over to lower income groups, who, for reasons cited earlier, tend to be locked in the central city. Any factor that tends to reduce the supply of housing available to them will increase their housing costs and lower their consumption of housing services. Because of the relatively high city property tax rate, the attractiveness of real estate investment in the city is reduced. This will reduce the supply of low cost housing in the central city.

There are two reasons to believe that the property tax bears particularly hard on low income housing. First, because homeownership is highly correlated with income, a substantial fraction of low income families are unable to avail themselves of the favorable income tax treatment accorded owner-occupied housing. Second, because of assessment practices, low income housing tends to be taxed at rates substantially above the city average.[19] Because reassessment occurs with a lag, housing in a declining neighborhood tends to be assessed at a higher fraction of its market value than elsewhere in the city. More dangerous, however, is the procedure often used to assess the market value of rental property. Generally, value is determined by applying some multiple of gross rents. Such multipliers are a decreasing function of the age of the structure, since the length of the rental stream declines with age. However, lower income rental units of a given age tend to have lower multipliers than for higher income rental units. This reflects two considerations: (1) Lower income units tend to have shorter economic lives; (2) the ratio of gross to net rents for lower income units is greater because of higher operating costs (see Peterson [1973]). All too often these considerations are overlooked by assessors. The result is higher assessment ratios on lower income rental units. In a study now underway for Baltimore City, I have uncovered numerous instances of assessment ratios of two or more on low income housing units.

While there is general agreement that the property tax adversely affects the supply of low income housing, we have virtually no information concerning the magnitude of its impact. In a recent study of a sample of U.S. cities, however, Peterson et al. could find little evidence that the maintenance and abandonment decisions of low income housing investors were directly affected by property taxes.[20] They found some evidence, however, of an indirect impact because of impediments to the transfer of ownership.

The argument goes something like this: Many low income property owners find themselves with mortgage debt exceeding the value of their property. They are effectively locked in. Their ability to make maintenance outlays is directly related to the cash flow their property generates. Since the property tax reduces this cash flow, it will reduce maintenance outlays. Peterson goes on to hypothesize that bringing assessments into line with market values will not only increase cash flow, but may raise the value of the property sufficiently to enable its owner to sell to someone else who, because mortgage payments are more in line with the market value of the structure, is in a better position to make profitable maintenance outlays.

Implications for Policy

The central theme of this paper has been that fiscal arrangements at the local level exacerbate the housing problem facing the urban poor. This arises from two considerations: (1) The property tax bears heavily upon low income housing; (2) the income redistribution implied by our present system of financing urban public services distorts locational decisions. We now consider policies that may eliminate or at least ameliorate these effects.

[18] This assertion does not allow for capitalization of fiscal redistribution in city land values. If the land presently occupied by upper income housing has no alternative use, full capitalization will result. However, such land has alternative uses; e.g., for housing lower income groups, sites for nonprofit institutions, and commercial and industrial uses. Demand for land by such groups will preclude full capitalization of differential income redistribution.

[19] See Peterson [1973].

[20] Peterson, et al. [1973].

Let us begin with the property tax. For reasons given above, the appropriate policy is one which is directed towards providing relief for the low income segment of the housing market. Two proposals are considered: (1) housing allowances of low income families; (2) the so-called "circuit-breaker."

That housing allowances can overcome the disincentives created by the property tax is straightforward. By subsidizing housing costs, demand will be increased and hence rents increased. The increase in rents will offset property taxes and hence encourage maintenance and rehabilitation expenditures. The major question involves the price elasticity demand for housing. The greater the price elasticity, the lower the subsidiy necessary to offset property tax disincentives.

A "circuit-breaker" is a measure which would place a ceiling on the property taxes a family pays relative to its income. An example of such a measure is Senate Bill 1255 (the Muskie-Percy Bill).[21] Although the intent of circuit-breaker legislation is to mitigate the alleged regressivity of the property tax, it also will offset some of the present disincentive to invest in low income housing. Indeed, as currently proposed, it may more than offset existing disincentives. This owes to the fact that, for rental housing, a generous fraction of gross rent—20 percent—is assumed to be paid in property taxes. If the effective property tax rate is 0.03, this would imply a gross rent-value relationship of nearly 7. Since gross rent multipliers are often much lower in poor city neighborhoods, the formula would overstate the property tax such individuals pay. For example, if a $3,000 income family spends $900 per year on rent, it is assumed that it pays $180 in property taxes. However, if the gross rent multiplier on the house is 3, and the property tax rate is 0.03, the true property tax is only $51. Senate Bill 1255 would provide for a rebate for any tax above 3 percent of income (for a $3,000 income). Hence, the family would be rebated $90, or $39 more than was actually paid on the unit.

The circuit-breaker has come under attack because of its assumptions regarding the incidence of the property tax and its use of money income as a measure of need. The incidence question has been discussed in an earlier section and will not be repeated here. The issue of money income mainly, though not exclusively, relates to the position of the aged. Although an aged person may have substantial assets, such as a home, he may also have low money income. Hence, it is argued that the circuit-breaker gives unwarranted subsidies to such individuals.

The merits of circuit-breakers cannot be pursued further in this paper. Suffice it to say that direct housing subsidies would appear to be superior because they can be better tailored to offset the property tax and do not involve undesired side effects.

Let me turn now to fiscal redistribution. The issues here are more complex and difficult to define than those involving the property tax. Not only do we have the question of the individual's fiscal incentives to relocate, but we have fiscal zoning by suburban jurisdictions and the fiscal viability of the city government. Each of these is intimately related to the distortion produced by fiscal redistribution.

Fiscal redistribution arises because of the divorce between payment of taxes and receipt of services within a jurisdiction. This suggests that if public services were priced in a fashion similar to private services, redistribution could be avoided. While it is clear that certain urban services—such as transportation, recreation, schools, and libraries—could be financed on a user charge basis, and that in some cases allocative efficiency would also be enhanced, there are many services—such as general government, police, fire, health, etc.—which cannot. Furthermore, even if it were feasible to impose user charges, it is not clear that this would prove a satisfactory mode of finance. This certainly would be the case for public schools. User charges carry the implication that the quantity and quality of services consumed are subject to choice by the user. Given their current income, the poor would have to curb their consumption of education drastically; that clearly is not in the interest of society. Although this outcome could be avoided by a voucher system, we are still left with the question of how to finance the vouchers.

The preceding remarks would appear to preclude user charges as a satisfactory mode for financing local public services. The alternative is to finance services on a wider geographic basis —metropolitanwide, statewide, or nationwide. We shall treat these in turn.

Metrowide government has often been proposed as a solution to the present fiscal crisis in our central cities. Because redistribution cannot be avoided by relocation within the urban area itself, it is contended that the present outflux

[21] For a discussion of Senate Bill 1255 and circuit-breakers in general, see Aaron [1973].

from the central city would be mitigated. Furthermore, the resources of the entire urban area rather than just the central city, would be available to be brought to bear on the problems of the urban poor.

While there is little doubt that metropolitan government would eliminate the perverse fiscal incentives that mark the current system, it is not without its shortcomings. First of all, it is not clear that a metrowide constituency would be as sensitive as the present city government is to the problems faced by the poor. Secondly, it would eliminate a mechanism through which individuals can express their preferences for public services. The diversity in the level of local public services that results from a decentralized system of local government gives people the opportunity, by means of their locational choice, to select that bundle of services that most closely corresponds to their preferences.[22] This takes on added significance when it is recognized that the ballot box is a highly imperfect mechanism for expressing preferences, and that centralization inevitably is followed by uniformity.

Despite these limitations, I believe that metrogovernment would constitute a major improvement over current arrangements. While it is true that a decentralized system has advantages vis-a-vis voter preferences, we do not presently have decentralized government in urban areas. What we have is a system by which half of the urban area's population is governed by a single government, and the other half by a multiplicity of governments. Thus, the opportunity to "vote with one's feet" is limited to a select subset of the area's population, at considerable cost to the remainder.

The major shortcoming of metrogovernment as a solution is its lack of feasibility. Such arrangements exist in only a few of our large urban areas—most notably the newest ones, where urban problems are less severe. There is very little reason to believe that suburban communities will voluntarily join with the city under a single government. Although it is conceivable that the State could force consolidation, the present rural-suburban dominance of State legislatures would effectively preclude such an eventuality. Thus, as matters now stand, metrogovernment is no more than a speculative concept.

Since a local government solution seems to be ruled out, we are left with the alternatives of State or Federal intervention. Much of the central city's fiscal plight could be resolved by an aggressive equalization program by the State or Federal Government. That is, centrally collected funds could be channeled to the city through intergovernmental grants. If the level of such funds were sufficient, the level of fiscal redistribution prevailing in the city would be reduced to suburban levels. Thus, not only would the central city be able to provide adequate service levels, but the incentive to migrate from the city would be eliminated. In addition, the present property tax gap would be closed. However, such a system would not affect the attitude of suburban governments to low income migrants—a point to which we shall return.

The prospects for State intervention along these lines appear slim. This is due in part to the lack of city voting power in State legislatures and in part to interstate competition for industry and well-to-do residents. Whatever the reason, however, there is evidence that, with the exception of direct welfare payments, present State aid programs tend to be nonequalizing.

There is, however, mounting pressure in many States for State takeover of the cost of education. This would shift the locus of redistribution through education to the State level. Because educational outlays constitute a substantial fraction of local government budgets, such action by the State could be expected to provide considerable relief. However, this may not in fact be the case. In Maryland, a State takeover would widen the fiscal disparities that now exist between Baltimore City and its suburbs.[23] This stems from the fact that the Federal Government presently provides considerable educational aid to Baltimore City. The result is that the suburbs stand to gain much more by State takeover. I believe that an analysis of other large cities would produce similar results.

Given the apparent reluctance of States to act, resolution of the problem would appear to rest squarely on the shoulders of the Federal Government. This is not surprising, since it is widely recognized that the Federal Government is the most suitable agent for income redistribution activities.[24] Thus far, however, Federal redistributive activity has focused mainly upon private goods and services. Hence we have Federal welfare programs, social security, medicare and medicaid, housing, etc. Since individu-

[22] This point was first made by Tiebout [1956].

[23] Oakland, et al. [1972].

[24] This argument is spelled out in Musgrave [1969; p. 310]. Basically, the reasoning is that sub-national governments should not engage in income redistribution because of the locational distortions which result and because all citizens share the responsibility for and benefits of such activity.

als require public as well as private goods, it seems reasonable to expect that Federal policy should begin to look after the public-goods needs of poor individuals as well. This has been particularly true in recent years, since the share of public goods in individuals' market baskets has risen sharply.

There would seem to be two approaches the Federal Government could follow with respect to public goods redistribution. The first is to provide relief on an individual basis. That is, the Government would provide for the public services of the needy, wherever they may be located. This could be done by payments to the local government in whose jurisdiction the individuals reside. Thus, the Federal Government would write two relief checks. One would be for the individual's private good needs—i.e. the present welfare check—and the other for his public good needs.

The second approach would be to direct Federal aid to those jurisdictions which are heavily populated by low income residents. In practice, this would mean that aid would be funneled to central cities and depressed rural areas. Aid could be restricted to those jurisdictions where the incidence of poverty was above some critical level. This would simplify the administration of the program.

While both approaches are capable of eliminating city-suburban fiscal disparities, there is a strong reason to prefer the first, or individual, approach. This has to do with the incentives for fiscal zoning by suburban jurisdictions. Because each poor individual, under the first approach, carries with him the resources necessary for his public good consumption, suburban jurisdictions would no longer have a fiscal interest in keeping him out.

Such a feature is absent from the second program. While it eliminates the fiscal incentive for the individual to migrate, it leaves unaffected the recipient community's incentives. Since there are powerful nonfiscal incentives to migrate, removing the fiscal incentives alone may do little to alter the composition of population between city and suburbs.

My principal policy recommendation, then, is for the Federal Government to underwrite, on an individual basis, the local public service costs of low income families. The cost to the Federal Government will depend upon the nature of the aid formula and its scope of coverage. Two aid formulas are considered. The first, Plan 1, allocates aid on the basis of per capita local service cost. The second, Plan 2, allocates aid partly on a per capita basis and partly upon education costs. The costs of both programs for fiscal years 1969 and 1973 are shown in Table 2. The 1969 figure is shown because the basic data used in arriving at the estimates were available for that year. The 1973 figures, shown for total program cost only, are projections. These figures give us a better idea of what a presently enacted program would cost.

Let us begin with Plan 1. Here, each person whose income falls below the poverty line is allocated a public service voucher equal to per capita local tax receipts in his community. At first glance, this might appear grossly to underprovide for local public service costs, since taxes finance less than half of local expenditure. However, expenditure financed by grants from higher level governments are not a source of local income redistribution, and hence are not relevant for the problem at hand. The same can be said of non-tax locally derived revenues from charges, licenses, permits, etc. Many of such fees are in the nature of user charges which, by their nature, do not involve redistribution. Thus we need only consider services financed by local taxes.

In 1969, local taxes per capita for the country as a whole amounted to $174. At the same time, there were 24.3 million people classified as poor in the United States. One estimate of a program cost, then, is the product of these figures —$4,225 million. Because this is based upon 1969 figures, adjustments are necessary to bring it forward to 1973. This was done as follows: The poverty population decreased at an annual rate of 5 percent per year during the 1960's. I assume that this trend will continue to 1973; hence, the 1973 poverty population is estimated at 21 million. On the other hand, per capita local taxes have been rising rapidly. Between 1969 and 1971, they grew by 20 percent. I assume that the 1973 figure increased by 15 percent over its 1971 level—to $243. Together, these adjustments imply a program cost of $5,068 million for 1973.

The preceding calculation is admittedly quite simplistic. It ignores the fact that poverty may be concentrated in high tax areas. Furthermore, it can tell us little about the distribution of program benefits among cities, suburbs, and rural areas. To correct for this, separate calculations were made for each of these areas. From Census sources, we can estimate metropolitan and nonmetropolitan tax differentials, and from Table 1 we have an estimate of intrametropolitan tax disparities. Finally, the Census provides data on poverty by place of residence. Using this information, I calculated program costs by area for 1969, as shown in Table 2. Remarkably, the total program cost, $4,229, is almost exactly equal to our first estimate. This suggests that accurate estimates can be made by employing simple aggregates. Nevertheless, this approach enables us to see the distribution of benefits. Central cities are shown to be the major beneficiaries of the program, receiving 57 percent of all benefits. The suburbs, on the other hand, receive only 11 percent of the benefits. As Table 2 shows, the aid under Plan 1 is equivalent to $41 per capita in central cities and only $6.50 in the suburbs. My calculations suggest that, in 1969, the per capita tax gap between cities and suburbs averaged $53. Hence, Plan 1, if it had been in effect, would have eliminated two-thirds of this gap. Thus, the program has the double effect of reducing fiscal incentives to relocate and reducing the incentive to zone out the poor.

We turn now to Plan 2, which takes into consideration the education costs a family may impose on its local government. This is important because education costs are of overwhelming significance in local budgets, absorbing 42 percent of the local tax dollar in 1969. Unlike other government services, school costs vary directly with the number of pupils in the school system as opposed to the size of population per se. Since current outlays per pupil are high, and because grants cover only about half of such costs, a family with school-age children will impose considerably more costs than one without such children. For example, in 1969, locally financed school expenditure averaged $300 per pupil. Plan 1 would assign a family of four with two school age children a voucher of $696. Since local education costs, alone, amount to $600, it is unlikely that such a voucher would prove suffficient to cover all local government service costs.

To allow for the disproportionate role of education, I propose the following scheme. From per capita local taxes, deduct locally financed school costs. In 1969, I estimate the latter to be $72.35. This leaves $101.65 ($174–$72.35) to be allocated on a per capita basis, as under Plan 1. For school costs, we would provide the family with an allowance equal to the number of school age children times the local cost per pupil. As indicated above, in 1969, the latter amounted to approximately $300. Thus, in the average community, our family of four would receive $406.60 in per capita aid and $600 in school aid, for a total of $1006.60.

Table 2. Estimated Program Costs and Distribution of Benefits

	Plan 1		Plan 2	
	FY 1969	FY 1973	FY 1969	FY 1973
Central Cities (total) *	$2,391	n.c.	$2,154	n.c.
Central Cities (per capita)	41.00	n.c.	37.00	n.c.
Suburbs (total) *	471	n.c.	739	n.c.
Suburbs (per capita)	6.50	n.c.	10.20	n.c.
Nonmetropolitan (total) *	1,367	n.c.	1,972	n.c.
Nonmetropolitan (per capita)	19.10	n.c.	27.50	n.c.
Total Costs *	4,229	5,068	4,865	5,839

* millions of dollars
n.c. = not calculated

Since poor families tend to have a greater number of school-age children than do nonpoor families, Plan 2 would be somewhat more expensive than Plan 1, as indicated in Table 2. From Census data, I estimated that, in 1969, there were 7,990,000 school-age poor children. Hence, the education portion of Plan 2 would cost $2,398 million, while the per capita portion would cost $2,468 million—totaling $4,866 million for 1969. Projecting to 1973, we arrive at a total cost of $5,839 million.

Table 2 also shows the breakdown of benefits by area for 1969. It is interesting to note that the central cities allocation under Plan 2 is lower than under Plan 1, despite the fact that the total cost of the former exceeds the latter by 15 percent. This reflects the fact that cities have a smaller proportion of all poor children than they have of all poor individuals. The converse is true for nonmetropolitan areas; hence, they obtain considerably more under Plan 2 than under Plan 1. Whether this pattern will continue in the future —indeed whether it holds for 1973—is difficult to ascertain. The continuing urbanization of the Nation may increase the share received by cities. Lack of more recent demographic data precluded me from making assignments of total costs among areas for 1973. I doubt, however, that the percentage breakdown for 1969 would be significantly altered in the near future.

Let us briefly consider the relative merits of the two plans. Plan 1 has the advantage of providing the greatest relative fiscal relief to the area that needs it most—the central cities. On the other hand, Plan 2 has the advantage of more nearly approximating the marginal public services costs imposed by poor families. In terms of impacts on urban housing patterns, then, Plan 1 does more to reduce incentives to relocate to the suburbs, while Plan 2 does more to remove fiscal barriers to suburban housing for the urban poor. If the tentative hypothesis of this paper is correct, the latter consideration should be given greater weight.

To sum up, the costs of a comprehensive public service program are high but not staggering—$5.1 billion to $5.8 billion. This makes it of the same order of magnitude of general revenue sharing. Furthermore, such a program is conceived in the same spirit as general and special revenue sharing. Indeed, it should be relatively easy to redesign the general revenue sharing program to produce the results of the plans discussed above. Whether the public service voucher is sent directly to the citizen or to his government makes little difference.

Program costs could be considerably reduced if aid were limited to citizens of metropolitan areas or central cities. In the former case, costs would be reduced to approximately $3.4 billion. Since fiscal distortions are most prevalent in urban areas, such a limitation would appear to make sense. Both plans above, particularly Plan 2, provide considerable aid to nonmetropolitan areas. If aid were limited to central cities, program costs would be reduced to $2.5 billion. While this would do much to reduce metropolitan fiscal disparities and reduce fiscal incentives to migrate to the suburbs, it does little to mitigate fiscal zoning by suburban governments.

Even if large-scale measures, such as the above, are beyond reach, there is a lesson to be drawn for HUD policy. The Federal Government has long been striving to induce local suburban governments to accept federally financed public housing. In many instances, HUD has met stubborn resistance. Such resistance may be weakened, however, if, in addition to providing the funds for constructing the housing itself, HUD were to pay the cost of providing local public services to the low income residents. Our calculations above revealed that a family of four, in 1969, imposed local public service costs in excess of $1,000. This figure is even higher in large urban areas. For the typical suburb, I estimate this cost to be over $1,200. Because the amortized cost of public housing unit is also in the $1,000 range, present HUD policy pays only half the cost of accommodating a low income family. Cast in this light, the reluctance of suburban communities to engage in low income housing programs has substantial economic underpinnings. While the proposal would tend to double the cost of present housing programs, it may have substantial payoffs in the form of dispersing the urban poor.

In closing, it is clear that whatever policy actions HUD or other Federal agencies may take in response to the issues raised in this paper, such actions can only be properly formulated with evidence we do not as yet have. While we have been able to offer crude evidence of the magnitude of fiscal redistribution at the local level and of the costs of offsetting it, much more research is needed on this question. Research is also needed to test the hypothesis of the paper—that fiscal incentives of local governments substantially affect the spatial distribution of housing opportunities in an urban area. Given the tremendous diversity of local government arrangements in our large metropolitan areas, it may be possible to test this hypothesis with the use of secondary data.

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The Division of Responsibility for Housing Policy in a Federal System of Government

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This paper addresses the specific proposition that one possible rationale for a Federal housing policy is that "failure to act on the State or local level may require Federal action." This statement, if accepted as correct, assumes that there is a proper role for government intervention in the housing market, that lower levels of government are the appropriate units of intervention, and that the Federal Government should become involved in housing markets only if lower levels of government abdicate their responsibility.

It is important to be careful in selecting an approach to this topic, for it is fraught with potential opportunities for question-begging. First, the statement assumes that there is an appropriate role for government intervention in housing markets. But is there a role? It would seem reasonable that one task of this paper should be to review the grounds on which government intervention in the housing market is justifiable, taking as given the basic commitment to a market economy that is widely shared in the United States, and to describe the characteristics of such a policy. Second, the formulation of this topic assumes that it is possible to determine when lower levels of government have failed to fulfill their obligations, which, in turn, indicates the appropriate corrective action for the Federal Government to undertake. But is it possible to determine when lower levels of government have failed to fulfill their responsibilities? By what criteria is this judgment made? And who makes the judgment that these criteria have been violated? That is, what is the epistemological content of a statement that lower levels of government have failed to fulfill their responsibilities regarding housing policy?

The first task of this paper will be to examine possible rationales for government intervention in the housing market, paying attention to the problem of specifying the level of government appropriate for housing policy. While there are numerous specific rationales, they can generally be summarized into three. The following three sections examine in turn each of the primary rationales, paying special attention to how they relate to the division of responsibility between Federal and State and local governments.

Primary Rationales for Government Intervention in Housing Markets

Even in an extreme laissez faire vision of a market economy, the definition of property rights and the enforcement of contracts is considered a necessary function of government. Even in this laissez faire vision of social order, then, government would participate in the housing market by defining the terms on which contracts concerning housing are enforced, and then enforcing those contracts if necessary. This role as a rulemaker and umpire is a universally acknowledged —anarchists excepted—task of government, for which the participation of government in housing markets provides one instance of fulfilling this task. The objective of this paper is to examine possible rationales for government intervention in housing markets that go beyond the policing and enforcing of contracts.

In what sense, if any, is the collective interest in housing different from the collective interest in, say, automobiles? The quality of automobiles varies greatly among the populace, but, so far at least, there is no government policy of subsidizing the consumption of automobile services so as to upgrade automobile standards.[1]

With housing, by contrast, there is a strong governmental effort to promote increased housing consumption. For instance, there are policies for providing subsidized interest for both owner-occupied and renter-occupied housing, there are special housing subsidy programs for the elderly, there are rent supplements, and there is the public housing program. These programs are designed to combat the presence of substandard

[1] There are, of course, various pollution and safety requirements relating to automobiles, but these are elements relating to the definition of the contractual obligation by which an automobile may be traded among buyers and sellers. There is not, however, a governmental policy of promoting wider ownership of higher quality automobiles.

housing. It is the intention of these programs that by reducing the price to purchasers of standard quality housing, housing standards will rise in quality. Yet no such programs exist with respect to automobiles, even though a part of the present automobile stock is also of substandard quality, and, furthermore, some people own no automobiles. Is there any rationale for this difference in the nature of government intervention in automobile and in housing markets?

Certain people gain from any public policy, and such persons are normally ingenious in generating rationalizations for such policies. In the case of housing policy, numerous specific rationalizations have crept into discussions of policy. It is claimed that poorer persons will be unable to afford decent housing without subsidization, that it is important and valuable to the community at large to counteract housing deterioration and community decay, that zoning and building codes restrict the supply of housing, that discrimination interferes with the operation of a free market in housing, and that housing programs are necessary to offset the effects of such programs as urban renewal and highway construction in destroying housing units.

Numerous other specific arguments can also be found in the literature. The myriad of specific arguments, however, can for the most part be condensed into three primary rationales for government intervention in housing markets. One rationale is based upon alleged imperfections in the operation of the housing market. If such imperfections are significantly strong, some form of housing policy might be necessary to offset the deleterious effects of these imperfections. Otherwise, there will be insufficient investment in housing, thereby promoting the existence of substandard housing. A second, related rationale is based upon alleged externalities in personal choices concerning housing consumption. If one person's decision concerning how much and what type of housing to consume imposes costs or confers benefits on others, there may exist some collective interest in decisions regarding housing consumption. For instance, if increased expenditure on housing by persons who consume substandard housing were to generate external benefits for others, the personal decisions of consumers might yield an insufficient expenditure on housing. A third rationale deals with income redistribution. The lower a person's income, the greater must be the percentage of income spent on housing in order to purchase standard rather than substandard housing. Some people suggest that this necessary percentage might be excessively large in the lower income ranges. Subsidized housing then becomes a means of transferring income to those in the lower income ranges.[2]

In the next three sections I shall examine the market imperfection, externality, and income redistribution rationales for government intervention in housing markets, paying particular attention to what these rationales imply about the relative responsibilities of Federal and State and local governments. The problem of trying to judge when a lower level of government has failed to fulfill its obligation, and whether such failure justifies Federal intervention, is a particularly complex one. The following may be seen by way of a brief illustration; more detailed discussion will appear in subsequent sections.

Suppose it is felt that a deterioration in housing quality in one area inflicts costs on other areas. Within limits, then, it would be profitable for other residents of the locality to invest in some program for financing improvements in housing quality in the offending area. Now, suppose a particular locality is observed to make no expenditure for such a program of housing subsidy. Does this "failure to act" present a case for Federal intervention in the local housing market? Under the postulated conditions, some subsidy program is a good business proposition to the remaining members of the locality. If this good business proposition is not undertaken, local taxpayers are harming themselves because they could get a greater return on their tax dollars at the margin if they were invested in such a subsidy program that if they were invested in other uses.

The question of Federal intervention and financing raises a question as to why residents of other areas in the Nation should subsidize benefits for a particular locality when the residents of that particular locality are themselves unwilling to undertake such a good business proposition? The failure of the locality to act quite likely indicates that such spillover benefits are not viewed by local residents as being significant, or perhaps even extant. In this case, the failure of the locality to act is quite understandable, and can hardly be labeled a "failure." While there would be no rationale for government intervention in this latter case, it is quite possible that federal intervention would take place nonetheless. There are well-known theorems of political economy that show that, when benefits are

[2] As will be evident from the following discussion, it is often extremely difficult to distinguish this redistributive rationale from the externality rationale.

highly concentrated while tax payments are diffused, excessive expenditure on such programs is likely to result.[3] Hence, government intervention could emerge from political processes at the Federal level even though the conditions postulated by the rationale were invalid—that is, even though the program being subsidized did not conform to the conditions necessary to justify the subsidy in the first place.

Market Imperfection as a Rationale for Government Intervention in Housing Markets

It is often suggested that investment in housing is retarded because of market imperfections that operate to make the gross rate of return on housing exceed the gross rate of return on other investments. If the gross rate of return on housing exceeds the gross rate of return on other forms of capital, the total return from the economy's capital stock could be increased by shifting capital from other forms to housing until gross rates of return are equalized. Such a disparity in gross rates of return, then, would indicate that the stock of housing was inefficiently small relative to the stock of other forms of capital. Zoning and building code regulations, and the operation of capital and credit markets, are the most frequently cited instances of market imperfections that operate to retard investment in housing. More specifically, it is claimed that zoning creates an inefficient segregation of housing by quality of units and income levels of residents, that building codes increase the cost of housing, and that credit markets fail to extend credit to fully efficient amounts.

Zoning is frequently cited as a market imperfection that decreases the supply of housing, consequently bringing forth frequent proposals to curtail the zoning powers of local governments. In what sense, if at all, can zoning be considered a market imperfection? First, it should be noted that "zoning" is not synonymous with "restrictions on the use of land." Houston, Texas, for instance, has no zoning ordinance. Yet the uses to which property in various neighborhoods in Houston may be put is regulated by restrictive covenants. These covenants are the spontaneous outgrowth of the operation of a competitive market in land, and their functioning illustrates that a competitive market in urban land—one operating without zoning commissions and regulations—will not be the uncoordinated, disharmonious mess that zoning apologists so often claim.[4]

Moreover, to some extent a zoning ordinance might simply accomplish more or less what would otherwise have been accomplished through the operation of market-generated covenants. The minimal lot sizes that were established by a zoning board, for instance, might approach those sizes that would have emerged through the operation of a free market in urban land. There would seem to be reasonable grounds for suggesting that, at least as a first approximation, a zoning ordinance would tend to serve as a reasonably close substitute for a free market in urban land, such as is found in Houston. This possibility concerning zoning may be explored by examining the implications of the opposite possibility—that is, by examining the implications for property ownership and local political processes if it is assumed that zoning generally produces inefficient patterns of land use.

If zoning did indeed operate as a market imperfection, it would imply that property was zoned in such a manner that the net rate of return to land-owners would be less than what it would be if the locality had a free market in urban land. In any locality there will be some pattern of land use that will maximize aggregate property values within that locality. Suppose a zoning commission were to establish minimal lot sizes that were inefficiently large. If such a result were to transpire, the aggregate value of property contained within the locality would be less than what it would be if minimal lot sizes were smaller. Under such circumstances, a locality, by reducing minimal lot sizes, could attract additional residents in such a manner that the contribution of such residents to the locality's tax base would exceed the additional cost of providing them with public services. Hence, if zoning operated as a market imperfection, the net rate of return to landowners-residents would be less than it would be under a free market in urban land. The size of this divergence between the two rates of return would indicate the size of the capital loss imposed by inefficient zoning on the owners of land situated in the locality.

If zoning operates as a market imperfection, then, it implies that zoning boards are not re-

[3] See James M. Buchanan and Gordon Tullock, *The Calculus of Consent* (Ann Arbor: University of Michigan Press, 1962), pp. 131–69.

[4] For a thorough examination of the Houston case, see Bernard H. Siegan, "Non-Zoning in Houston," *Journal of Law and Economics*, 13 (April 1970), 71–147.

sponsive to the aggregative interests of landowners. If zoning boards were responsive to such aggregative interests, zoning regulations would tend to approximate what would have resulted from the operation of a free market in urban land. There are reasons for suggesting that zoning boards will not be perfectly responsive to the aggregative interests of landowners. Zoning regulations grant licensing privileges to a zoning board, and such a regulatory agency has the ability to confer monopoly privileges. Consequently, zoning, as with regulation generally, will tend to generate monopoly rents by restricting treated at the State and local levels of government.[5]

Policies that maximize the net wealth of the members of the zoning board, or of a majority of the members of the zoning board, or even of a majority of the landowners in the locality, will not necessarily, nor even generally, maximize the aggregate value of land situated within the locality. The existence of zoning makes it possible to create monopoly rents through the operation of the land market. Whenever monopoly rents can be created by regulation, it is very likely that they will be created. Hence, while zoning choices—like political choices generally—will tend to reflect citizen preferences, this approximation or tendency is not the same thing as saying that zoning is a perfect substitute for a competitive market in restrictions on urban land. A monopolist, after all, also tends to reflect consumer preferences, but this tendency does not imply that competition and monopoly are perfect substitutes.

There is a tendency, then, for land use under zoning to approximate land use in a free market. This is only a general tendency, however, for zoning will serve only as an imperfect substitute for a free market in urban land. Despite this imperfect substitutability, however, it is questionable to what extent any such imperfections that might exist can be said to constitute a rationale for offsetting action by the Federal Government. That residents of a particular locality may be less wealthy than they could be because the land market operates imperfectly due to zoning may be unfortunate for such residents. But several remedies for such a situation are available at the State and local level, so any imperfection that may exist seems to provide at most a tenuous rationale for Federal intervention in housing markets. Such localized imperfections clearly seem to be an issue more appropriately treated at the State and local levels of government.[6]

More specific than a restriction of the supply of housing generally, it is frequently claimed that zoning restricts the supply of low income housing especially, particularly in more affluent areas. It is undeniable that low quality housing is not generally interspersed with high quality housing. This observation, however, would hardly seem to indicate a market imperfection; if anything, it would seem to indicate the contrary. Free markets in land, such as those found in Houston, produce quite similar housing patterns as those found in zoned cities. The present residents of a locality generally will want to attract residents so long as the marginal tax revenue generated by additional residents exceeds the marginal cost of providing public services to those residents. If, in addition, a locality is constrained to provide approximately equal services to all residents, the locality will tend toward homogeneity in the composition of its residents. That the residents of a locality consisting of one-quarter acre, single family residences would not want a high density, low income apartment development in their midst does not indicate a market imperfection. On the contrary, it would seem to indicate that land markets are operating relatively efficiently.

While zoning is unlikely to perform exactly as a free market in urban land, the controversy over zoning seems to have little to do with market imperfections. Homogeneous housing patterns also exist in Houston; this suggests that homogeneity is a likely outcome of a competitive market. The opposition to zoning does not seem to reflect a concern that local residents and propertyowners are being exploited by a monopolistic zoning board, and does not seem to be motivated by a desire to enable local residents to maximize the aggregate value of property in the locality. Rather, the opposition to zoning seems primarily to reflect the dislike by some people of the outcome of individual choices as reflected in market processes. That is, the controversy over zoning exists because some people dislike the pattern of housing produced by a reasonably

[5] For a careful analysis of this general point concerning regulation in general, see George J. Stigler, "The Theory of Economic Regulation," *Bell Journal of Economics and Management Science*, 2 (Spring 1971), 3–21.

[6] This is not to deny that a localized problem that is common to many localities will not in fact, through the operation of poitical processes, come to be treated at the federal level. Such a result, however, will often reflect the ability of majority coalitions to secure favored treatment for themselves despite the creation of a net social loss. On this point, see Richard E. Wagner, *The Fiscal Organization of American Federalism* (Chicago: Markham, 1971), pp. 41–46.

competitive market. In any market, of course, those with larger incomes will be able to make larger purchases. This is as true for housing as for anything else. To object to the distribution of income, however, is quite a different matter than to call a market imperfect.

It is often argued that building codes inject an additional element of imperfection into the operation of housing markets. In fact, building codes and zoning regulations can be viewed as complementary institutions. Zoning regulations operate to increase the cost of the land upon which a structure is to be placed; building codes operate to increase the cost of the structure that is to be placed on the land. Building codes increase the cost of construction, for instance, by requiring thicker foundations, by requiring heavier electrical wiring, or by requiring more costly plumbing installations.[7] Building codes, then, it is suggested, operate similarly to featherbedding in that both institutions operate to increase the cost of production from what it need be.

The issues surrounding building codes are quite similar to those surrounding zoning, so they can be treated in considerably less detail here. Three points can be made: First, if building codes truly operate as a market imperfection, propertyowners in the locality will be earning a lower rate of return on their property than they could earn if building codes were not so restrictive. Second, if building codes do indeed operate as a market imperfection, the imperfection is highly localized, so it is questionable whether a rationale for Federal internvetion is created. Third, the concern over building codes, as with the concern over zoning, seems at base primarily to reflect a concern about the consequences of competitive market allocation with a particular distribution of income, rather than reflecting a concern about market imperfection itself.

Besides zoning and building codes, it is sometimes suggested that credit and capital markets also operate imperfectly, thereby restricting the supply of housing. It is especially suggested that the supply of credit to lower income persons is inefficiently low, thus exacerbating the difficulty they face in purchasing standard quality housing. Interest charges, of course, form a substantial share of payments for housing, and such charges generally rise with income. Because mortgage interest is deductible in determining Federal tax liability, and because the relative use of itemized deductions rises with income, the provision for deductibility is a policy that makes the amount of subsidy rise with income. While deductibility gives relatively larger subsidies to persons with larger incomes, much of the allegation concerning imperfect credit markets nonetheless seems to reflect a concern with the distribution of income rather than a belief that credit markets are imperfect. If the concern about imperfect credit markets were the dominant one, no rationale would be provided for making subsidized interest loans to lower income persons. Instead, there would be a desire to see that all persons faced the same interest rate, aside from differences due to variations in riskiness and lending terms. Considerations of riskiness and lending terms, of course, would generally operate to produce lower interest rates for higher income borrowers. With such a policy, however, it is doubtful whether mortgage interest could continue reasonably to be deductible in determining Federal tax liability.

One strand of the argument that credit markets operate imperfectly implies that lenders are passing up opportunities to make profitable loans. An argument that the supply of credit to lower income families is inefficiently low implies that an expansion of credit to such persons would be profitable to lenders. There is reason for suggesting that managers of monopolized firms will be less vigorous in monitoring their firm's activities, and in pursuing profit opportunities, than managers of competitive firms.[8] The greater the risk associated with a potential borrower, the greater the required expenditure of managerial effort in deciding about the case and in monitoring it. To the extent that the enterprise is monopolistic, which enables managers to relax in pursuing their activities, managers will curtail higher-risk lending more sharply than lower-risk lending. The net return on the firm's capital will be less than it could be, and lower income families, who would tend to be disproportionately represented in higher-risk classes, will be unable to borrow as much as they could in a competitive market. Such a point as this one, however, argues not so much for a Federal housing program as for policies designed to promote greater competition in financial markets—markets that

[7] Until 1966, for instance, the construction of timber-framed houses was forbidden in London. See F. G. Pennance and Hamish Gray, *Choice in Housing* (London: Institute for Economic Affairs, 1968), p. 8.

[8] See Arman A. Alchian and Reuben A. Kessel, "Competition, Monopoly, and the Pursuit of Pecuniary Gain," in *Aspects of Labor Economics*, Universities—National Bureau of Economic Research, Special Conference Series, No. 14 (Princeton: Princeton University Press, 1962), pp. 157–75.

currently are among the most highly regulated and, hence, monopolistic of all markets.[9]

Standing in contrast to the preceding discussion of market imperfections that might operate to curtail the supply of housing, moreover, are other imperfections that seem to operate to stimulate investment in housing rather than to retard it. The presence of the corporation income tax is the major illustration of such a market imperfection. Because the tax on income from capital invested in the corporate sector exceeds the tax on income from capital invested in housing, the gross rate of return on corporate capital will exceed the gross rate of return on housing capital. This condition concerning gross rates of return is necessary to attain an equality of net rates of return, and it indicates that the social productivity of corporate capital exceeds the social productivity of housing capital. Furthermore, the bias toward housing capital that is produced by the corporation income tax is compounded by the deductibility of mortgage interest payments under the federal income tax. The provision for deductibility subsidizes the price paid for housing, thus encouraging investment in housing. Simultaneously, the taxation of the income from corporate capital discourages corporate investment. Both policies, then, operate to expand investment in housing relative to investment in corporate enterprise. Corporate taxation, especially, and interest deductibility to a lesser extent, then, are market imperfections that promote excessive investment in housing. Consequently, while various market imperfections may impinge upon the operation of the housing market, they work in offsetting directions, though not necessarily in offsetting magnitudes, as some imperfections operate to stimulate investment in housing rather than to retard such investment.[10]

Consumption Externalities as a Rationale for Government Intervention in Housing Markets

It is often claimed that poor housing inflicts external costs on others, or, conversely, that an increase in the quality of housing units in the lower quality ranges, would confer external benefits on others. If this is the case, a person's choice concerning housing consumption will not be made with full cognizance of all the costs and benefits of his choice. If the external cost of low quality housing could somehow be incorporated into personal housing decisions, housing standards would rise, especially in the lower quality ranges. It is often claimed, for example, that an increase in housing standards in the lower quality range, besides increasing housing standards for tenants, will also reduce crime rates, reduce the incidence of contagious disease, and reduce future burdens on welfare rolls, to name a few possibilities.

If third parties should indeed benefit marginally from increased housing consumption by residents of substandard units, purely private decisions concerning housing consumption will produce an inefficiently low consumption of housing. Some subsidization of housing consumption is one possible means of promoting an increase in the quality of housing units. Moreover, if the external costs from substandard housing increase as the quality of housing becomes poorer, an efficient subsidization program will require that the amount of subsidy vary inversely with the quality of the housing unit. To the extent that housing quality varies directly with income, income could replace housing quality as a variable for determining the amount of subsidy in such a subsidy program.

To observe a correlation between poor quality housing and such things as crime, disease, and broken families, does not, of course, necessarily imply that an improvement in housing standards will alleviate these ills—as experience with public housing projects has perhaps tended to show. Moreover, the existence of social costs due to substandard housing does not necessarily imply that subsidization of housing consumption is required. A program of taxing the source of the external diseconomy would entail the taxation of substandard units of housing to discourage the nonconsumption of housing. In this case, the tax placed on substandard units would vary inversely with the quality of the unit. Additionally, the presence of substandard units could be reduced or eliminated by regulation. This could be accomplished simply by prohibiting occupancy of housing units that fall below minimal quality standards. The presence of substandard housing units combined with a desire to eradicate or reduce such housing, then, does not require the existence of a positive, as distinct from

[9] As an illustration of how regulation may be used to suppress competitive pressures, the Federal Home Loan Bank announced on 20 June 1973 that it would continue to refuse to permit the use of variable-rate mortgages to supplement fixed-rate mortgages. The failure to permit variable-rate mortgages means that the risk associated with mortgage loans will continue to be greater than it might be, with the result being a higher price of mortgage loans to reflect the greater risk.

[10] This is not to deny, however, that some imperfections impinge relatively more heavily on persons with relatively lower incomes.

a negative, housing program. A desire to insure minimal quality standards does not necessarily require a positive policy of providing those units. A negative policy of prohibiting units below those standards is another possibility.

There are some obvious distributional differences between a positive and a negative policy, although either policy seems capable of insuring that housing units at least attain some minimal quality standard.[11] The positive policy would subsidize persons with relatively low incomes while the negative policy would tax them. If either policy were equally efficient and subject to equal administrative cost, a person's choice among these programs would be based upon his own preferences concerning the distribution of income. If one program were more efficient than the other, however, the efficient program should be chosen, with any adverse distributional consequences being corrected through monetary transfers. Although it is an empirical matter, it seems likely that a positive policy would be more effective in promoting the attainment of minimal quality standards than a negative policy. A policy of subsidizing consumption can rely primarily upon market-generated information regarding housing expenditure and personal income. A negative policy of taxing nonconsumption, however, would confront the absence of market-revealed data on "nonconsumption." It would be necessary to take information on consumption, develop some measure of desired consumption, and label the difference, "nonconsumption." Therefore, it would seem likely to be more costly to implement a negative policy for raising housing standards than to implement a positive policy.

Thus, the existence of consumption externalities associated with low quality housing seems more likely to provide an argument for the subsidization of acceptable housing than for the taxation or regulatory prohibition of unacceptable housing. It is questionable, however, whether the existence of such externalities can reasonably be used to provide a rationale for Federal rather than State or local government action. Any such external costs from crime, disease, and broken families would seem to be highly localized. Due to personal mobility, some of these external costs will pass beyond neighborhood and city boundaries, and a lesser amount will pass beyond State boundaries. This latter possibility provides an argument for Federal as contrasted with State and local action. The contribution of the Federal Government, however, would be a relatively small share of the total subsidy payment.

One might object to this analysis by claiming that while most external costs remain localized, local governments fail to act in such matters; this leaves Federal action as the only alternative. If such external costs do indeed exist, a subsidy program would contribute more to enhance the value of property within the locality than would other uses of the funds. Therefore, to argue that local governments fail to act efficiently is to argue either that their residents do not know what is best for them or that there are substantial imperfections in the operation of local political processes. If the former is held, there is no reason at all for assuming that people who do not know what is good for them at one level of government suddenly find out what is good for them when their affairs are transferred to a higher level. If the latter is held, there is substantial evidence to suggest that national political processes do not operate any less imperfectly.[12] Neither argument, then, produces much of a case for a Federal housing policy to deal with whatever externalities might be associated with the consumption of housing.

It is possible that the external economies associated with housing consumption would manifest themselves only after a substantial lapse of time. The significant externalities may be due not to such things as reductions in the threat of disease, fire, and crime, but, rather, may revolve around possible longrun changes in the characteristics of the recipients of housing subsidies. Residents of low-quality housing often have not only poorly marketable labor skills but also are unable to provide a home environment that is conducive to the acquirement by their children of personal characteristics that are likely to produce future success in the labor market. If the increase in housing consumption were somehow able to promote the cultivation of a set of personal characteristics by parents and, probably more importantly, by children, that would generate greater income prospects in the future, then the program would reduce the future dependence of such persons on public support. Given the high rate of mobility that exists in the United States, such external economies would seem to require action by the Federal Government, because a lower level of government would lose a significant share of the benefits of its expenditure through the out-migration of recipients.

[11] See Ronald H. Coase, "The Problem of Social Cost," *Journal of Law and Economics*, 3 (October 1960), 1–44.

[12] See Charles M. Tiebout, "A Pure Theory of Local Expenditure," *Journal of Political Economy*, 64 (October 1956), 416–424.

Scattered-site housing is an illustration that comes immediately to mind. If this type of long-run, dynamical process were to be set in motion by such a housing program, the recipient families might acquire habits and modes of behavior—presumably via demonstration effects from neighboring families—that were more consistent with success in the labor market. This would hold for parents, of course, but it would seem to be an even more important consideration concerning children.

The opposite result is also conceivable, of course, and no analysis or evidence yet exists to present a firm basis for choosing between the two possibilities. If this opposite result should transpire, such a housing program would generate external diseconomics rather than external economies. The result might not be that children and parents in lower income families acquire, through learning via demonstration, habits and characteristics consistent with success in the labor market. Rather, the result might be that children and parents in upper income families come to acquire, again through learning via demonstration, habits and characteristics less consistent with success in the labor market. Rather than unmotivated children suddenly becoming motivated, formerly motivated children may become less motivated. A still further possibility is some movement in both directions—some regression toward the mean. In any event, to summarize, such a policy might be akin to moving an asthmatic from Florida to Arizona; but then again, it might be akin to moving a tuberculosis patient into a crowded rooming house.

Income Redistribution as a Rationale for Government Intervention in Housing Markets

The final rationale for governmental intervention in the housing market is distributional, with subsidized housing being used as a vehicle for transferring income among persons. Several specific arguments commonly advanced in support of government intervention in housing markets are, at base, derived from the existence of persons with low incomes. Income redistribution is a theme that underlies nearly all discussion concerning housing policy, though this theme is usually submerged within other themes. When the issues are untangled, however, there would seem to be little in the way of a housing policy that would survive if it were not for the existence of low income persons.

The argument that the housing market cannot or should not be relied upon to produce and allocate housing reflects a basic dislike by some people of market allocations, which, in turn, reflects their dislike of the distribution of income. The concern over zoning and building codes, for example, cannot readily be explained as reflecting a concern about market imperfections. Rather, such concern seems largely to reflect the desire of some people that certain classes of citizens should receive differentially favored treatment with respect to the price they pay for housing and the public services they receive from their associated tax payments. That is, certain persons should be able to purchase housing at prices that are lower than they would confront in a competitive market. Similarly, the discussion about imperfect capital and credit markets does not seem substantially to reflect a concern that such markets operate inefficiently. Rather, the discussion seems to reflect the belief by some persons that certain other citizens should be able to confront lower interest rates than they would confront in a competitive market.

Even most externality arguments seem, at base, to be redistributional arguments. Questions of administrative cost aside, the primary objection that would be raised against a negative policy for reducing substandard housing would be the distributional objection that such a policy would be especially burdensome to lower income families. The only externality argument that does not seem to collapse into a redistribution argument is the possibility that certain forms of housing programs may create more productive citizens in the future by somehow inducing a change in personal characteristics and attitudes. If such a process were to exist, and in the correct direction, the attainment of someone's desired income distribution might still leave unexploited an opportunity for a housing program to promote such demonstration-effect external economies. But this would seem to be the only nonredistributive rationale for government intervention in the housing market—as contrasted with government action to increase competitiveness of housing markets.

Thus, it would seem as though the case for a government housing policy would rest primarily upon the effort to transfer income. A certain class of citizens is to be subsidized via its consumption of housing, with the subsidy being paid by the remainder of the taxpaying citizenry. Defense of this position, in turn, should rest upon the superior performance characteristics of redistribution in kind via housing subsidies, as against redistribution through monetary transfers.

Suppose a certain amount is to be transferred to lower income citizens. This might be accomplished through some such program as a negative income tax or a wage subsidy. Or it might be accomplished through a program of subsidizing housing expenditure, perhaps a subsidy whereby the rate of subsidy declines with rises in expenditure on housing. Under what circumstances would the housing subsidy be preferable to the negative income tax as a means of transferring income? Because some higher income families have relatively low housing expenditures, and because some lower income families have relatively high housing expenditures, an income transfer program in which the amount of transfer was based on housing consumption would necessarily involve numerous instances where higher income families received larger subsidies than lower income families. Therefore, the use of housing subsidies as a means of transferring income would seem to perform poorly in comparison with a negative income tax. Hence, there would seem to be no case for using housing subsidies as the instrument for pursuing a policy of income redistribution. Therefore, while it is widely acknowledged that income redistribution is more appropriately a function of the Federal Government than of State and local governments, the issue of the appropriate level of government for using housing subsidies to transfer income does not seem germane to an examination of rationales for Federal intervention in housing markets.

Conclusion

The main thrust of this paper has been that the case for government intervention in the housing market seems generally to be weak, especially at the Federal level. Much of the support for housing subsidies stems from the existence of low income persons, and would be dissipated if the income levels of such persons should rise. Since some persons with relatively high income live in substandard housing while other persons with relatively low income live in standard housing, income transfers would seem superior to housing subsidies as an instrument for transferring income.

Hence, the case for government intervention in housing markets—as distinct from a policy of government action to permit housing markets to become more competitive—would seem to rest upon the existence of external effects associated with housing consumption. While empirical evidence on these externalities is scanty to date, it would nonetheless seem to form the primary rationale for public intervention in housing markets. Such possible externalities from substandard housing as crime, fire, and disease would seem, however, to call primarily for local action. And if local governments should be observed not to act, it seems more likely that the reason for this inaction is that the external benefits are not felt to exist than that local governments are plagued by political failure. A rationale for Federal intervention in housing markets would seem to require the aforementioned longrun, demonstration externalities, which may or may not exist, and which may be either external economies or external diseconomies.

The Role of New Construction Subsidies in National Housing Policy

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Summary

There has been steady and impressive progress in reducing the incidence of substandard housing in the United States. Nevertheless, there remains a large role for public policy in accelerating the rate of progress for the Nation as a whole and for subgroups of the population, particularly families close to or below poverty levels.

We choose to attack the housing problem directly rather than relying solely on income transfers for two reasons. One is that we cannot realistically expect the Congress to enact income transfer programs in the near future that will eliminate poverty altogether, but we seem to be able to transfer some income to the poor in the form of housing and other commodities and incomes. The second reason is more fundamental: We believe that the housing market, left to its own devices, does not generate the socially desirable quantity and quality of housing, especially for the lower end of the income distribution, even in the absence of absolute poverty.

Traditionally, we have intervened on the supply side of the market, through the encouragement of new construction by public authorities, or by private builders with government subsidies. Such intervention has been widely criticized. Many projects have had dismal experiences: some, financial; others, poor and deteriorating housing conditions and asocial behavior. The size and location of many projects have been counterproductive in terms of social and economic integration. Past commitments have awesome projected budgetary costs. These programs generate serious inequities among the poor.

These disappointments generate interest in other approaches focusing on the existing stock of housing and on demand side measures. Rent vouchers not dictating form and location of supply, except for minimum standards, avoid the pitfalls of new construction strategies. But this approach has difficulties from political and economic standpoints. Inadequate voucher levels and supply inelasticities constrain this strategy's potential. Supply side intervention remains essential to achieve greater supply elasticity. Subsidies for new construction thus complement a demand approach if used effectively in eliminating barriers to supply.

Introduction

Although the vast majority of Americans live in decent housing, as suggested by the figures in Table 1, the problem of inadequate housing still occupies a very high position on the Nation's agenda of issues requiring public attention and the expenditure of tax resources. Despite considerable disagreement on strategies and goals, nobody is seriously suggesting that we should depend entirely on the workings of the private market for further progress in achieving improved housing standards. In part this reflects the unequal progress by race and area so that, again referring to Table 1, the incidence of poor housing is much greater among Negroes and outside urban areas. In part it reflects the conviction that, despite the statistics, conditions are getting worse rather than better in many city neighborhoods. Finally, and perhaps of greatest relevance to this paper, is the fact that the cost of housing rises almost as fast as income so that, despite general economic progress, people whose income has moved up at the average national rate have to devote an ever larger proportion of their income to improve the quality of their housing.[1]

It is this latter phenomenon which creates a prima facie case for the subsidization of the construction of new housing as an important component of a strategy to improve the nation's housing stock. In this paper we shall focus on this aspect of public policy, its rationale, the record and the experience of past and present programs, and suggestions for modifications of such policies in the future.

[1] James Heilbrun, *Urban Economics and Public Policy,* New York, St. Martin's Press, 1974, p. 249.

Table 1. Trends in the Condition of Urban and Rural Housing by Race of Occupants, 1950–70

	PERCENTAGE OF ALL OCCUPIED UNITS							
	OVERCROWDED (OCCUPIED BY 1.01 OR MORE PERSONS PER ROOM)			SUBSTANDARD (DILAPIDATED OR LACKING COMPLETE PLUMBING FACILITIES) [3]			PERCENTAGE CHANGE, 1960–70, IN PROPORTION	
	1970	1960	1950	1970	1960	1950	Overcrowded	Substandard
All Races								
Total U.S.	8.2%	11.5%	15.7%	6.0%	16.0%	35.4%	−29%	−62%
Urban	7.6	10.2	13.3	3.1	9.6	21.9	−25	−67
Rural	10.1	15.1	20.6	14.5	32.6	62.4	−33	−56
White [1]								
Total U.S.	6.9	9.7	13.3	4.8	13.0	31.8	−29	−63
Urban	6.3	8.5	—	2.4	7.0	18.2	−26	−66
Rural	8.8	12.9	—	11.4	28.0	59.1	−32	−59
Negro [2]								
Total U.S.	19.9	28.3	32.0	16.9	44.0	73.2	−30	−62
Urban	18.1	24.7	—	8.5	31.8	61.2	−27	−73
Rural	30.1	40.8	—	62.3	85.5	96.3	−26	−27

[1] In 1950 and 1960 this category includes only whites; in 1970 it includes whites and other races, except Negro.
[2] In 1950 and 1960 this category includes all nonwhites; in 1970 it includes only Negroes.
[3] Since data on dilapidation were not available, figures for 1970 refer to plumbing condition only.
Sources: U.S. Bureau of the Census, *Census of Population and Housing, 1950, 1960,* and *1970;* and Housing and Home Finance Agency, *Our Nonwhite Population and Its Housing,* July 1963.

Rationale and Objectives

Why is housing an issue for public policy? In the jargon of economics, there are both efficiency and equity motives for intervention. To isolate the efficiency motive, imagine a society with complete income equality. In such circumstances the case for intervention rests on the suspicion that there are such significant gaps between the private and the social calculations of benefits and costs that the results of unconstrained private decisions would be viewed by the group as nonoptimal, namely, that an alternative set of outcomes would be preferred.

Where are the gaps?

1. The gap between the private and the social valuation of the benefits of good housing to the individual. This is an elitist view of unproven validity. But what is maintained is that many of us do not fully appreciate the beneficiary byproducts of good housing to ourselves (and our children) so that, left to ourselves, we would tend to spend less on housing than we "should." A similar argument is made for education.

2. The gap between the benefit to the individual and the benefit to society that arises out of the importance we attach to the quality and other aspects of other people's housing. In other words, you may be satisfied with your shack but I'm not satisfied with your shack for a variety of reasons. First, I don't like to look at shacks, especially if they're on my block. Second, shacks are more combustible and that costs me money, either in fire insurance or in taxes to pay for a bigger local fire department. I can't readily make you share these extra costs to me unless we come together and make some collective choices.

The potential for generating "external" benefits and costs from individual acts of production or consumption is pervasive, but we don't necessarily intervene in every case to alter private decisions, because the costs of administration would be too great. However, because housing is so visible, so permanent, and so important in shaping the quality of the environment, the externalities are sufficiently strong and persistent to justify intervention.

Thus, we make housing cheaper to encourage greater consumption of housing. But intervention takes many forms, it should be noted, and subsidization is only one of them. We also intervene to regulate the quality of housing (codes) and the location of housing and the relation of housing to size of lot (zoning).

One would have thought that the amount of subsidy justified by efficiency arguments would be modest, especially as incomes increased and gave "natural" encouragement to the consumption of more housing. But, as Henry Aaron [2] and others have so forcefully pointed out, the subsidy implicit in the tax treatment of home ownership is by far the most expensive federal housing program. The benefits of this "program" accrue very heavily to the nonpoor. In fact, because of the structure of the federal income tax, the richer you are, the cheaper is an extra investment in housing insofar as interest and local property taxes are concerned.

Such subsidies are also defended on the grounds that, when middle- and upper-income people purchase more expensive housing, they vacate good quality housing which "filters" down to the poor. This is an argument we shall deal with in detail below. It applies not only to the implicit subsidy via the tax laws but also to the explicit subsidization of new construction aimed at nonpoor buyers and tenants.

Let us now turn to the equity aspects of the rationale for public intervention in the housing market. In this context, housing subsidies are viewed as a mechanism for achieving income redistribution, hence, a greater degree of equality.

Why should we resort to housing subsidies and not just straight transfers of cash to achieve that goal? There are three answers to this question. One rests on the same fundamentally elitist view discussed earlier, namely, that we know better than the poor what is best for them—specifically, that good housing is more important than other goods and services they might choose to purchase with their cash payments.

A second answer flows from a fundamentally selfish interpretation of the redistributive urge. We really don't "bleed" for the poor except as their condition adversely affects the quality of our lives. Among other things, we are annoyed by slums and their consequences and we are willing to spend our income to improve the housing of the poor more than we are willing to improve their general welfare. Here the equity and efficiency arguments are joined.

Finally, and most persuasively:

> Housing subsidies are an expedient way of redistributing income to the poor. Thus one might favor such subsidies while remaining skeptical about the merits good or external benefits arguments. Economists have generally agreed that income redistribution is most efficiently accomplished not by making transfers in kind, but by making cash transfers which leave the recipient free to choose whatever additional goods he most desires. Yet the "realist" who wishes to redistribute income may believe that it is politically easier to legislate adequate transfers in kind than in cash, and that this consideration outweighs the contrary argument based on economic efficiency.[3]

Do these different answers have important implications for the goals of policy? They do. If the motive for action is the poor quality of housing occupied by poor people, then the goal of policy ought to be to provide every family with adequate housing and to pursue that goal stubbornly until it is achieved. If the motive for action is income redistribution, then we should abandon housing policies as soon as we discover more efficient ways, which are also politically acceptable, of redistributing income in adequate answers.

Do these different answers have important implications for the choice of policy tools? They do. The current popularity of rent vouchers, for example, could be based on the fundamental preference for straight income transfers, which are better approximated by rent vouchers than by subsidies to new construction or improved maintenance. One does not have to argue that rent vouchers are more effective in raising housing standards as one would have to if the goal of policy is, in fact, not just income redistribution but redistribution in a particular form, namely, housing. If we fail to design a rent voucher system of a sort that guarantees that the poor will spend more on housing but can get congressional approval nevertheless, why bother?

In evaluating policies to encourage new construction, I shall assume that the goal of policy is better housing for the poor and near-poor. But, given our uncertainty about the side-effects of good housing, we can only define goals in terms of housing conditions, namely, to bring within closer reach of the low- and moderate-income family a wider choice of housing options of good quality in preferred locations and to accomplish that objective at the lowest possible cost to the taxpayer.

Public Housing

The most direct application of the strategy of new construction to improve housing opportunities for the poor is public housing. This program has been in operation for 35 years and has resulted in the construction of a little over 1,000,000 units. Such housing now accounts for 1.4 percent of the total stock of housing, and for approximately 4 percent of the housing occupied by households with incomes less than $6,000.[4] It

[2] Henry Aaron, *Shelter and Subsidies*, Washington, D.C., Brookings Institution, 1972, p. 53.

[3] Heilbrun, op. cit., p. 264.

[4] Aaron, op. cit., p. 115.

is true, however, that the bulk of public housing is occupied by poor people and, in that sense, the program is effective, i.e., it is well targeted.

As originally envisioned, a much greater number of public housing units were to be built. For example, the Housing Act of 1949 called for the construction of 810,000 units in 6 years, an amount close to what has actually been built in 35 years. The recent record has been considerably better than the average for the entire period: approximately 100,000 per year in the last 3 years. Thus, the program has become more vigorous with age.

The failure to achieve more ambitious quantitative goals can be attributed only in part to serious reservations about the quality of the program. The fact is that, despite the many criticisms which we shall detail below, the "demand" for public housing on the part of eligible tenants has been strong. "Most projects have extremely low vacancy rates and long waiting lists for admission." [5]

Moreover, this very gap between supply and demand is itself one of the major issues raised by critics. It is unfair, they argue, to offer such a substantial subsidy ($2,100 per year, on average [6]) to such a small proportion of low-income people. This gross violation of equity—the unequal treatment of equals—also greatly complicates the administration of the program. A lot of time and energy and frustration is devoted to the tenant selection process at the level of the individual project, and to project selection at the level of the local public authority and at the federal level. This is a generic problem which has plagued many underfunded social programs in the last ten years. But there is hardly another example where the violation of individual equity is so clear-cut. If only one out of ten depressed areas can get an EDA grant, that is one kind of problem. But if only one out of ten poor people can get a $2,100 subsidy, that is another kind of problem.

To anticipate somewhat, it is precisely the latter kind of problem that helps to generate a preference for rent vouchers as opposed to subsidized construction. If you operate with an inadequate budget on the supply side, you cannot avoid this kind of inequity, because the subsidy is not sufficiently divisible. If you tried to spread the limited budget over a very much larger number of projects and housing units, you could hardly afford to build housing that meets minimum social standards. You could supply every poor person with a tent. On the other hand, the rent voucher is perfectly divisible. In the extreme, you can give each poor person a one-dollar voucher; it will not buy him much in the way of housing, but at least everyone would receive the same treatment. Based on an average subsidy of $2,100 for 10 per cent of the poor, the same public outlay would allow for $210 vouchers for all. Obviously, equitable programs which are grossly inadequate are not the answer, either.

Other difficulties with public housing may also stem in part from its limited quantitative impact but may, nevertheless, be considered apart from that issue.

Public housing typically has been built in large-scale, multibuilding projects, often covering a large number of acres. These projects have been widely criticised for their uninspired architecture and inhuman scale. Their interior amenities reflect the deliberate imposition of a "no frills" policy. Consequently, it has long been predicted that public housing projects, though built at great expense, are destined to be the slums of the future. In some cases they have already taken on the characteristics of slum neighborhoods.

Income limits imposed on tenants both for admission and for continued occupancy also raise difficult problems. On the one hand, such limits seem necessary in order to confine the substantial benefits of public housing to those most in need. On the other hand, they produce a public housing population with a high concentration of poverty and distress. The income limitations for continued occupancy provide a direct disincentive to individual self-improvement.

"The most serious criticism leveled at the conventional public housing program is that it fosters racial and economic segregation, both within neighborhoods of central cities and between central cities and suburbs. Nonwhites made up more than 50% of public housing tenantry in 1970, a proportion that was, in fact, far higher than their share of the central city poverty population in the same year. Since projects tend to be large, the high proportion of nonwhite tenants in a project automatically establishes a degree of neighborhood segregation. At the same time, efforts to reduce such segregation by scattering smaller projects through white neighborhoods often arouse intense local opposition from whites, who fear an influx of the nonwhite popu-

[5] Aaron, op. cit., p. 108.
[6] *Setting National Priorities, the 1974 Budget,* Washington, D.C., The Brookings Institution, 1973, p. 137.

lation that they know to be typical in public housing."[7]

The Alternative of "Leased" Public Housing: A potentially important improvement in public housing policy was introduced by the "Section 23" leasing program, enacted in 1965. Section 23 permits local housing authorities to lease units in privately owned and operated buildings and sublet them at low rents to their usual clientele. Thus, public housing tenants can live among tenants in conventional buildings and existing neighborhoods instead of being concentrated into "projects." Congress has sought to encourage use of Section 23 by requiring that 30 percent of assistance funds for future expansion of the public housing stock be contracted for leased units.

A leasing program can also contribute to three other goals. If the units are leased in new buildings (as some have been), the program stimulates new construction and helps expand the supply of new housing. On the other hand, if units are leased in older buildings and neighborhoods, the program can be used to help arrest housing deterioration. The rents paid by tenants plus the contributions added by the local housing authority are sufficient to cover standard maintenance and operating costs. Finally, a leasing program can contribute to racial and economic integration by placing tenants in appropriately chosen neighborhoods.

In many of the older central cities, the housing supply is shrinking because demand is weak. As the population thins out, relatively good older housing becomes available at moderate cost. Therefore, a policy that makes effective use of the older stock makes more economic sense than one which attempts to stimulate new construction and thereby actually accelerates wasteful abandonment of existing structures. The leasing program is thus a variant of the demand approach to subsidization of low income housing to the extent that it is directed away from new construction and toward utilization of the older stock.

Subsidized Private Housing

By far the most important components of subsidized new construction in the last few years have been the units built by private developers with financial assistance from government. The figures are shown in Table 2. Note that of the total of 439,000 subsidized units in 1971, for example, 236,000 were built with assistance provided under Sections 235 and 236 of the 1968 Housing and Urban Development Act alone. (I shall assume that the reader is generally familiar with the nature of the financial provisions available under these sections as well as the older 221(d)(3) provisions and concentrate instead on the issues raised by these forms of subsidy and the experience of these programs to date.)

In the most general terms, these programs are aimed at the stimulation of private construction of units to be offered to eligible tenants at prices or rents substantially below the costs that would be incurred by the private builder if there were no government subsidies. The subsidy ultimately takes one of two forms: the artificial reduction of capital costs via interest rates substantially below market rates, and/or the flow of revenues to the builder supplementing the rent paid by the tenant. The latter form, which dominates current activity, has the distinct advantage that the amount of subsidy can be varied with the income of the tenant, so that tenants with different incomes pay different amounts, and the same tenant will pay different amounts as his income varies.

These programs, unlike public housing, have indeed produced impressive quantitative results, as indicated above. If they are "working," in that sense, what are the qualitative faults which have brought these programs into question?

The recent freeze was unquestionably motivated by reported scandals and the very large-looming budgetary implications associated with these programs. But these urgencies aside, the direction of housing policy implied in these programs has also been challenged. An obvious question is: Do these programs expand housing opportunities for the poor and near-poor? The answer varies from program to program, as seen in Table 3. The most effective program, it would seem, is rent supplements, in which tenants with incomes less than $4,000 accounted for 93 percent of the units. The least effective is Home-Ownership Assistance (235), in which 80 percent of the beneficiaries have incomes of more than $5,000, and 29 percent have incomes of more than $7,000. But this measure of effectiveness ignores the relative numbers of people assisted by each program. While the rent supplement program reaches down deeper into the income distribution, because the average cost per tenant is very high, the total number of poor people

[7] Heilbrun, op. cit., p. 272.

Table 2. Housing Production Toward the National Housing Goal

	Fiscal Years — Thousands of Units Produced				
	1969	1970	1971	Est'd 1972	Est'd 1973
Total Production of New Units	1,969	1,762	2,233	2,750	—
Unsubsidized production—total	1,806	1,466	1,794	2,330	—
Construction	1,437	1,063	1,359	1,780	—
Mobile homes	369	403	435	550	—
Subsidized production—total	163	296	439	420	496
1 to 4 family homes	32	108	207	212	249
Section 235	8	70	136	137	157
Other	24	38	71	75	92
Multiple dwellings	132	189	232	209	247
Public housing	64	83	92	57	62
Conventional	36	29	25	19	15
Turnkey and leased	28	55	68	38	47
Section 236	1	49	100	134	158
Rent supplement	16	22	15	10	18
Section 221(d)(3)	39	24	11	4	1
Other	12	11	14	4	8

Source: President of the United States, *Fourth Annual Report on National Housing Goals*, Washington, D.C., June 29, 1972, Table 1, p. 9, and Table B-2, pp. 44–45.

affected is much smaller per $1 million of outlay than is the case under the 235 and 236 assistance programs.

Table 3. Distribution of Tenants in Homeowner and Rental Assistance Programs, by Income

Characteristic	Percentage of all tenants in program: Below-market-interest-rate loans (1968)	Rent supplements (1969)	Home-ownership assistance (1971)	Rental assistance (1970)
Income bracket (dollars)				
Under 1,000	0.3	7.7	—	—
1,000–1,999	2.5	41.1	—	—
2,000–2,999	4.7	27.3	1.1	10.7
3,000–3,999	10.1	17.0	4.2	13.5
4,000–4,999	17.0	5.7	15.2	23.5
5,000–5,999	22.6	1.2	25.7	25.6
6,000–6,999	21.6	0.1	25.0	17.6
7,000–7,999	12.5	—	16.8	6.6
8,000–8,999	5.3	—	7.7	1.9
9,000–9,999	1.9	—	2.8	0.4
10,000 and over	1.5	—	1.5	0.2

Source: Henry J. Aaron, *Shelter and Subsidies*, Washington, D.C.: The Brookings Institution, 1972, p. 130.

This "illustrates the brutal choice of housing assistance—whether to concentrate assistance on the poorest households whose need is presumably greatest or to spread assistance among more households whose deprivation is less severe." [8]

Do the poor benefit additionally from 235 and 236 programs through the process of filtering? Aaron reports on a study of Columbus, Ohio, which concluded that 235 and 236 projects in that city "reach more households indirectly through filtering than either rent supplements or low rent public housing. . . . Homeownership assistance affected more than three times as many households and more than one and a half times as many poor households as did the rent supplement program per dollar spent." [9]

As we suggested at the outset, the validity of the "filtering" concept is crucial to an assessment of the antipoverty effectiveness of all assistance programs that are not directly accessible to the poor. Even the massive subsidies implicit in the federal tax treatment of mortgage interest and local property taxes acquire some modicum of respectability if we put credence in the filtering process. To quote Aaron: "Until 1970, United States housing subsidies added up unambiguously to a filtering strategy." [10]

The seminal critique of filtering was developed by Lowry in a paper published in 1960,[11]

[8] Aaron, op. cit., p. 143.
[9] Ibid.
[10] Aaron, op. cit., p. 163.
[11] Ira S. Lowry, "Filtering and Housing Standards: A Conceptual Analysis," *Land Economics*, Volume 36, No. 4, Nov. 1960, pp. 362–70.

at a time when Lowry claimed that there were only "four publications which deal with the subject at any length" and that "the partisans of filtering . . . have never put anything in writing" which articulates their model of housing market behavior. The ideas developed by Lowry in 1960 were fundamental to his late 1960's analysis of and policy recommendations for the housing crisis in New York City.

The fundamental point in Lowry's paper is that housing quality depends as much or more on the flow of maintenance expenditures as it does on the age or other attributes of the structure. Even assuming that the capital costs of sound structures are reduced through a process of filtering—an assumption which is by no means valid in all circumstances—the operating costs of maintaining good quality are beyond the means of poor households. Thus, the filtering process ultimately leads to a decline in quality below acceptable standards and is self-defeating. This is especially true if operating costs rise at a more rapid rate than the income of the poor households, as has certainly been the case in recent decades.

The Demand Side Strategy

The limitations of public housing and subsidized private housing in meeting the housing needs of the poor and the near-poor have engendered a growing preference for subsidy programs which operate on the demand side of the market. The logic of this, put in its best possible light, runs as follows: If you enhance the rent-paying or purchasing power of poor households, they will be able to afford better housing in the private market. Responding to the pressure of their greater demand, producers, without the benefit of complicated subsidy programs, will make the additional higher quality housing available either by upgrading the existing stock or by new construction that may be appropriate in particular situations.

The arguments in favor of the demand side approach are formidable. Incentives to economize are preserved on both sides of the market. The tenant or the buyer has resources which he can devote to other uses and will be looking for the best housing bargain. Since the supplier is subject to the usual degree of competition because he does not have a captive customer, he will be under the usual pressure to offer as much quality as an acceptable profit margin will permit.

The subsidized household will have greater freedom of choice of location because the family's money is good everywhere, and households will not be constrained as they are now by the limited number of sites on which subsidized housing is built. On average, therefore, the demand subsidy should lead to greater racial and economic integration.

Administrative costs are assumed to be much lower, though not trivial, for a demand-oriented subsidy. It is necessary to monitor incomes, and that is not a simple task. But it is not necessary to go through the complex application preparation and review process and then, forever, the complex monitoring process. The need for planning is greatly diminished.

As suggested earlier, demand subsidies are also more attractive than supply subsidies on equity grounds. In either case, you cannot do the whole job in a period which is so short that you can afford to overlook the inequities that occur in the process. But on the demand side you can distribute the anguish somewhat more evenly than you can on the supply side, where one is clearly "in" and the other is clearly "out."

Proponents of demand subsidies have been careful not to paint such an idealistic picture. They fear for inadequate and improper supply side responses and have insisted that, at a minimum, the poor tenant or buyer should have some extra consumer protection. They are also concerned that many poor households may elect not to use any of their augmented purchasing power for housing and, despite their preference for consumer sovereignty, they would like to see better housing result from a housing subsidy program.

There are enough uncertainties regarding the working of a housing allowance approach to the subsidization of housing to justify caution and experimentation, and this is where we are at this point in the development of housing policy. The important question for this paper is whether inevitably, on the most optimistic outcomes of the experiments, there will be and should be a role for the subsidization of new construction as part of our national housing policy, and, if so, what form should such subsidization take?

What Role for New Construction?

Taking into account a number of factors limiting their effectiveness, we must conclude that complete reliance on demand side strategies is not likely to yield an acceptable rate of progress in housing quality for low- and moderate-income households.

First, one cannot realistically expect Congress to move quickly to adopt levels of income transfers and/or rent vouchers of sufficient magnitude. Second, one must reckon with supply inelasticities that will negate part of the additional purchasing power. These inelasticities will occur for a variety of reasons, some general, some specific. A very substantial general increase in demand will inevitably result in higher prices in the short run because the supply of both labor and capital to the construction industry is not perfectly elastic in the short run. The uneven spatial distribution of the poor creates additional problems. In the central city, housing sites are in limited supply, but there is the alternative of upgrading the existing stock. In the suburbs, zoning laws introduce an artificial limitation of supply.

But if we are to operate simultaneously on the supply side, we do not necessarily improve matters unless we focus on the removal of barriers to greater elasticity. The simple provision of subsidies for new construction—as, for example, under 235 and 236—does not solve the problem of inelasticity, unless we assume that labor, capital, and land are mobilized more quickly in response to these subsidies than they are in response to the direct demand pressure of the renter or buyer. This will be true only if supply subsidies are employed strategically in combination with other measures to ease supply adjustments or to take advantage of otherwise favorable supply situations which are not likely to be exploited by the private market in response to demand pressure alone.

Supply subsidies must be used as an incentive to removing the barriers of zoning, housing codes, unionization, land assembly costs, and other resistances to more elastic supply. Otherwise, supply subsidies and demand subsidies are indistinguishable in their impact on prices in the short run, except insofar as we can assume that government, acting somewhat like a monopolist, will exact a lower price than will an unorganized group of buyers with equivalent purchasing power. But the logic of that result calls for a more limited quantity of new construction, or renovation of the existing stock.

If we could operate directly on the factors which limit supply, subsidies for new construction could be justified only as being more politically acceptable than demand subsidies. I suppose we have made some progress by direct assaults on zoning laws, housing codes, etc. But that progress has been slow. If it can be accelerated by the skillful manipulation of supply subsidies, we ought to be willing to live with some of the unavoidable inefficiencies of intervention on the supply side.

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Credit for Financing Housing Investment: Risk Factors and Capital Markets

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Summary

The major objective of this paper was to consider the mechanism through which financial markets influence housing investment, and to evaluate current and future roles for government policies in these markets. The focus of the paper was further narrowed, in view of space and time limitations, to the consideration of two basic topics: On the microeconomic level, the effects of risk factors on mortgage borrowers and the location of housing collateral were developed; on the macroeconomic level, the question of whether the free capital markets could provide an adequate amount of housing finance was investigated. The conclusions that were drawn for government policy with respect to these two questions were quite different. With regard to the microeconomic question of risk factors, the general conclusion was that government intervention could be useful under conditions in which risk factors have caused certain mortgage markets to cease to function effectively. On the other hand, with regard to the macroeconomic functioning of the capital markets, the general conclusion was that there were only limited opportunities for government intervention on this level. The following two paragraphs give a more specific summary for each of these questions.

On the level of microeconomic risk factors, the basic theoretical point is that risk factors can make markets, which otherwise would have operated normally, fail to operate effectively. Furthermore, when such failure does occur, it is the minority groups and poor income classes generally who will suffer. Indeed, the market failure is likely to take the form that these groups will be denied access to mortgage markets, almost regardless of the mortgage interest rate that they offer to pay. Consequently, it is under these circumstances that government intervention in the mortgage markets can be very useful. As indicated, the government intervention can take a variety of forms, including further government insurance programs, aid and subsidies to already existing lending institutions, and aid and subsidies to new forms of institutional lending.

On the level of the macroeconomic functioning of the capital markets, an aggregate model of the mortgage markets was developed in the text. The key point that comes out of such a model is the importance of the variability of the mortgage-house ratio. The empirical evidence strongly indicates that programs that attempt to create permanently an augmented flow of mortgage funds are likely to fail both because only the mortgage-house ratio will change (without a significant effect on housing investment) and because the general level of interest rates simply will be driven up. The implication, therefore, is that government intervention on this level will not be efficient, and the stress should be instead on housing subsidy programs and the general array of institutional changes suggested in the Hunt Commission programs. Attention was paid, however, to two more specific problems—the cyclical variability of housing, and the imbalances in regional mortgage and housing markets. The general conclusion with respect to the regional imbalances was that this was not a major problem, although some Hunt Commission proposals relating to it should be considered, and the problem reevaluated at a later date. With regard to the cyclical variability of housing, this was acknowledged as a more major problem, although, by definition, it occurs only in a short run (one or two quarter) context. In this context, however, it was indicated that government programs that attempt to augment the private market supply of mortgage funds could be effective, but it was stressed that the value of these programs was limited to a very shortrun effectiveness.

Part I: Introduction

The major objective of this paper is to consider the mechanism through which financial markets influence housing investment, and to

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evaluate current and future roles for government intervention in this process. A thorough study of this topic would exceed the time and space allowed here. Consequently, I have significantly narrowed my attention to what I consider the two most important and fundamental questions.

The first of these questions relates to the means by which factors of risk interact with mortgage locations and specific borrowers. This inquiry is developed on a microeconomic level, and the main issue is whether the risk factors are such that government intervention in mortgage and housing markets might be deemed useful. The material on this topic is contained in Part II of the paper.

The second question is placed on a macroeconomic level and relates to the issue of whether the free capital markets provide a sufficient volume of housing finance. The basic concern of this topic, therefore, is with questions of the aggregate volume of housing investment. The material on this topic is contained in Part III of the paper.

Part II: Risk Factors Involved With Mortgage Locations and Borrowers

II.1 Introduction

The major focus of this part concerns the implications of risk factors on mortgage loans for the intervention of government in the operation of mortgage markets. It is useful to be precise at the outset about the meaning of risk factors and government intervention as developed in the report. On the broadest level, there are basically three types of risk that are faced by an investor lending funds on a mortgage. First, there is the risk of delinquency and default on the loan. The factors that determine this risk relate primarily to the specific borrower, although the nature of the collateral may be indirectly relevant. Second, there is the risk relating to the realized value of the collateral (the house) should default occur. Obviously, this risk is reduced on an ex ante basis, the smaller the loan to (expected) value ratio of the contract. Third, there are market risks for the lender. A basic market risk, of course, is the possibility that market rates of interest will rise in the future, creating an implicit or explicit capital loss on the mortgage contract for the lender. Other market risks include factors relating to unexpected inflation and, in the case of depository intermediaries, to unexpected changes in deposit rates and deposit flows. In this part, we are concerned only with the implications for the mortgage market of the risks relating to delinquency and default on one hand, and to the realized value of the collateral on the other. The risks due to market factors are considered in Part III.

With respect to the question of government intervention, there are two fundamental grounds on which the government may intervene in the operation of mortgage markets. First, it may be the case that mortgage markets are failing to operate effectively. The term "effectively," of course, is itself not objective, so that some standard or reference must be used in judging whether a market is operating effectively. Granting this problem, however, the point is that government intervention may be useful if the private markets do not operate effectively on their own. Second, even if mortgage markets do operate effectively, the government may wish to subsidize either mortgage loans or housing on the basis of social priorities. The premise in this case would be not that the market is failing, but that consumers are failing in not buying the socially desired quantity of housing or that the income distribution is wrong. In this part, the main emphasis is placed on the grounds for government intervention when mortgage markets fail to operate effectively. Again, the issue of subsidies to mortgages and housing is discussed in greater length in Part III.

Thus, in summary, this report is primarily directed at the question of whether factors of risk arising from delinquency, default, and housing values can cause mortgage markets to fail to operate effectively, and if so, what are the major policies for government intervention that are available? The remainder of this part is divided into three sections. In section II.2, the theoretical economic question of how risk factors can lead to market failure is considered. This theoretical material provides the starting point for any serious investigation of the operation of mortgage markets and for consideration of possible roles for government intervention. In section II.3 the actual operation of mortgage markets, and the various areas in which the markets do and do not effectively handle the problems of risk, are considered. In addition to the general considerations, the discussion also considers the issues of "red-line," of "reasonable cost" for mortgage credit, and of whether risk premia on mortgages are capricous or justified by experience. In section II.4, the major conclusions of the part are summarized in terms of general and specific proposals for the role of government intervention in the mortgage markets.

II.2 The Principles of Risk

It is useful first to review the standard analysis of general equilibrium and welfare economics. The starting point of the standard analysis is an economy consisting of large numbers of household units that consume goods and services—hereafter called consumers—and of manufacturing units that produce the goods and services—hereafter called firms and companies. The final array of prices, factor uses, and produced goods of an economy using a private enterprise market mechanism is termed the general equilibrium of the system. The analysis of the properties of the general equilibrium solution, particularly in terms of the allocational efficiency of factors and goods and in terms of the equity of the distribution of income, is labeled welfare economics. Perhaps the most important propositions available from economic theory concern the optimality properties of factor and goods allocation and at least the descriptive properties of income distribution that are valid for the general equilibrium of a perfectly competitive market system. Conversely, welfare economics is equally concerned with the nonoptimal features of a system in which perfect competition breaks down, and with the possible roles for government intervention in such cases. As a simple example, we know that generally the price of goods should equal its marginal cost of production; and should the market achieve only a higher price, then there may be grounds for government subsidization of the production of the good.

While we shall continue to have in mind an economic system of the type just outlined, our point of emphasis is a system or market in which risk is a critical feature. Economists think of risk as a commodity or characteristic of commodities much as, say, vitamin B_{12} is a commodity or characteristic of certain foods. One can then consider markets that specialize in risk—that is, in which risk is bought and sold—and these are generally called futures markets and/or insurance markets. Through the early 1950's the analysis of economic systems with risk is best described as sublime. Culminating in the classic work of G. Debreu (1959), it was shown that the basic welfare properties of an economic system continue to hold even with risk, as long as futures markets and insurance markets exist and function properly. Unfortunately, this begs the basic real-world question—namely, do markets for risk exist, and do they, in fact, function properly? Or to put the question on the other side—are there grounds for expecting that risk markets will fail under the same conditions that normal markets operate properly? Fortunately, these questions have been studied extensively in the last 20 years, particularly by Professor Kenneth Arrow ((1971), Chapter 8.)

The answers to these questions that are developed in the studies of Arrow and others, are difficult, both in terms of the analysis and the contents. Also, one can understand, in the context of the present situation of HUD, that there may be a strong incliniation to scrub theory, when practical solutions are required immediately. It should be argued strongly, however, that in matters of risk, and particularly as they apply to mortgage and other loan markets, an understanding of the theory developed by Arrow is absolutely critical in proceeding to any sort of systematic solution of the problems. On the other hand, having done this, one is then in a position to confront directly the specific institutional structures of mortgage markets and the possibilities for government intervention in these markets.

The major theme of the literature on risk is that markets, which otherwise would have operated perfectly, break down in the presence of risk and uncertainty. Then, in the absence of normal functioning markets, a number of nonmarket institutions and modus operandi arise in order to perform the necessary economic exchanges. These nonmarket structures, furthermore, have the important and unfortunate feature that they do not meet the standards of allocational efficiency, or even of equity, that we generally associate with normally operating markets. Consequently, there arises a potential role for government intervention; namely, to regulate the nonmarket structures in such a way to achieve allocational efficiency and equitable distributions, or to subsidize the market mechanism in such a way that it operates in a more normal fashion, or, finally, for the government itself to operate the market.

II.2.a The "Pure" Case of Risk-Neutral Investors Purchasing "Objective" Risk: To begin, it is necessary to define two terms: "risk-neutrality" and "objective risk." Risk-neutrality is a characteristic of an individual investor's reaction to risk. It is best illustrated and defined by a simple example. Consider a coin-flipping game using an honest coin with 50 percent probabilities for both heads and tails, and in which you pay a fee (say \$1) to play and receive a prize (perhaps \$2) if heads appears. Given the probabilities, it should be clear that the game may be termed (actuarial) fair if the payoff ratio (prize/fee) is in fact 2. Similarly, the game is termed unfair if the payoff ratio is less than 2; and it is actuarial favorable if the payoff ratio is more than 2.

Now, an individual is described as risk-neutral if he will freely play only favorable games, and he is indifferent between playing or not playing an actuarial fair game. Also, an individual can be defined as risk-averse if he will never play an actuarial fair game, and, in fact, he can be induced to play at all only by offering him a sufficiently favorable game.

The term objective risk describes the nature of the risk or uncertainty that the investor faces. A simple, although not rigorously complete definition, is that objective risk is risk that is common knowledge and that none of the participants can control. For example, in the coin-flipping game as we described it, the risk of heads or tails is objective. On the other hand, we shall have many examples below in the mortgage market where risk is explicitly not objective.

Now let us consider a market where the organizations in the market are risk-neutral and in which the risks are objective. We want to ask whether this market would operate efficiently by itself, or whether it would tend to break down and perhaps require government intervention. The answer, developed in economic theory, is that insurance markets dealing with objective risk and in which the insurance companies are risk-neutral will operate as well as any other markets; that is, the risk factors themselves will not tend to disrupt the markets. Furthermore, the theory indicates that the purchasers of the insurance (the consumers) will pay a price for insurance that approximates the true actuarial odds (including the costs of administration in the odds). The implication, of course, is that risk itself would not provide a context for government intervention in the market. (This is not to deny that there may be many other grounds for government intervention even in this form of insurance market—monopoly power being one case).

Moreover, markets that in reality can be identified as approximating risk-neutrality with objective risk do appear generally to function quite well. Life insurance is one example. Markets for fire insurance, theft insurance, automobile liability insurance, etc., are all examples of private markets undertaking insurance roles. Each of these examples, of course, is also a case in which there are problems—and our point is not to deny these problems. Rather, it is to stress there are conditions under which private insurance markets could operate; and that these conditions are essentially risk-neutrality and objective risk.

II.2.b When Markets Do Fail to Operate Effectively: We now turn to the other side—and indeed more relevant side—of the coin; namely, the conditions under which risk markets will fail. As a starting point, we can look to our two conditions—risk-neutrality and objective risk.

Risk-Aversion as Grounds for Market Failure: Using the insurance example, let us consider a case in which the insurance company is risk-averse in its attitude toward risk. This would mean that it would not be willing to sell actuarial fair insurance. Instead, if it were to sell insurance at all, it would require some risk premium, or payment above the actuarial odds, in order to induce it to sell the insurance. From the standpoint of the consumers, of course, this means they are being offered actuarial unfair insurance. Now, would the consumers buy such insurance? If the consumers are risk-neutral then they will not buy actuarial unfair insurance and thus no insurance market would exist; everyone would self-insure. On the other hand, if consumers are sufficiently risk-averse themselves—and indeed it is required that they be more risk-averse than the insurance companies—then they would continue to buy insurance, even knowing it was not fair. The simple principle involved is that the consumers would be willing to pay a risk premium in order to avoid the risk, and if the premium they are willing to pay is at least as great as the premium required by the insurance companies, then the market could continue to function. But it is equally clear that the amount of insurance issued in such markets would be less than the amount that would have been issued if the insurance companies were truly risk-neutral; and consumers would be paying more for the insurance that they do buy. Thus, in summary, risk-aversion limits the activity in risk markets and introduces the possibility of risk premium, but it does not generally eliminate the markets.

Absence of Objective Risk as Grounds for Market Failure: The problems that arise when risk is not objective are well known to participants in insurance markets. First, two main categories should be noted: "moral hazard" and "adverse selection." Moral hazard is said to occur when the granting of an insurance policy removes the incentives of the insured to avoid the calamity. Examples can include automobile drivers who become more careless when insured, homeowners who do not take precautions against fire when insured, and, in the extreme, individuals who commit suicide on account of life insurance. Moral hazard is a case where the risk is not objective because the individuals can control the odds of the calamity and in fact the act of insuring may indeed create incentives to worsen the odds.

Adverse selection arises when information on the true odds is not equally well known to all participants in the market. For example, it might generally be the case in life insurance markets that individuals have information on the state of their health which is not available (or is available only at a cost) to the insuring company. The insurance company then really has three options, and it will generally pursue all of them: (1) It can attempt to buy the information—for example, by requiring and paying for a doctor's examination of the individual; (2) it can attempt to use various "screening" devices that tend to correlate with the desired information, but are less costly to obtain—for example, the age of an insurance applicant would be obviously a very useful screen; (3) the company can simply set its rates so that it covers the average of all candidates for insurance, with the results that some applicants pay too much relative to their actuarial odds, whereas others pay too little. The important point is that, to the extent average pricing is used, there will be incentive for the less risky individuals not to insure—and for the above average risks to "overinsure." The process through which the higher risk consumers tend to buy the insurance is called adverse selection.

The meaning of "market failure" in the cases of moral hazard or adverse selection must be treated carefully. It is really neither the issuing company nor the consumer who is at fault—both of these groups can be assumed to be following normal profit maximizing or utility maximizing behavior under the conditions of competition. Rather, it is truly the market that fails, and the market failure is in turn due to the specific features of the commodity "risk." Furthermore, the specific form of the market failure is difficult to predict in general. As some examples, the market failure can take the following forms: (i) "unreasonable" prices may be charged some consumers; (ii) limits may be placed on the amount of insurance available; (iii) various screening devices, not directly related to the risk, may be used to discriminate between consumers; and (iv) the market may simply cease to exist in general or, for some consumers, in the sense that no firm will agree to sell the insurance.

Other Grounds for Market Failure: In anticipating the specific problems of mortgage markets, at least two other grounds for market failure deserve special attention. The first concerns noneconomic motivation in supply. For example, a case of racial prejudice in which some group could not obtain loans would be so classified. The second concerns the effects of externalities and concern for "spoiling the market." For example, a lender might be refused to make a specific loan on the grounds that the loan would tend to hurt a "neighborhood" and thus increase the total risk of all the mortgage loans made by the companies. Both the cases of noneconomic motivation and externality are best discussed directly in the context of the institutional structure of the mortgage market, and this will be done below. They are introduced here, however, to stress that they are different from either the problems of risk-aversion or objective-risk.

II.2.c Summary and An Introduction to the Mortgage Market: The main point of this section has been to outline the significant factors relating to risk that can cause markets to fail. These factors are:

- Risk Aversion on the part of lending and insurance companies.
- Adverse Selection, in which the worst risks of any population opt to buy insurance or take out loans.
- Moral Hazard, in which the availability of insurance or a loan affects the behavior of the borrower or insured in an undesirable fashion.
- Externalities, in which granting a specific loan can affect the value of other loans already granted.
- Prejudice and other noneconomic motives that can influence supply in the market.
- Usury Ceilings, in which legal limits are set on the rate that the lender can charge (or the borrower can pay), thus eliminating certain classes of transactions from the market.

The result of each of these factors is that the market will cease to operate in the normal fashion of economic theory, and that the standard properties of optimality associated with perfect markets will not be valid. Instead, a variety of nonmarket mechanisms may arise. For present purposes, two such mechanisms should be stressed. First, quantity rationing, in which lenders limit the amount of the loan that they will make, regardless of the interest rate they are offered, may arise. The extreme of quantity rationing, of course, is the case in which a borrower cannot obtain any loan at all. Second, devices for screening loan applicants are likely to become important in the operation of the market. Screening devices will have the property that they correlate with the various risks that the lender wishes to avoid. The problem with screening devices is that they are valid only for aggregate populations, and will not predict perfectly on an individual basis. This has the implication that specific borrowers will feel "discriminated" against, should a screen be used under which they obtain a poor rating.

We now wish to translate the theoretical material of this section into the specific operation of mortgage markets. The basic issue, of course, is the nature of risks in mortgage lending. We define a mortgage contract as a loan with an effective maturity on the order of 10 years, which uses a house as the prime collaterial. The key features of the contract are the interest rate charged on the loan, and the ratio of the loan to the full value of the house. Needless to say, there are many other contractual features of a mortgage loan, including the maturity as one important item. But for present purposes, the interest rate and the loan-to-value ratio are the critical variables.

II.3 Risk Factors in Mortgage and Housing Markets

II.3.a Introduction: In making a mortgage loan, lending institutions perceive two major risks. The first is the risk of default, and the second is the risk that in case of default the value of the mortgaged property will not sufficiently cover the institution's investment in it. Thus, ". . . the borrower is the first line of defense against possible default or foreclosure, while the property as security represents the second line of defense against loss in the event of foreclosure." (Helms (1973), p. 55) And in the words of the American Savings and Loan Institute (1971), "The *basis* of a sound mortgage lending policy is the reasonable probability that the borrower will be able and willing to protect his ownership of the mortgaged property. As long as the borrower meets his monthly payments, no loss can come to the lender." (p. 72, emphasis added.)

Given these concerns, we can expect that the availability of mortgage credit, and the terms at which such credit is available, will vary both with the characteristics of the borrower and with the characteristics of the property on which the loan is to be made. The following discussion will deal both with the way in which lending institutions perceive the riskiness of individual borrowers, and with their perceptions of the effect of the location of properties on the value of such properties as security for a loan. The emphasis will be on the behavior of savings and loan associations (S&L's) and mutual savings banks (MSB's), as these are the institutions which grant most of the higher risk mortgages. Both life insurance companies and commercial banks tend to purchase safer mortgages (including FHA and VA), the former due to a lack of knowledge of local conditions, and the latter due to a relatively volatile liability structure (see Dhrymes and Taubman (1969), p. 118). These patterns of behavior are reflected in the fact that the effective yields of both S&L- and MSB-granted mortgages are generally higher than those of life insurance companies and commercial banks (Fredrikson, (1971)).

Since the characteristics of borrowers desiring business loans (for commercial properties) can be relatively easily determined by a lending institution, which will have available to it a great deal of information about the credit of a firm or businessman, the discussion below will focus on the bank's behavior with regard to a borrower desiring to occupy and own his own home. The discussion of the riskiness of particular locations, however, will deal both with owner-occupied housing and rental housing, as many of the locations which have in fact been "red-lined" are in rental neighbhorhoods.

II.3.b Riskiness and Borrower Characteristics: Both savings and loan associations and mutual savings banks place strong emphasis on the importance of lending to a credit worthy borrower. The characteristics of borrowers which are considered to be important by lending institutions will be discussed and evaluated in light of the potential causes for market failure outlined in section II.2.

Credit Analysis: The major concern of credit analysis, of course, is that the creditor will have adequate income throughout the life of the loan, and a good attitude toward his debts. The American Savings and Loan Institute lists the following characteristics as being important to the credit worthiness of a borrower ((1971), pp. 79–81):

1. Age of Applicant: The prime working years are considered good. If the applicant is either just into the labor force or of retirement age, this is considered poor.

2. Number of Dependents Other than Spouse: The fewer, the better. More than four children is considered to be poor.

3. Life Insurance: An index both of the attitude of the borrower and of lender protection in case of default. More than the amount of the mortgage is considered good, less than half the mortgage is poor.

4. Number of Jobs Held: A borrower who holds more than one job is considered to be a poor risk.

5. Occupation: Self-employed workers, unskilled, and commission salesmen are seen as poor risks. White collar and skilled, average. Professional and government employees are good risks.

6. Employment Record: Stability is valued. Less than 2 years on the job is considered poor, more than 7 years, good. It is noted that the mobility of certain types of occupations may change these ratings.

7. Credit References: Small loan and auto finance companies are poor references; retail trade, average. Banks and mortgage companies are considered to be good references.

8. Carrying-Charge Ratio: If the ratio of the family's net annual income to the monthly mortgage payment is less than 50, it is poor. If it is more than 75, this indicates a good risk.

9. Loan Length: Over 25 years, poor; less than 15 years, good.

10. Junior Financing Ratio: If a second mortgage of 15 percent or more is held, this is poor.

11. Age of Property: The newer the better. Over 50 years is considered to be poor.

12. Equity in Property: The more the better. Less than 15 percent is considered to be poor.

There are three main points to be stressed with respect to such rating systems. First, the focus of the discussion emphasizes that the decision to be made is whether or not to grant the loan, not to pick the terms which will satisfy objective risk considerations. In introducing the discussion, the manual states:

> A rating system for evaluating loan applicants is helpful in a number of ways. It enables clerks and other office workers to make competent preliminary decisions on loan applications. It quickly weeds out many applicants who do not measure up to association standards, saving the association and the applicant time and money. Most important, it actually reduces the number of poor loans accepted and thereby reduces collection costs ((1971), p. 78).

At the end of the discussion the reader is admonished to "keep in mind that loan risk does not necessarily involve loans to borrowers with a poor credit rating. Higher loan-to-value ratios, older properties, and longer loan terms will increase risk" ((1971), p. 82).

Second, the discussion emphasizes that a good credit analysis will also include personal references and information, such as the stability of the applicant's marriage, and detailed information on the way in which the applicant has managed his financial affairs in the past ((1971), p. 73).

The concerns of MSB's in making mortgage loans are similar to those of S&L's. Again, the emphasis is on limitation of "probabilities of collection difficulties and foreclosures" (Held (1973), p. 57), rather than on finding an interest rate commensurate with objective risk. And again, the importance of good personal information, as well as a good objective credit evaluation, is stressed.

Third, and perhaps most importantly, it can be seen that the factors used in the credit rating systems will give low rankings both to borrowers that are poor (low income) and to members of minority groups (primarily blacks). With respect to poor borrowers, it can be seen directly from the list that they will rank low because most of the factors are income or income related. With respect to the minority groups, they will rank low both because they tend to be poor, and because they tend to be evaluated especially low on such rating systems (for reasons to be developed in a moment). This conjunction of poor borrowers and minority group borrowers creates important problems in analyzing the effects of risk in mortgage markets. In particular, while the causes for discrimination against the two groups may appear quite similar, the remedies may well be quite different. For this reason, it is stressed that care should be taken in the following section in distinguishing between those factors that relate to poor borrowers in general and those that relate directly to minority group borrowers.

II.3.c Borrower Characteristics and Market Failure: In section II.2, it was argued that charges for objective risk were a "reasonable cost" of mortgages. In practice, however, the borrower characteristics which are of concern to lending institutions, and the way in which they are used, may result in mortgage credit simply being unavailable to certain borrowers. (The market response to the unavailability of mortgage credit is discussed in II.3.e, below.) There are a number of causes of this lack of availability of mortgage credit to certain borrowers. Although listed separately in the discussion below, they can, and in fact do, interact.

Overall Conditions in Mortgage Markets: One cause of lack of mortgage credit to borrowers who have relatively high objective risk is the general condition of the mortgage market. Thus, "When the demand for loan funds is high, associations seldom raise interest rates to justify making higher-risk loans. There are two reasons: First, at such a time there is no shortage of low-risk lending opportunities; second, demand has usually pushed even low-risk rates to regulatory ceilings." (ASLI (1971), p. 82). Part III of this paper discusses the behavior of the mortgage market in a national context. However, it should be noted here that an environment of "loose money" can be expected to contribute to the willingness of lending institutions to grant mortgages to borrowers with relatively high objective risk. Furthermore, interest rate ceilings make the granting of such mortgages extremely unlikely.

Bias in Credit Criteria: Another potential cause of a lack of mortgage credit, particularly to minority group borrowers, is that the list of characteristics of "objective" creditworthiness given above will tend to make a white borrower appear to be a better risk than a minority group borrower, even if their family incomes are the same. (The fact that homeownership is less likely for blacks than whites, at all incomes, has been well documented. See for example, Kain and Quigley, (1970)). Among the ways in which this can happen are the following:

1. Banks often discount the incomes of working wives of child bearing age, due to the objective probability that they will have children and withdraw from the labor force (ASLI (1971), p. 76, Held (1973), pp. 57–58). But it is well known, for example, that labor force participation rates are much higher for black married women than for white (Rees (1973), p. 9). Thus, the income of the wife in a black household should be discounted less heavily than that of the wife in a white household.

2. The concern with moonlighting and part-time income will make it more difficult for any borrower whose wages are relatively low, regardless of his motivation to succeed, to obtain mortgage financing. An argument parallel to that presented just above will apply as well with reference to the mortgage granting institution's concern with occupational status.

3. The fact that lending institutions consider credit references from small loan and auto finance companies to be unsatisfactory will reflect badly on the credit ratings of many poor families who may have been unable to obtain financing for durables bought in the past.

4. If it is indeed true that minority groups are restricted as to the locations in which they can buy housing, they are much more likely to seek loans on housing that is more than 50 years old than are whites—as housing in most Northern central cities is of at least that age.

In all of these cases, economic discrimination against the poor and minority groups in other markets (housing and labor, for example) would appear to cause the objective risks of default on a loan to be higher. Following the argument presented in section II.2, it would seem to be quite reasonable that lending institutions respond to this higher objective risk by lending only at higher rates of interest, or, within the institutional context in which they operate, not lending at all.

Adverse Selection: However, also following the argument presented in section II.2, it seems quite probable that one cause of market failure in the market for mortgages to the poor is due to asymmetries in information, and the fear, on the part of banks, of adverse selection. The creditworthiness criteria listed here depend crucially on the quality of the information available to the lending institutions. As long as there is economic discrimination practiced in the markets from which the lending institutions obtain their information, the poor, on average, will not have available to them credit references, both objective and personal, of the same quality as the middle class. Phrased differently, it will be both more difficult and more expensive—perhaps practically impossible—for a lending institution to acquire what it considers to be reliable information on the creditworthiness of many poor borrowers. The market response to this situation, as was shown in section II.2, may be market failure. The poor will be uninsurable against risk, at terms that they perceive to be reasonable, because the insuring institutions (lending institutions) are unable to predict reliably the objective risk to their own satisfaction. Policy implications of this phenomenon will be discussed in section II.4.

Risk Aversion: The factors of risk discussed so far may also disrupt the mortgage simply on the basis of risk aversion on the part of the lender. In the case of risk aversion, we can assume that the lender has been able to quantify all the relevant costs of the loan, and has found an implicit mortgage rate at which he can profitably make the loan on an actuarial basis. However, the loan will then remain risky in the sense that the lender cannot be certain of the actuarial outcome. A simple and direct procedure for the lender to follow is to charge an additional premium to compensate for the bearing of risk. Several complications make this simple solution more difficult, however. First, usury ceilings may make it impossible for the lender to charge the rate necessary for risk compensation. Second, borrowers may balk at a high interest rate, using moral protests as the basis of their complaint. Third, the considerations of moral hazard and adverse selection as just discussed may be present along with simple risk aversion. The effect of each of these complications is that the lender may not achieve his compensation for bearing risk in the form of a higher interest rate. Instead, he will attempt to minimize the size of the loan, or not grant any loan at all, for the cases of high innate risk.

Other Causes and Some Evidence of Market Failure: That lending institutions have, in the past, been apparently discriminatory in their granting of mortgages to blacks has been well documented (McEntire, (1969)). Thus, if we observe that homeownership rates among blacks and whites are different at the same incomes (Kain and Quigley, (1970)), we should not rule out the possibility of simple racial prejudice on the part of the institutions.

A more complex cause of such apparent prejudice which seems equally plausible is that lending institutions that deal primarily with white depositors fear that if they deal with blacks they will build up ill will in the market upon which they rely for their livelihood. A variant of this argument will be presented in some detail in section II.3.d.

Another potential cause of the problem is that race is used as a screening device in the sense discussed in section II.2. Or it may be that screens which work quite well in the evaluation of whites as credit risks do not work well in evaluating blacks.

Evidence on the cause of mortgages being granted less freely to blacks than to whites would be impossible to obtain without direct access to loan negotiations. However, the theory presented in section II.2, and the practices used by banks as enumerated above, make it appear likely that even if lending institutions are unprejudiced themselves and do not respond to the prejudice of their white customers, the availability and terms of mortgage credit will be inferior for blacks relative to whites.

II.3.d Riskiness and Neighborhood Characteristics: Housing as Collateral: Housing is a unique good, largely due to the interaction between its long life and the fact that any unit of housing (save for mobile homes) is tied to a given geographical location. In making housing investments, therefore, as well as in financing them, investors will be properly concerned with the possibility that changes in the characteristics of the neighborhood in which the investment is made will cause changes in the value of the asset. Put another way, the characteristics of the neighborhood are an important determinant of the value of the asset, because the asset is not mobile.

Neighborhood Characteristics and Real Estate Appraisal: Given the characteristics of housing as an asset, it is not surprising that S&L's and MSB's stress the importance of both the quality and stability of neighborhoods in making real estate appraisals. The American Savings and Loan Institute writes: "The location of a property certainly has a strong effect on its value; some experts even go so far as to say that a neighborhood determines value." ((1971), p. 93) And H. Held of the National Association of Mutual Savings Banks, stresses that "Familiarity with past, present, and probable future neighborhood conditions and with the circumstances surrounding them is an absolute essential to good appraising." ((1973), p. 65) The American Savings and Loan Institute lists a number of neighborhood characteristics which are important in determining value ((1971), pp. 93–100):

1. Proximity to desirable or undesirable other uses of land is an important neighborhood characteristic in determining value.

2. Governmental influences, such as zoning and assessment ratios, are also considered to be important.

3. Both the quality and the homogeneity of the population which currently resides in the neighborhood, as well as its stability, are considered to be very important. Thus:

Homes occupied by owners in lower income brackets are apt to be poorly maintained unless the owners have a sizeable equity in the home. Neighborhoods in transition from primarily owner-occupied to renter-occupied housing also may show evidence of poor or deteriorating maintenance. These differing attitudes affect value in a neighborhood. Those which attract the junior executive group tend to show a rapid population turnover, since most of the breadwinners either move upward into more expensive homes as their careers succeed or move geographically in order to obtain a better job opportunity. The turnover rate gives many chances for disruptive influences to enter the community and push values downward. (p. 96)

4. The concern with stability expressed in the above quotation is emphasized again under the heading, "Effects of Change." Here it is argued that "any change in a neighborhood can have a radical effect on property values. . . . It is not important whether the change is an asset or a liability when considered objectively; what is important is the attitude of property owners toward the potential or actual set of new conditions." (p. 96) Indeed, it is argued that the change need not even take place. Among other things, it is stated "that there are certain urban areas which are so precariously balanced that panic arises when gossip merely hints that a resident is going . . . to sell to members of a minority group. If 'For Sale' signs sprout all over the neighborhood as a result of a rumor, property values drop . . . whether or not the sale is made." (p. 96)

One interesting feature about the lending institution's concern about the effect of future neighborhood characteristics on future property values is that it is unsymmetrical. If the neighborhood should appreciate in quality, the lending institution does not gain—it merely gets its loan back. If the neighborhood should change in such a way that a mortgage property should fall in value, however, there is a real possibility that the owner of the property may have negative equity, and that the loan will become insecure. Viewed in this light, it is not surprising that lending institutions are so greatly concerned with neighborhood stability.

The Simple Economics of "Red-Lining:" The "red-lining" of neighborhoods by institutional lenders is a clear example of market failure. Furthermore, there is persuasive evidence that this procedure, which means that institutional mortgages are simply unavailable at any price in certain geographic locations, is a pervasive one.

George Sternlieb, in a number of studies, has documented the existence of red-lining in the cities of Newark and New York (Sternlieb, (1966) (1971)). Michael Stegman (1973) has documented pervasive red-lining in the central city of Baltimore. The National Committee Against Discrimination in Housing (1972) finds red-lining in Oakland, California. Hearings before the Senate Committee on the Judiciary strongly indicate red-lining in Boston (1971). Hearings before a House Subcommittee (1969) strongly indicate the presence of a form of red-lining in the Nation's Capital.

The cause of red-lining, however, like the causes of mortgages being less available to blacks than whites, need not be due to direct racial discrimination on the part of lending institutions. Rather, both theory and evidence indicate that the major cause of red-lining is the fact that the objective risk of lending in certain areas is either unmeasurable or so high that usury ceilings make it impossible for lending institutions to be compensated for it.

In *The Urban Housing Dilemma,* Sternlieb cites a number of interviews with lending institutions made in an effort to find out their reasons for being unwilling to lend on particular parcels. Time and time again, he finds that the neighborhood, or uncertainty about the future of the neighborhood, is the cause. Indeed, neighborhood characteristics were given as a reason for negative response to the question "Is the building good collateral?" in 18.4 percent of those surveyed. No other single cause was more important, though all of the survey buildings were rent-controlled. One case is cited in which a building was considered as good collateral, and had an excellent repayment history, but "the appraiser for the bank indicated that he would not extend the mortgage 'because of the area which surrounds this parcel. It has been good and stable to date, but it is questionable in the future.' " ((1970), p. 625)

It is fair to conclude from Sternlieb's interviews and surveys both that red-lining is pervasive in New York, and that the major cause of red-lining within the city is the concern of institutional lenders that they will be unable to get their money out—that the volatility of neighborhood characteristics and their effect on property values make buildings in many areas unsuitable as collateral for loans of any term. The implication of such behavior for housing investment within these neighborhoods is, of course, disastrous. Furthermore, it seems likely that some neighborhoods decline because they are red-lined, rather than being red-lined because they are declining.

In the context of the theoretical discussion presented in section II.2, there are a number of potential causes of red-lining. First, it may be that the objective risks associated with a given parcel of land are so high that no legal interest rate can compensate the lender for these risks. Second, even if very high rates of interest were legal, banks might have other reasons—such as public relations, and the complexities of granting mortgages at many different rates of interest—for not wanting to make loans in such neighborhoods.

More important, however, is the fact that in a dynamic urban housing market, composed of many neighborhoods, the cost of obtaining the information necessary to determine the objective risk may be extremely high. Indeed, it may be impossible reliably to estimate objective risk at any cost.

In any neighborhood where the estimate of objective risk is considered to be unreliable by the lending institution, the institution either will not make loans, due to the possibility of adverse selection, or will demand that it be compensated for the possibility of adverse selection by setting the cost of mortgage credit so as to reflect the possibility that its estimate of objective risk is too low. Even in this case, as described in section II.2, there is the possibility that adverse selection will cause the market to fall completely.

Thus, red-lining may be a perfectly rational response to lack of information in the market. To the extent that usury ceilings are operative, and to the extent that lending institutions are unwilling, for other reasons, to lend at greatly different rates to different mortgage customers, red-lining will be all the more likely. But even in the absence of these institutional constraints, the possiblility of adverse selection, due to the inability of institutions to make reliable estimates of objective risk, may cause the market for mortgages in volatile or declining neighborhoods to fail completely. The responses of the noninstitutional market will be discussed later in this section. The policy implications of red-lining are discussed in section II.4.

Market Spoiling and "Greenlining:" While it is well documented that blacks have a lower probability of homeownership than do whites, it is also the case that many blacks do get mortgage finance, and do own their own homes. It is also widely held, however, that mortgage finance is unavailable for blacks who wish to locate in heretofore all-white neighborhoods.

For example, in a study done jointly by the National Academies of Sciences and Engineering, it was found that "Mortgage lending institutions have had separate lending policies for blacks and whites. They have been timid in developing policies for realizing mixed residential areas." ((1970), p. 27) The NCDH study cited earlier in this report confirms this observation, for Oakland.

Rose Helper, in a study of real estate practices in Chicago, found that all of the real estate brokers interviewed agreed that lending institutions would not grant credit to a black family that wished to purchase a house in an all-white neighborhood ((1969), p. 71). Older studies, notably McEntire (1960), also have found that mortgage money is generally unavailable for blacks in white neighborhoods.

The expressed and documented concern of lending institutions with neighborhood stability provides a plausible explanation of this phenomenon. MSB's and S&L's rely heavily on their knowledge of local market conditions in granting residential mortgages (ASLI (1971), p. 67; Held (1973), pp. 38, 41, 87; Jacobs (1966), p. 113). Indeed, much of their competitive ability in originating mortgages will depend on their expertise in the areas in which they lend. Once a lending institution "knows" a certain neighborhood, future loans made in that neighborhood will be relatively inexpensive to research—reliable information already will be at hand. Thus, in any given neighborhood, it is likely that a potential lending institution already will have made loans. If it has not, some other lending institution will be prepared to loan in that neighborhood (provided it has not been red-lined) at lower cost.

In granting a mortgage to a black family to live in an all-white neighborhood in which it has already granted a number of loans, a lending institution will be running the risk that the change in neighborhood characteristics caused by its action will cause a change in the value of all the properties in the neighborhood. The lending institution would itself be introducing instability into a neighborhood in which it operates—even though stability is one of its major concerns in granting loans in the first place. Such a practice, therefore, is highly unlikely. In addition, an institution might be concerned that white depositors would resent its having aided black entry into their neighborhood. This would further inhibit the institution's willingness to grant loans for this purpose.

An interesting feature of the lending institution's concern with neighborhood stability is that there is considerable evidence that the movement of blacks into white areas does not, in the long run, depress property values. (See, for example, Laurenti (1960); Guttentag (1970)). However, if housing values do not fall in the long run, an attempted exodus of white residents, all trying to sell at once, could leave the institution in a position in which it was forced to assume ownership of a number of properties—a practice which lending institutions would rather avoid.

It also should be noted that to the extent that lending institutions are inhibited from making loans to blacks in all-white neighborhoods due to the risk that the neighborhood change will induce a fall in property values, the risk is not an insurable one, due to the problem of moral hazard.

Finally, note that market spoiling in mortgage markets need not lead to credit being unavailable to blacks or to credit only being available at unreasonable terms. Rather, it will only lead to such phenomena in neighborhoods that are all white. If there are enough locations in a city that are all black, or which are known to be stably integrated, the banks may "greenline" these areas as being appropriate for loans for black families. There is evidence that this has happened in Boston, Oakland, and Chicago, (U.S. Senate (1971); NCDH (1972), op. cit.; Helper, (1969), p. 171). The practice may be quite pervasive (NAS, NAE (1970), p. 27). Greenlined locations would, of course, have to meet the institution's normal criteria for neighborhood quality and stability, and the black borrowers would have to meet the normal credit criteria. Greenlining is a phenomenon which gives evidence of a situation in which mortgage credit is unavailable, or available only at unreasonable costs to some borrowers at some locations. The same borrowers may have no difficulty at other locations. The appropriate policy response would seem to be legal in focus, rather than economic.

II.3.e Market Responses to the Unavailability of Mortgage Credit: We have seen above that institutional lenders respond to what they perceive to be high risk situations by simply refusing to write mortgages on any terms. Where there is measurable objective risk, such behavior can only be explained by usury ceilings or by an unwillingness of respectable institutions to become involved in what they perceive as speculative ventures. Where the objective risk is not feasibly measurable by the institution, it has been argued that the problem of adverse selection may be at the root of the problem. In either event, we are left with the question of what happens to borrowers who, by virtue of their own credit characteristics or the characteristics of the neighborhoods in which they seek to invest, do not have institutional mortgage credit available to them.

Unfortunately, little firm evidence on this question is available, although there is a good deal of fragmentary and anecdotal evidence to indicate that credit is available, from noninstitutional sources, at very high cost. Perhaps the most common instrument that is used to permit borrowers to obtain credit on housing in changing neighborhoods, and to permit poor borrowers who cannot obtain credit from institutional lenders, is some form of installment contract, in which the lender retains title to the property throughout the length of the contract.

Typically, these contracts demand very small downpayments (a few hundred dollars) and specify that if the monthly payments are kept up for the term of the contract, title will be given to the borrower. The high interest rates associated with these contracts are easily hidden, as there is no need for a price of the property in current dollars ever to be quoted. (Stegman (1970), pp. 199–212).

The use of such instruments in Baltimore has been well documented by Stegman (1972). Their use in Chicago has also been well documented (Helper (1969), pp. 168–71). In Washington, D.C., hearings before a House Subcommittee strongly indicate that the practice has been widespread there as well, although in a somewhat different form. The basic mechanism, however, is that the value of the property is overstated, and that the seller of the property also sells financing—the high price of which is hidden in the overstated price of the property. Sternlieb has documented a number of such situations in both New York and Newark for rental properties in the inner city (1966), (1970).

Unfortunately, noninstitutional mortgage finance is a subject which has received little academic study, largely due, no doubt, to the fact that there is little in the way of data suitable for studying the problem. It would seem that credit is available to some persons and properties that cannot obtain institutional mortgage credit. The cost of such credit appears to be very high, however. Whether or not this is reasonable is discussed below.

II.3.f. Reasonable Cost: Perhaps the most common interpretation of the term is that there be a supply of funds to the national and regional mortgage markets such that the annual rate of housing starts grows smoothly in line with household formation and population increase. In other words, the focus is not so much on the cost of mortgage credit as upon its availability. If mortgage credit is generally available, then the housing market will be stable, the construction industry will be efficient, and financial markets will be easily able to cope with the finance of both new construction and the sale of old units.

In a *Study of Mortgage Credit* (1967), all those interested groups and specialists submitting papers were concerned with the supply of funds, rather than the price, except for four. The four groups which also discussed their opinions on the appropriate cost of credit were:

1. The VA, which simply pointed out that with higher interest rates, equity builds up slower, increasing the possibility of difficulty in case of default (p. 133).

2. The Home Manufacturers' Association, which was quite concerned with the effect of high interest rates on consumer demand for housing: ". . . high rates with short terms make your housing an unattractive value for the consumer." (p. 105) However, no suggestion was made of the right rate.

3. The National Association of Real Estate Boards, which, like the two previously mentioned groups, was primarily concerned with a stable market for mortgage funds, also noted that mortgage terms affect the demand for housing (p. 303).

4. The National Farmers' Union actually uses the phrase "reasonable level," p. 311, and argues that 3 percent would be a good rate when there has been a natural disaster, and that, in general, farm rates must be lower than their current levels. Indeed, in surveying other sources of the opinions of special interest groups (U.S. Senate Hearings (1969); U.S. House Hearings (1969, 1968)), one finds almost all of the groups and Congressmen using the words "reasonable costs" are associated with agricultural interests. The one possible exception is the AFL-CIO, (House (1969)). While the AFL-CIO favors interest rate ceilings, it says that it does so not for considerations of reasonable cost but because it argues that empirically every time ceilings have been raised, housing starts have fallen (p. 487).

Thus, in general, it is fair to say that "reasonable cost" is not a well-defined notion, and that the vast majority of interest groups associated with housing and mortgage markets are primarily concerned with a stable supply of funds to those markets, such that they are shielded from the lack of availability due to the business cycle, not from paying the cost of capital. Many issues related to stability of these markets will be discussed in Part III of this paper.

In the context of the concerns of this part —variations in mortgage costs by borrower and location at a given time and in a given area, the phrase "reasonable cost" is rarely used as stressed above. However, it is implicit in the comments of many interest groups, particularly those concerned with equal housing opportunity, that it is unreasonable that some borrowers of equal incomes borrow on different terms, and that housing of equal value in different locations receives loans on different terms (Denton (1967), p. 59; NCDH, op. cit., p. 1). Consequently, to conclude this section, it is useful to comment on the economic relationship between factors of risk and "reasonable price" for mortgage credit.

The starting point, and one on which there can be general agreement, is that factors of objective and verified risk are reasonable components of the cost of mortgage credit. In this case the borrower will be charged the actuarial value (plus administrative costs) of the risk, and standard principles of economic efficiency will be valid.

A more difficult case arises when the risk remains objective, but the lender is risk-averse and charges a premium above the actuarial value for bearing the risk. In this case, the interpretation of the term "reasonable" becomes one of definition.

The most difficult cases, however, occur when the mortgage market literally fails, due to considerations of adverse selection, moral hazard, etc. Under these circumstances no mortgage credit may be available, and the issue is whether this is "reasonable". The opinion of most special interest groups is that such market failure is distinctly not reasonable. It should be stressed, however, that matters of definition of this sort are generally not usefully discussed at length. Rather, the critical question is whether government can intervene in such a way as to improve the situation, and this is the matter to which we now turn.

II.4 Risk Factors and Government Intervention: Conclusions

II.4.a Some Principles for Government Intervention: This brings us then to the ultimate issues of this part, the grounds for government intervention in a risk market. We should note immediately that we are discussing government intervention in mortgage and housing markets here only as it relates to the risk characteristics of the mortgage contract itself. There are, of course, many other grounds on which arguments for the subsidization of housing and even mortgages themselves can be based, but they are not of immediate concern.

The price of risk, as we have developed the analysis so far, can be divided into essentially four categories: the costs of the objective risk, the premia that cover risk aversion, nonobjective risk (moral hazard and adverse selection), and noneconomic motives. The economic considerations that apply to government subsidization of each of these components are quite different, and it is worthwhile to consider them separately.

The Subsidization of Objective Risk: The spirit of the argument, so far, has been that elements of objective risk—for example, fire in a house—should be and can be treated much as any other cost. Thus, it follows that the questions of the subsidization of objective risk can be placed in the framework of more traditional subsidy analysis. For example, with respect to housing, the government could provide low-cost (subsidized) fire insurance as one means to stimulate investment in housing. The point, however, is that in the case of objective risk the private markets will function well, and thus there are no social grounds, or foundations of social externalities, except for the outright subsidization of housing, to warrant government intervention in this area. On the other hand, there is the possibility that even seemingly objective insurance problems, such as fire insurance, may have elements of risk that are not objective (see, for example, Syron (1973) for a discussion of fire insurance in ghetto areas).

The Subsidization of Risk Premia Due to Risk Aversion: Now consider a case where the company charges a premium for its handling of risk, with the result that the price exceeds the true actuarial odds. The government can intervene in this situation in one of two ways. First, it could undertake the insurance function itself, thereby eliminating the risk for the private markets; or it can attempt to induce the private market to eliminate the risk premium through government subsidies. The interesting difference between these two methods is that the government insurance route is in principle costless, whereas the government subsidy route involves an explicit cost. This creates an obvious presumption in favor of the government's operating the insurance funds itself.

The Subsidization of Risk Premia Due to Nonobjective Risk: The case of nonobjective risk is the most difficult one for public policy. The difficulty in this case is that while certain individuals are paying a price for risk that is unreasonably high relative to their true risk, the private market finds it too expensive to isolate these individuals for special consideration. This leaves basically two alternative routes for government subsidy. One possibility is an across-the-board industry subsidy, in which all consumers—both relatively risky and relatively risk-free—receive the benefits of the subsidy. The adverse feature of this approach, of course, is that subsidies will then be provided to some individuals—the truly risky ones—who do not warrant it. On the other hand, such programs may be easy to manage. The alternative approach is for the government to subsidize the costs of obtaining information relating to the riskiness of individuals. In this case the problem is confronted directly, the information is obtained, and then efficient pricing is used. The difficulty with this approach is the possibility that it may be very costly, and there is, of course, the possibility that the information is not available at all.

Subsidization When Noneconomic Motives are Involved: The case of noneconomic motives, for example of racial discrimination, is perhaps the easiest to deal with in principle. It is fair to assume that U.S. law, both in terms of Restraint of Trade law and Civil Discrimination law, provides an ample basis for prohibiting discriminatory and noneconomic motives in mortgage and homebuilding activities. One could argue that economic subsidies should be provided to counter the discrimination, but in terms of both costs and moral issues, cases of simple discrimination should be confronted and eliminated directly.

II.4.b Specific Proposals for Government Intervention: Following is a discussion of some of the major proposals in this area.

The Elimination of Usury Ceilings on Mortgage Contracts: It is difficult to obtain data on the extent to which usury ceilings have actually been effective in restraining the level of mortgage interest rates. This is not surprising, because when usury ceilings are effective, loans are not made, and thus data exist only in the form of loan applications. In addition, at least in some cases, State usury ceilings have been regularly raised whenever they did become effective. Whatever the situation, however, it is critical that the adverse effects of usury ceilings be recognized. The problem is that risky borrowers will generally be required to pay higher interest rates than the average borrower. But if usury ceilings make it impossible for the lender to charge the borrower an appropriate rate, then the lender's response will be to limit the size of the loan, and perhaps make no loan at all. Furthermore, the advantages of usury ceilings—protecting borrowers from "unreasonable" loan rates—are illusory: in organized loan markets, "unreasonable" rates are simply never observed; in unorganized markets (black markets) the ceilings are not respected in any case. The elimination of any legal limits on the level of mortgage interest rates is thus strongly endorsed.

The Provision of Government Insurance on Mortgage Contracts: Government insurance on mortgage contracts may be introduced for at least three reasons. First, insured mortgages are better instruments for secondary market trading on a national basis. This is a topic to be discussed further in Part III. Second, government insurance may be used as an inducement for risk-averse lenders to make certain classes of loans. A key feature of such an insurance program is that it should operate, on average, without loss, and the current FHA programs are good examples. The alternative to government insurance for this purpose would be to make lenders less risk-averse in a direct fashion. Insurance programs, however, would appear to be the more efficient solution. Third, government insurance may be used as an attempt to aid a mortgage market that has ceased to operate effectively for the reasons of market failure developed above. Here the issue becomes more difficult. A key feature of insurance in such situations is that it is likely to require a significant subsidy. Indeed, loss rates on insured loans will be likely to rise simply on account of the availability of the insurance, since lenders will have only limited incentive to separate good risks from bad risks. On the other hand, some subsidization may be deemed worthwhile if the market would not function at all otherwise.

The Subsidization of Information by the Government: An alternative to insurance in cases of market failure is for the government to subsidize in a direct fashion the information that is necessary for the market to function in a normal fashion. As stressed, many parts of the mortgage market appear to break down because it is too costly for the standard participants in the market to obtain the information necessary for market operation. For example, it may be the case that existing institutional lenders (commercial banks, S&L's, MSB's) do not have the expertise and personnel required to evaluate "core city" mortgages. Under the prodding of subsidization for undertaking credit evaluations in these areas, however, it may be that the market could be made operative. Alternatively, the government may wish to assist a new class of institutions that would specialize in making loans of this sort. In fact, a start has been made in this direction under the FNMA Loan Correspondent program. Additionally, it could be that some existing institutional form of lender, such as Federal Credit Unions, could serve this purpose with changes in their chartering regulations. Whatever the specific form of the institution, however, it should be recognized that a subsidy will certainly have to be provided in the short run for the program to begin. In the long run, on the other hand, there is the possibility that institutions may develop that do not require subsidization.

In this context, it is also useful to distinguish between subsidies for insurance and subsidies for information retrieval. In the case of risk aversion, insurance plans should not require a subsidy, and information is not the problem; consequently, in this context government insurance programs should be supported. In the case of market failure, however, the absence of information is really the basic problem. Insurance programs can provide a partial solution, but the more effective they are, the more costly they will be—and there would be no reason to expect the costs to diminish over time. Subsidies for information, on the other hand, get to the core of the problem, and although they too have a cost, there is at least the hope that over time the subsidy element may diminish.

Further Research: Perhaps surprisingly, there does not appear a great payoff to further large-scale studies of the current operations of mortgage markets by HUD. The problems, as developed here, seem clear, and the effectiveness of alternative solutions is not going to be decided on paper. Instead, a main recommendation is that HUD consider starting a number of pilot programs in which alternative attempts at government insurance and at the subsidization of information retrieval be considered. Such studies could be undertaken with relatively small amounts of "seed money" and the required subsidies would be small given the scale of pilot programs.

Part III: Macroeconomic Considerations: Sufficiency of the Free Market Supply of Credit

III.1 General Principles

The stress in Part II of this study has been on the conditions under which elements of risk can lead to a failure in mortgage markets and therefore to a basis under which government intervention in mortgage and housing markets can be rationalized. These considerations of risk were essentially microeconomic, in the sense that the risk is a characteristic of individual borrowers, and must be faced by the individual lenders. Therefore, the impact of risk, and government programs that affect it, will certainly be found in the distribution of mortgage funds and housing among individuals, but there will not necessarily be an aggregate effect. Consequently, in this part, it is useful to return again at the outset to basic principles, and to develop a macroeconomic or aggregative model of the mortgage and housing markets. As we shall see, the factors relating to government intervention in mortgage and housing markets on the macroeconomic level are quite different—with risk being only a relatively minor one—and our conclusions with respect to the importance of government intervention are quite different from the fundamental role that we suggested for dealing with microeconomic (risk-related) market failure.

III.1.a A Model of Housing and Mortgage Markets: We begin by setting a basic structure for the mortgage and housing markets, in terms of the demand and supply components for housing. Because housing is a durable stock that yields its services over time, the demand for housing is accurately presented as a demand for housing services. Most empirical studies show the aggregate demand for housing services depending on income and wealth variables, demographic variables, and the price or rental rate for units. The supply of housing services, in the short run, consists of the services available from the existing stock of housing. In the long run, on the other hand, the supply of housing services will respond to new construction, which in turn has been shown to depend on the ratio between the market value of a housing unit and the cost of constructing such a unit (see Gramlich and Jaffee (1972), Chapter 6).

The equilibrium of this market occurs, of course, when demand equals supply. The equilibrium is achieved by the price being set at the appropriate level, indicating a movement along the demand curve for the shortrun equilibrium, and along both the demand and supply curves for the longrun equilibrium. It is important to stress that the price referred to here is the market value of a house or, equivalently, the present discounted value of the market determined rental rates.

The mortgage market is closely related to this housing market, but for clarity an analytic distinction should be maintained. A mortgage contract is a loan based on a house as collateral. One could anticipate that the same individuals that are demanding houses also are going to be demanding mortgage loans. But it is critical to understand that the house/loan ratio, or the value-to-loan ratio, is a variable from the homeowners' standpoint that has been shown to depend in a positive fashion on the mortgage rate (see Gramlich and Jaffee (1972), Chapter 5). Consequently, while there is a linkage between house demand and mortgage demand, the relationship is a flexible one. As an additional point, it is obvious that the suppliers in the mortgage and housing markets are different. In the housing market, the supply is built by the construction industry. In the mortgage market, the supply is the funds available from the various lending institutions.

As a perfectly functioning, longrun equilibrium system, the mortgage market achieves its equilibrium by the mortgage rate being set at a level at which the demand equals the supply. To see how the system works then, consider an increase in the supply of available funds by the lending institutions. The increase in the supply of funds will lower the mortgage rate in order to bring the mortgage market into equilibrium. The reduced mortgage rate, however, will then stimulate the demand for housing (since the cost of capital is one of the elements of demand), causing the price of housing to rise in the short run, and/or creating more construction in the long run. The increase in the housing stock could then stimulate more mortgage demand, creating some pressure for the mortgage rate to rise, and in this way the markets would move toward the final equilibrium. Regardless of how the market dynamically reaches the equilibrium, however, the final position resulting from an increase in available mortgage funds would be a decrease in the mortgage rate, an increase in the stock of housing and the stock of mortgages, and some pressure for housing prices to rise.

An important question, of course, is how strong are the effects of the increase in the supply of mortgage funds. The empirical evidence here is quite strong as a number of studies have all pointed in the same direction (see Gramlich and Jaffee (1972), Meltzer (1972), Fair and Jaffee (1972), and Swan (1973)). These studies all indicate that the stimulus to housing, resulting from a shift in the supply of mortgage funds, is very small. Two main mechanisms have been developed to explain this small effect.

First, there is the question of the mortgage-house ratio. As we have indicated, the mortgage-house ratio will rise as the mortgage rate falls upon an increase in the supply of mortgage funds. Thus it is possible—and empirical studies indicate that this is the case—that an increase in mortgage funds results primarily in an increase in the mortgage-house ratio, and only secondarily and in small amounts in an actual increase in housing.

As a second explanation for this result, it has been pointed out that any increase in the availability of mortgage funds that comes directly or indirectly from other capital markets will have the effect of raising the general level of interest rates in the economy. This general rise in interest rates will certainly offset the relative decline in the mortgage rate, and some studies indicate this offset can approach 100 percent. Thus, for both reasons, it appears to be the case that attempts to stimulate the availability of mortgages will result primarily in stimulation for the mortgage market, but not for the housing market.

It is clear that these results, therefore, are generally going to point against the use of mortgage subsidy programs; rather than pursue the policy implications here, however, we shall discuss them in the concluding section. Instead, we first want to take up two special issues—the cyclical behavior of mortgage and housing markets, and questions of changing regional demands.

III.2 Factors Relating to Cyclical Fluctuations of Mortgages and Housing

The material discussed so far relates primarily to the longrun equilibrium of the mortgage and housing markets and to their longrun growth trends. The question of the cyclical fluctuations in mortgages and housing, however, is perhaps equally important. The shortrun environment that is relevant for the cylical factors can differ from the longrun situation just discussed in two main ways. First, one should consider what variables do show significant cyclical fluctuations in influencing the basic demand and supply functions. Second, one must allow for the possibility that in the shortrun the mortgage market is not clearing—that is, that the mortgage rate is restrained from moving to the equilibrium level.

With respect to the variables that cyclically influence demand and supply, the major interest is on the supply side. For the demand side, the variables we have mentioned—income, wealth, and demographic factors—generally do not vary significantly on a cyclical basis. (It should be noted that the income variable generally found relevant in empirical studies is some measure of "permanent income.") On the supply side, in contrast, the most important factor has been the cyclical nature of the flow of funds into depository financial intermediaries—these include savings and loan associations, mutual savings banks, credit unions, and, of course, commercial banks. All of these institutions have shown a tendency to lose time deposits, or to have the growth rate of their time deposits slowed, in periods of high economic activity. This slowing of their deposit growth is related, in turn, to a sluggish behavior in their raising of their time-deposit interest rates. Before 1966, the sluggish rate-setting appears simply a basic part of their behavior; since 1966, it can also be explained by the deposit-rate ceilings that have generally restricted the deposit rate-setting of these institutions. (For further discussion along these lines, see my papers on the Hunt Commission Report—Fair and Jaffee (1971), and Jaffee (1972).)

The upshot on the supply of funds side, therefore, has been a situation in which during periods of high economic activity and high and rising interest rates, the flow of deposit funds to the thrift institutions and commercial banks has fallen off, and consequently the flow of funds for mortgages has been significantly reduced. This, then, appears to be the major factor responsible for the observed cyclical sensitivity of the mortgage sector of the economy. In order to link this with an effect on housing, however, we must also consider the second factor mentioned above, namely the shortrun disequilibrium of the mortgage and housing markets. If the markets were equilibrating in the short run under the conditions just developed, then one would expect the mortgage interest rate to rise significantly whenever the supply of mortgage funds is reduced. One consequence of the higher mortgage rate could be a reduced demand for housing; but, as we have indicated, the empirical results indicate that the major change of a rising mortgage rate would be simply a lower mortgage-house ratio, with the amount of housing investment unaffected. Thus one is led by logic to the conclusion that during cyclical peaks we should find mortgage flows falling off, mortgage rates rising, and housing relatively unaffected by these factors.

Turning to the empirical evidence, however, we find that, in fact, during cyclical peaks the mortgage flows fall off (as predicted) but that mortgage interest rates rise relatively little (that is, they rise in absolute amount, but fall relative to the average level of interest rates) and that housing is indeed adversely affected in such periods. The explanation offered to fit this all together is that during such cyclical peaks, the relatively small rise in the mortgage interest rate is a symptom of a disequilibrium in the mortgage market. That is, the mortgage rate does not rise to its long run equilibrium level, and the result is that mortgage credit is rationed. This results, at least in part, from the fact that many mortgage contracts are negotiated on an advance commitment basis that can occur as much as a year before the contract is actually taken down. From the borrower's standpoint, this means that he finds relatively low rates of interest in the mortgage market, but funds are simply not available at this rate. It might be noted that this is fully consistent with the view of the various special interest groups, discussed above in section II.3, in which their major concern is not with the cost of mortgage funds, but with the availability.

The implications of this view should be treated with care. There are basically two solutions available for solving the problem of short-run disequilibrium (or limited availability) in the mortgage market. One possibility is to encourage the lending institutions to raise their mortgage rates more quickly, thus allowing the price (or interest rate) to clear the market as it would normally in a longrun situation. This would involve structural changes in the mortgage market, including perhaps, some change in the manner by which advance commitments are negotiated. The other possibility is for government agencies (FNMA, GNMA, etc.) to fill the gap between the demand for funds and the private supply of funds during such periods. This latter solution would then effectively make the existing mortgage rate the market clearing rate, given the appropriate amount of government supply.

In terms of actual events, considerable progress has been made along both of these lines in reducing the cyclical tendency of the mortgage and housing markets. As a case in point, the relatively good performance of housing in 1969, compared to the dismal performance in 1966, is generally used as the example. But while progress has been made, it is clear there is still room for more advances in both of the indicated areas. To be specific, along the lines of strucural change, the proposals of the Hunt Commission should be seriously considered. In previous studies (Fair and Jaffee (1972) and Jaffee (1972)), I have provided arguments in favor of these proposals, so I will not repeat them here. I stress, however, that it is my view that Hunt Commission proposals for structural change will help housing and mortgage markets, even if deposit-rate ceilings are removed (and they should be). To be more specific along the lines of government supplied mortgage funds, I would argue mainly in favor of the extension of current programs for creating a thick and orderly secondary market for mortgages. With regard to programs that directly supply mortgage funds to the market, I suspect that current programs are quite adequate. In particular, I want to stress that the available FNMA and GNMA programs have been shown to have an effect on the housing mortgage only during the one or two quarters of the most severe credit rationing; in any longer-run context, substitution of public mortgage funds for private mortgage funds occurs, with no net effect observed for the FNMA or GNMA operation.

III.3 Factors Relating to Changing and Imbalanced Regional Demands for Mortgages

We now turn the discussion from the disequilibrium of mortgage markets over time to the imbalance of mortgage markets over different geographic locations. It has been observed frequently over time (see Fredrikson (1971)) that mortgage interest rates in the Northeast United States are significantly lower than the equivalent mortgage rates in the South and West. Indeed, results have been obtained that show there is a high and significantly positive correlation between the level of the mortgage rate in a region and the actual distance of the region from a point in the Northeastern United States.

Now, if the private markets are to respond to this situation, then we would expect a flow of funds available for mortgages from the Northeast and to the insufficiently supplied regions. To some extent this has been observed in a variety of ways, and it is useful to list at least some of them. For one thing, thrift institutions in the South and West have competed very strongly for deposit funds, and have succeeded in creating a flow of funds toward their region. For another, national lenders (such as insurance companies) have naturally been attracted to the affected areas and have tended to invest more than the normal proportion of their funds in mortgages in these areas. Finally, even local lenders (that is, local thrift institutions) have found some means through which they can invest surplus mortgage funds in mortgages from the insufficiently supplied regions.

What is surprising, however, is that these various interregional funds flows have not been sufficient to solve the problem—specifically, we continue to observe the regional spread in mortgage interest rates. Two questions then arise: First, what has stopped the private markets from achieving the complete equalization of mortgage rates in different regions? Second, is there a useful role for government intervention in the private markets on these grounds?

With respect to the question of the private markets, several answers have been suggested, and each appears to have some validity. First, there is the point that the data are less than perfect, and part of the problem may therefore be reporting an error. Second, the contracts that are being compared for the different regions may actually be different in terms of their technical features or in terms of the riskiness of the contract. Third, and finally, it is known that there are a variety of constraints that limit and inhibit the ability of various financial institutions to undertake the necessary capital flows to erase the regional differences. It is hard to evaluate the relative importance of these factors, but the third factor has certainly been acknowledged as important (see especially Fredrikson (1971)).

With respect to the question of government intervention, one obvious direction is to eliminate any government regulations that do currently limit the ability of financial institutions to make regional fund flows. Such proposals, for example, are provided in the Hunt Commission *Report* (1971), and they should be carefully considered. And, along the same lines, any other proposals that serve to perfect the capital markets are also likely to help solve this problem (for example, deposit insurance has aided the interregional deposit flows that do occur). More forceful policies, of course, would involve government agencies in supplying funds to the appropriate regions. In fact, there already exists a mechanism—the various regional Federal Home Loan Banks (as well as the Federal Reserve Banks, possibly)—through which such funds could be disbursed. It should be indicated, however, that the regional differences do not appear to be one of the major problems facing the mortgage and housing markets, and thus the Hunt Commission proposals might well be tried as a first step, and the dimensions of the problem then reconsidered.

III.4 Conclusions

The basic question considered in this section has been whether the free market supply of housing credit on an aggregate basis can meet consumer demand. We have indicated that three more specific questions have to be distinguished: Will the longrun supply of housing credit be sufficient? Will cyclical factors interfere with the shortrun supply of housing credit? And are differences between regions of the country likely to create problems? Perhaps the most important point to make in conclusion with respect to these questions concerns the extent to which the problems that do exist in aggregate housing credit markets are "manmade." That is, many of the problems in housing credit markets are the result of government legislation and intervention in these markets that were undertaken at some earlier time and in a different setting. To be specific, we have indicated how the proposals of the Hunt Commission *Report* are to an important degree directed at eliminating capital market restrictions of this sort.

A second major point concerns the difference between a mortgage subsidy and a housing subsidy program. It was argued strongly and at length in Fair and Jaffee (1972) that housing subsidy programs generally will be more efficient in terms of housing output per dollar input than mortgage subsidy programs. The reason is that mortgage subsidy programs operate only indirectly on housing—their direct effects are to increase the amount of mortgage financing. For this reason, mortgage subsidy programs should be used primarily as shortrun stopgaps when disequilibrium characterizes the mortgage markets. Under such circumstances, financing would be a binding constraint on housing investment, and thus programs that alleviate the mortgage constraint will be of value. In any longrun context, however, there is a strong presumption in favor of housing subsidy programs. These programs can include the so-called "brick and mortar" stipends as well as various rent reduction programs.

A third and final major point relates to the interest elasticity of the demand for housing. It is frequently observed (and documented in Fair and Jaffee (1972)) that the demand for housing is significantly more interest-elastic than the demand for fixed-productive capital investment. The result, therefore, is that in periods of high interest rates, housing investment tends to decline relative to business investment. This raises the question of whether this is acceptable or whether government subsidy should be attempted in order to raise housing investment in such periods. Even more basically, one should consider why housing demand is more interest-elastic. One possibility is that the capital markets are particularly imperfect with respect to housing. Our discussion has indicated, however, that on the aggregate level this is not the case. The important exception, perhaps, concerns the technical aspects of the mortgage contract under inflation—Tucker (1973) has argued that the cost of mortgage credit rises "artificially" under inflation, and that changes in the contract should be made—and it would appear that he is quite right. The alternative ground for the high-interest elasticity of housing is that consumers view housing as a postponable purchase. If this is the case, then there may be true and "real" economic foundations for the high elasticity; and it would follow that care should be taken in devising subsidy programs that circumvent what might be the most efficient response of the economic system to high interest rates.

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Improved Housing and Health State: A Focus on Rural Housing

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Summary

Previous housing policy has assumed the low income user to be an undifferentiated constant; it failed to consider seriously housing as a process. The predominant focus on adequacy of housing stock—which is in and of itself a worthy goal—fails to address the more pervasive lifestyles found in rural areas. The magnitude of inadequate housing in rural areas constitutes a national crisis. The sheer burden of existence in a debilitating residential environment reinforces the alienation and apathy—and, finally, resignation—so common in rural areas. The amelioration of generations of ills is not easily nor quickly possible. There is, however, a clear and highly visible product of Federal neglect that can best be remedied by a recognition of the need for people-oriented policies.

Results of the rapid urbanization of rural America have brought the associated problems of residential relocation, occupational change, and a host of others. While this population shift brought with it an inordinately high incidence of physical and mental health problems, there is no evidence either of actions to facilitate this process of change or to predict and anticipate future problems of a similar sort. There are, however, groups in Mississippi, eastern Kentucky, and elsewhere that have addressed these issues and attempted to resolve inadequacies of public policy.

The resolution of the rural housing crisis can be viewed in two stages. Stage one is the development of a delivery system that can function effectively to correct serious housing deficiencies that affect safety and physical health. This delivery system is critically needed in rural areas where housing problems are the most severe. This rural delivery system should be oriented towards providing basic sanitation (clean water and waste disposal) and structurally sound living space for the low income population. Public funds first should be used to alleviate the worst housing problems. Realistically, this approach necessitates building or rehabilitating units for the very poor that are smaller and of lower quality than those occupied by moderate income families.

The housing delivery process should be viewed (and planned) as one component of a comprehensive service delivery system to be administered at at the local level by a central governmental agency. Such a comprehensive delivery system would include housing and the basic human resource services, e.g. health care, day care, welfare, etc.

Stage two is the introduction into the housing delivery system of a predictive process based on the rationale that the ability of people to influence public decisions that affect them will have a direct and abiding influence on their satisfaction and, ultimately, their health state. This predictive process would include involving potential users in the decisions concerning the location and size of new projects, the types of services to be provided, the design of living units, and the type of management. The Government should take the responsibility for assessing the needs and preferences of potential users in a specific locale. From this assessment a programmatic set of requirements can be formulated. This program then becomes the criterion to be used in the planning and design of the project. Three specific strategies for implementation have been developed:

Involvement of Users in the Housing Process

The involvement of affected people in the decision process is clearly the beginning of establishing a better understanding of the meaning of a "suitable" living environment. The formulation of programs that verbally and graphically describe the housing needs and preferences of low income families can enable planners and designers to produce suitable environments. To secure the type of user participation necessary, the Government must develop administrative techniques that encourage low income people in a specific locale to voice their feelings. Essential to this process is the need for a clear presentation to users of the types of decisions (i.e., site location, room layout, community facilities, etc.) that must be made and of the alternatives possible.

Postconstruction Evaluation of All Federally Subsidized Housing

To determine the degree to which designs meet the programmed needs of the users, a postconstruction evaluation of Government-assisted housing projects should be conducted. The purpose of this policy would be to provide a continuous process of feedback and assessment to the professionals from the user's point of view. The Government should take the responsibility for preparing the evaluation and communicating the results to the professional community and the user groups.

Performance Oriented Housing Approach

At present, we establish housing standards in the form of building codes and minimum property standards based on the assumption that human behavior can fit into traditional three- and four-bedroom dwelling units. The standards are generally oriented towards the traditional middle-class view of "housing necessities," and deal largely with housing technology. What are needed are performance requirements or a performance code that would state the desired attributes of a material, component, or system in order to satisfy the needs of the intended user without regard to the specific means to be employed in achieving the results. Performance requirements would be derived from the characteristics of users (the physiological, psychological, and sociological needs and processes) which the built environment can affect. In short, a performance code would be the legislated final result of the process of involving users in the housing delivery system.

Introduction

For the past half century, programs of social action have been directed toward the achievement of improved housing for substantial segments of the population. These programs (such as health codes and code enforcement, and regulation of housing infractions) have stemmed, no doubt, both from humanitarian beliefs in social justice and from the pragmatic belief that housing plays a central role in health and well-being. The belief that housing is a factor in physical and mental health has arisen from the clinical and common sense observation of physicians, public health officials, criminologists, law enforcement agencies, sociologists, welfare workers, and others, that many health and social disabilities have greatest prevalence in areas—urban or rural—in which the poor reside. While it is evident that deleterious housing is caused by poverty, housing can be isolated as an independent measure.

The effects of an unsatisfactory residential environment upon man's physiological health and psychological well-being, together with his inability to escape from these conditions because of economic and/or educational reasons, demand immediate and extensive involvement by the Federal Government.

The home and its environs commonly involve more of man's time and that of his family than any other single place in an urban or nonurban area (1).

The most severe threats to health and well-being in the residential environment affect the poor. There are at least 12 million households (approximately 44 million people) who are forced to pay in excess of one-fourth of their income for shelter; the majority of these households are low and moderate income (2). Families are forced to pay excessive amounts for housing because shelter, even when inadequate, is very expensive compared to other consumer items. Over the last 20 years, shelter costs have increased at a much faster pace than disposable personal income (3).

Thus, when a family is living on a relatively fixed income (which most of the poor are doing), the only two alternatives to increased housing costs are to spend more money or to vacate. Both of these alternatives result in problems. To spend more money on housing means reducing the amount available for food, medical care, transportation, and the various constructive forms of release for emotional tensions. To vacate each time shelter costs increase means to move into successively lower quality or smaller housing accommodations.

Too little recognition has been given to social and psychological aspects of housing in relation to human health and welfare. Basic human needs must be met to insure the health and well-being of individuals and families. These needs are fulfilled, in part, through tangible goods and services, including sound dwelling and means of maintaining the home and its furnishings and equipment.

Noted psychologist Abraham Maslow has developed a classification of basic human needs which are ranked in ascending order. Each need must be satisfied before an individual can function at the next higher level. They are:

- Physiological needs such as hunger, thirst, rest, and activity.
- Personal security and safety and release from anxiety aroused by threats of various kinds.
- Love needs, including acceptance and a feeling of belonging in one's relationship with parents, friends, and other social groups.
- Esteem needs, including a sense of self-mastery and self-worth.
- Need for self-actualization through creative self-expression in personal and social achievements.

In family life, goods and services connected with housing and its environs provide satisfaction of a basic need. A dwelling can furnish shelter and protection, thus contributing to physiological and safety needs. The value of household inventories and of the home itself, if it is owned, may contribute to family financial security and personal esteem. The house and its furnishings can serve to provide an important element of family social and spatial environment. Spatial patterns provide the setting for social interactions in which love, esteem, and self-actualization needs may be met. Where the dwelling fails to provide protection from the elements and hazards, basic sanitation and facilities, adequate space for living, and privacy in sleeping, the social and psychological health as well as the physical health of its occupants is endangered.

Although this report describes the health problems related to housing, the combined effects of these problems may produce irreversible effects that would not result if they occurred singly. The problems should be considered in a total program of managing man's residential environment.

Lack of Interest in Physical Conditions: The Effect of Tenure and Turnover

The following discussion is drawn from Robert Coles' analysis of the hollows of Appalachia in which he combines clinical work and social observation.

In the outlying valleys and hollows, where plumbing may be virtually nonexistent, one can see an almost uncanny mixture of the tidy and the orderly, the littered and the unkempt. Among migrants and sharecroppers, Coles found a pervasive lack of interest in the house, its appointments and appearance. "We leave them, one after the other," a migrant farm worker once said when asked whether he ever tried to give his home the same scrubbing he was then giving his car. Likewise, among tenant farmers in the rural South, a similar indifference was noted.

Although many of the cabins have been abandoned, thousands remain inhabited. Those who remain know they have been left behind—have, in effect, been chosen to be left behind—feeling stranded, perhaps (4). "I don't know why we're still here, but we are; and I guess we always will be, yes sir."

Poor housing conditions are but one of several objective expressions of poverty that include absence of money, and the presence of hunger and malnutrition, parasites, and disease.

A boy of eight drew a picture of his house; the kitchen, in this case, was the entire house. He had this to say: "It's what we have. It's not the best place to live in the world, my mother says so, and if we looked far enough, we might find a better place, but it's ours, and so long as we're here, there's no reason to leave, because before we'd be long on the road, looking for something better, we'd probably get put in jail or get bad sick, and there'd be no one to help us."

The following quotations are based on a study conducted by R. J. Margolis, former research director of the Rural Housing Alliance. "In a bad house," a sharecropper has remarked (5), "troubles do tend to batch." There is no place in a bad house to iron out one's troubles, either in private or as a family. "The whole front room was filled with beds," recalled a former shack dweller who, with his wife and eight children, now lives in a better house. "There were just narrow aisles between the beds, like a dormitory in a school, except there was no room to study. We had another room in the back, but the only way you could get to it was to walk out the front door and around the house and through the back door." He was lucky; few shacks had back doors.

Noise, crowds, nerve-shattering pressures—the classic depredations of urban life—are the daily tormentors of low income rural families. The toll they take on family morale is incalculable. "I keep yelling at the children," says the grandmother of a large farmworker family. "Out of my way . . . can't get by. I try to stop, but I can't."

The shack, then, is both the medium and the message. Its gloom generates a kind of creeping helplessness that steals upon one. "It can't be fixed, it can't be fixed, it can't be fixed. When it leaks in one room," says a Mississippi woman "'we move to another."

Review of Research Strategies

The major criteria of housing quality or the "independent variable" used in most housing research generally are discrete elements of housing usually obtainable from census data or explicit measures of crowding. Another housing criterion consists of more general indicators of housing quality, ordinarily not measured explicitly but rather inferred from the general environs or employing subjective estimates of overall quality. Typically, the studies attempt to have test and control housing representing good and bad housing, respectively.

The dependent variable, containing those factors whose association is being sought, have generally been an investigation of one or two entities, such as morbidity or adjustment, which generally have considerable medical or social importance. Typically, their studies focus on single disease categories such as pneumonia (6), respiratory infections (7), streptococcus infection (8), as well as crime (9), psychoneurosis (10), and children's programs in school (11).

Investigations of a small number of serious or traumatic dependent variables are appropriate when the interest is primarily in the variables under consideration. For those with an interest in housing, this type of research offers some handicaps to an understanding of the general range of influence of the housing environment on human affairs. Moreover, concentration on such matters as tuberculosis, infant mortality, and juvenile delinquency singles out only the "very serious" end of the range of possible physical and social variables.. It is entirely possible that the maior effects of housing—as indicated by influences on the largest number of persons—may well lie below the level of the seriously traumatic, and may not necessarily be measurable exclusively by the more traditional pathologies that reach the state of public statistics.

There is, furthermore, a question as to the adequacy of exclusively negative measures. Treating good or improved health only as absence of lowered incidence of recognizable disease may possibly be sufficient. For psychological health and social adjustment, however, adequate measurement at the positive end of the scale seems unlikely to emerge from concentration on crime, delinquency, and suicide rates alone.

Although there have been numerous attempts to define mental health and mental illness, there is still little accord on the definition of these terms in the health field. The term "mental ill health" has been used by different researchers to refer to such diverse manifestations as schizophrenia, suicide, unhappiness, juvenile delinquency, and passive acceptance of an intolerable environment. Many researchers regard subjective unhappiness as a symptom of mental disorder. It is, however, important that unpleasant feelings may persist and may lead to serious physical disturbances (12).

In varying degrees, the frontiers of research in housing are reaching the problems of types of housing demand (13) or the "ecology" of the dwelling—that is, the internal spatial design of dwellings as a self-contained shelter for social relations and personality development—(14–16); resident morale in planned communities (ranging from mere inventories of complaints to explorations into the determinants of morale) (17, 18); the social and psychological consequences of diverse managerial policies and practices (19); the social relations between residents in housing projects and environing community (20); factors involved in privacy (21, 22); and emerging social organization of residents (23). In several of these spheres, there are continuing advances in research methods and procedures (24).

Previous empirical studies have made an important case for the argument that physical planning is an important influence on individual behavior and social action. Planning for housing, however, like other physical and biological conditions to which human beings respond, is significant in the sense that without it there would be no human society as we know it. The issue is no longer the relative importance of the physical environment to other factors, but rather whether spatial differences in the environment are related to corresponding differences in attitudes and behavior.

Different approaches for the study of housing design and social values have been used yielding different types of data.

Wants and Preferences Approach

The first is the wants and preferences approach that gives clues as to sales appeal items that would attract home seekers' attention before purchase (25). These surveys of family preferences have covered such structural items as stories and number and types of rooms. The weakness of these studies that ask about dining rooms, kitchens, bedrooms, and basements is that families must answer within the limits of their experiences, necessarily disregarding environmental possibilities beyond the scope of their experience. Reimer has pointed out that persons quizzed about their wants and preferences are likely to respond to whatever housing wants are currently of greatest concern. Wants satisfied by his current accommodations will be overlooked in favor of wants most keenly felt in comparison to what other families in his social range have acquired.

Likes and Dislikes Approach

Second is the likes and dislikes approach that reveals obvious malfunctioning features experienced while living in a particular place. In considering social factors related to planning of neighborhoods and its positive contributions, Foote (26) has stated that "When the housing consumer evaluates his neighborhood satisfaction, his central concern is neither geographic site nor physical characteristics." Among consumers satisfied with their location (nearly ⅔ to ¾ of all consumers), the chief reason for satisfaction seems to be the social characteristics. Furthermore, studies have shown that neighborliness is best achieved in groups that have more similarities than differences and that neighborhoods are likely to continue to be more homogeneous than heterogeneous from the standpoint of social characteristics.

A survey of housing likes and dislikes with the purpose of providing answers to architects and builders was conducted by Paxton (27). The study dealt with the features the buyers liked in their houses, the changes they would make if they were to buy another house, and the changes buyers would have made if they had had to buy a lower priced house. Though the results show wide variations in the responses of buyers, no effort was made to relate the responses in terms of sociopsychological or economic variables.

These studies provide knowledge about the preferences of a given population at a certain time without providing any theoretical basis that can influence future planning decisions. To fill the gaps between "wants" and "dislikes," studies were made dealing with actual use-patterns from which inferences presumably could be made as to the "workability" and "suitability" of the environment for other families. However, due to the plasticity of human behavior, different family types adopt their use-pattern to tremendous varieties of dwelling structures, and therefore the information gathering had limited predictability for other families. Also much of the detail that went into precise evaluation of housing operations seems to have been above the average user's threshold of awareness.

Household Activities Approach

Another approach has been to analyze household activities; that is, what goes on in the house. The activities approach is sounder than the previous approaches because it provides a valid basis for the design of housing that is more consistent with the preferred mode of performance of activities in the household. This is significant because there is a higher degree of similarity among the types of activities that are performed than in the spaces in which they are performed. This approach also deemphasizes the influence of existing house arrangements on the research results.

Many studies have tried to establish the relationship between deviant behavior and housing. The concepts have been undergoing a process of evolution. Earlier studies (28) showing a relationship between substandard housing and deviant behavior led people to believe that substandard housing is a cause of deviant behavior. Comparatively recent studies (29) have indicated that such a cause-effect interpretation is not valid.

In the light of these, it is being recognized that it is important to study the setting in which a host of social, economic, and political factors operate, and also the interpretations given to these settings by the people who find prosperity and depressions are important only in terms of aspirations, needs, socially defined status, and cultural conditions of the person (30).

Other studies have tended to relate social phenomena with housing. For example, the M.I.T. study of the Westgate Housing Development shows that physical layout is clearly related to the pattern of group formation and the several pressures they exert on the residents (31).

In other studies, research by Collins and Deutsch (32) and by Merton (33) concur in the finding that the residential environment has a marked influence on race attitudes and friendship formation between the races.

Rainwater stresses the aspect of "high threat expectancy" in low income families with the implication that housing design can ameliorate at least the nonhuman dangers since housing has its prime purpose in sheltering individuals from threats in their environment. The taxonomy of dangers that Rainwater describes are human (e.g., violence or hostility) and nonhuman (e.g., fire, freezing, cost, or deterioration) and in Fried's work (34) it is suggested that in one type of working class lifestyle, the families are content with much about their housing —even though it is below standard in the eyes of housing professionals—if the housing does provide security against the most blatant of threats.

In addition, studies of attitudes, preferences, and behavior can be extremely misleading unless they are related to an understanding of the number of types of families in the housing market and the lifestyle of the consumer. A significant portion of families that occupy housing consists of single persons, households of two or more unrelated persons, married couples, and widowed, divorced or separated persons with or without children. Most studies of housing preferences deal only with husband-wife-child type families.

It is also clear that housing preferences relate directly to one's stage in the life cycle, where a person stands in the sequence of childhood, marriage, parenthood, and later life.

From the implications of the research findings stated above and other research in related areas, one may impute that the whole sociohousing environment should be related to the residents' total scheme of values.

Explanations are necessary in the context of social and psychological factors, individual's various physical needs and preferences, and neighborhood-related attitudes and values. There is research needed on the way multiple needs are compromised in order to fit them into an adequate accommodation and on their differential impact on housing values and on members within a family. The associated environmental factors are the location of the dwelling unit to other major social environments where family members participate, the extent to which housing design encourages or discourages performance of the living functions within the dwelling space or outside of the home, the orientation of neighborhood dwelling units to each other and to local neighborhood contact centers, and the ways in which the spatial organization is related to the interaction of family members with each other.

It is necessary to recognize that families are influenced by their environments in all sorts of ways that neither the family, the designer, nor the social scientist alone may be aware of. In order to provide appropriate housing environments, a designer must be familiar with the social traits, activities, and desires of a diverse population. Research investigations could form the basis for understanding how housing design relates to human values.

The assumption is that there is an important relationship between spatial arrangements and social behavior. Thus the implication for social ecology is that common residence in the same size and same density does not imply common psychic or social exposure to the same set of environmental stimuli. The manipulation of physical space does have effects on social behavior, but the effects will vary according to the presence of nonphysical variables. Thus, there is literature that suggests that the architect who designs a house and site plan, decides the location of roads, the orientation to other dwellings, and the proximity, is to a large extent deciding the pattern of social life among the people who will live in these houses.

Conversely, other studies of social life have shown that people tend to choose friends on the basis of similarities in backgrounds, such as age and socioeconomic level, values such as those with respect to privacy and child rearing and interests such as leisure activity preferences (35).

These findings suggest that social relationships are influenced and explained by people's homogeneity with respect to a variety of characteristics.

Gans (36) suggests "if propinquity is most important in determining friendship formations and neighbor relations, the ideal patterns—if such exist—would have to be implemented through the site plan. If homogeneity of characteristics is most important, the planner must decide whether to advocate homogeneous residential areas, if he wishes to encourage friendliness and friendships among neighbors, and heterogeneous ones, if he wishes to encourage more distant neighbor relations and spatially dispersed friendships."

The existing studies suggest that the two explanations are related, but that homogeneity of characteristics is more important than propinquity (37). Although propinquity initiates many social relationships and maintains less intensive ones, such as being neighborly," it is not sufficient by itself to create intensive relationships. Friendship requires homogeneity.

Gans (38) argues that though homogeneity violates the American dream of a "balanced" community where people of diverse age, class, race, and religion live together, heterogeneity at the level where face-to-face interactions occur will not produce the intended tolerance, but will lead to conflict that is undesirable and essentially insoluble. He further suggests the elimination of the neighborhood unit and plans for a heterogeneous array of homogeneous blocks, each separated from the next by a real or symbolic barrier to assure those concerned with property values.

Thus, the nonphysical dimensions may be as follows:

- Relations with neighbors.
- Attitudes and behavior toward neighborhood community.
- Social self-concept and aspirations.
- Personal and family relations.
- Psychological state (optimism-pessimism).
- Reactions to neighborhood environment.

From these dimensions it is possible to extrapolate a number of variables for testing hypotheses.

Ethnic Group and Migration

Series of associations between mental illness and ethnic group and between mental illness and migration have been reported. At present, blacks are experiencing much higher rates of mental institutionalization than whites.

Mental hospital admission rates have been substantially higher for foreign-born than native-born white populations during periods of heavy migration, such as in New York State in 1939–41. In Manhattan, impairment rates were similar for the foreign-born and the native-born and for the native New Yorkers and those who migrated from another State within the U.S. after World War II (39).

In attempting to reconcile these disparate observations, it is evident that the circumstances of migration within the borders of the United States were very different in 1939–41, shortly after the peak of Depression, from those after World War II. The earlier period reproduced in the migrant group much more closely the economic deprivation that had been consistently associated with high mental illness rates. If migration is causally related to mental illness, then it is possible that recency of migration and the economic circumstances accompanying it are important modifying factors. The current excess of the hospitalized mentally ill among blacks is compatible with such interpretations, particularly in view of the rapid urbanization of rural areas.

Death rates for all causes in the United States were higher in urban areas than in rural prior to 1950. By 1960, however, the rates had become reversed, rural rates being higher than urban, and since 1960 the ratio of rural to urban deaths has been increasing steadily (20). Thus, paradoxically, even though cities have been increasing in size since 1940, death rates have fallen more rapidly in these crowded circumstances than in the more sparsely populated rural areas. Part of this phenomenon may be due to improved medical care and sanitation in cities and part to the migration of younger people to cities leaving an older, more susceptible population behind in the rural areas. While these may be partial explanations for the reversal in rural-urban health ratios, it is clear that the rural excess in the incidence of scarlet fever cannot be attributed to either of the above phenomena.

Death rates rise during periods of industrialization and urbanism as explained by the incidence of tuberculosis during those periods, yet rates have fallen off and continue to do so despite increasing population density. In some recent studies (41), it has been found that tuberculosis does not necessarily occur under crowded conditions but under circumstances where people are socially isolated. No relationship was found between crowding and tuberculosis in a study conducted with all families living in a city. Those individuals living alone, however, had a tuberculosis rate some three to four times greater than families.

Migration theory and its implications will be further expanded in the section entitled Population Density and Crowding.

From the data then, urbanization and social change can contribute to the individual's health state. In fact, Caplan's paradigm, the concept of life crisis, suggests that during a person's development he encounters periods of psychological unrest generated by a state of transition or a challenge of greater severity than he is accustomed to cope with.

Prevention

Measures for the primary prevention of mental illness are of two kinds: 1) those directed against the specific diseases known to be responsible for organic brain syndromes, and 2) those directed at psychosocial situations believed to have relevance to the functional disorders. In both cases, the effect of the measures on mental illness is an indirect one, since in a well-organized community such programs would be undertaken regardless of their impact on rates of mental illness. The provisions, then, of adequate housing consistent with the human needs of its occupants would be a worthy objective in its own right, whether or not an impact on mental illness could be statistically verified. Clearly both objectives, improved housing and community programs, are equally important in preventing mental illness.

Caplan (42) describes psychosocial and physical components of a prevention program in terms of "supplies" needed by individuals to remain healthy. These supplies are described as food, shelter, sensory stimulation, and the like. Failure of one or more of these supplies at appropriate stages of development may shift a person toward the illness end of the illness-health continuum. In addition, a person's development is punctuated by "crises"—periods of emotional and psychological unrest prompted either by the transition from one phase of development to another or by a hazard or challenge imposed by the environment of greater severity or duration than that with which the individual is accustomed to cope.

Against this background, Caplan describes a variety of professional, social, and legal actions aimed at providing appropriate "supplies" or supporting people in crises that are seen as being preventive of mental illness. Included are actions aimed at provision of adequate housing and its influence on safe-guarding family integrity and functioning, in addition to prevention of mother-child separation, parental education, etc. As Caplan and most other proponents of such notions readily admit, the effectiveness of any component in reducing mental illness rates remains to be demonstrated. The fact, however, that a substantial body of psychiatric opinion believes that such a reduction is a likely effect lends additional rationale for support on a far wider scale than now exists (43).

Health and Inadequate Maintenance of Basic Sanitation

A number of health problems are related to inadequate facilities and provisions for maintaining basic dwelling sanitation. Acute respiratory infections (colds, bronchitis, grippe) and certain infectious diseases of childhood (measles, chickenpox, and whooping cough) are causally related to multiple use of toilet and water facilities, inadequate heating and ventilation, and inadequate and crowded sleeping arrangements. Minor digestive diseases and enteritis (typhoid, dysentery, diarrhea) are related to poor facilities for the cold storage of food and to inadequate washing and toilet facilities. Studies by the U.S. Public Health Service show that the incidence of certain parasitic diseases can be reduced fourfold simply by the installation of water closets inside the dwelling unit. In addition, interior water closets reduce accidents and respiratory infections from exposure to the cold of winter. Infectious and noninfectious diseases of the skin are related to crowding and facilities for washing.

Vectors of Disease

Rats proliferate in many areas where environmental sanitation is grossly inadequate—commonly in the poorer parts of our urban centers. In 1957, the rodent population was estimated at 90 million. In 1965, rats and mice caused an estimated \$900 million in damaged food and property. In the same year, no fewer than 6,000 cases of rat-transmitted diseases and 14,000 cases of rat bite were reported nationally (44). Sampling surveys in New York City revealed that reported rat bite cases are about one-third of the actual number each year.

Rat-borne diseases include murine typhus fever, plague, salmonellosis, trichinosis, Weil's disease, and rat bite fever. Contact with a rat is not essential to transmission of some of these diseases; victims have become infected while living or working in rat-infested buildings (45). In addition to disease transmission, the presence of rats in the home and/or evidence of an encounter, such as an infant's rat-multilated lip or ear, may have deep adverse psychological effects on an individual's personality. Helpless persons (infants, aged, paraplegics, and persons incapacitated by alcohol and drugs) are attacked more often than able persons (46). In cities, rat-inflicted injuries are more common under crowded conditions, in substandard housing, and in areas with poor environmental sanitation, or in neighborhoods where rat-infested property is being destroyed. However, rats do not respect socioeconomic status and have been found alive in covered toilet bowls of upper socioeconomic homes, having entered the home via sewer lines (47).

Personal and Family Stresses Conditioned by the Residential Environment

Injury, illness, incapacity, and death are not the only dangers or problems in housing and its environs. The mere threat of such physical harm from human violence and nonhuman dangers inhibits a state of emotional well-being; many urban poverty groups are particularly sensitive about the security that housing should provide against the most blatant threats (48). The National Advisory Council on Civil Disorder points out that 47 percent of the housing units occupied by nonwhites were substandard and 24 percent were overcrowded in the 1967 civil disorder areas.

One's home is a symbolic extension of one's self (49, 50). Rats, overcrowding, the stench of inadequate plumbing, and the inability to keep one's family from freezing in winter convey to slum dwellers in devastatingly graphic terms their inability to control their own destiny and provide a stable family environment. The physical and social disorder of their world presents a constant temptation to give up or retaliate in kind (51, 52). The continuing disparity between slum dwellers' housing expectations and their lack of fulfillment has been stressed as a common source of recent ghetto rioting. The long-term consequences for health and well-being in adapting these and previously mentioned psychological and physiological problems associated with the residential environment are unknown.

Wilner (53), in a longitudinal study of 5000 persons, found that rehoused slum families, in contrast to control families remaining in the slum, responded to greater space and improved dwelling conditions. The findings show that larger proportions of rehoused families liked their apartments, commented favorably on the safety of their children's places, felt they were getting their money's worth for the amount of the rental, indicated an increased likelihood for personal privacy, and reported less friction and dissension directly related to space. Other factors were:

1. Better personal relations and lessened friction between family members (particularly in the mother's reaction to and discipline of children). The data showed an increase in mutually shared activities, both routine and leisure-time pursuits.

2. Markedly increased assistance to neighbors with household chores, children, and in time of illness. Closer and more amicable relations with neighbors occurred among test families as a consequence of differences in their physical environments. Some of the factors in the housing project that were considered conducive to the formation of these relationships by the test group were: a dwelling architecture providing many opportunities for daily contact, a dwelling unit possessing some aesthetic qualities and sufficient room space, and the existence of facilities used in common under noncompetitive circumstances.

3. More pride and care in maintaining their immediate neighborhoods. The rehoused families reported more activities devoted to keeping up the neighborhood and gave far more favorable views regarding its adequacy as a place to live and to raise children.

4. An increased sense of improvement in their position in life, even without increases in income. The findings show that test respondents more than controls were likely to indicate felt improvement in their position in life and to report themselves rising in the world. Findings for a series of 10 psychosocial scales consisting of variables pertaining to the self-revealed optimism and satisfaction with personal state of affairs as a result of moving from a generally depressed and deprived environment to good housing.

Psychiatrists believe that these factors indicate a more stable emotional state and better mental health. Rainwater (54) found that rehoused slum families evidenced a "dramatic drop in anxiety about nonhuman threats within the dwelling" and viewed the improved house as a haven from human threats, but not a complete solution to human threats.

The Impact of Government Housing Programs on Mental and Physical Health Problems in Rural Areas

In the first section of this paper, the causal relationship between inadequate housing facilities and infectious disease was defined. The relationship between poor housing and mental health problems was also explored. The effect of poor housing conditions on health has long been an issue of public policy. In 1949, Congress declared that the health and living standards of American people required that government efforts be initiated to realize the goal of a "decent home and a suitable living environment for every American family" (55). During the past 2 decades, the categorical programs designed by the Federal Government to produce decent housing have not been sufficiently funded and/or administered to alleviate inadequate housing (56). While the vast majority of critical evaluation has been related to Government housing efforts in urban areas (57), recent testimony before the Select Senate Committee on Nutrition and Human Needs indicated that two-thirds of all inadequate housing was outside metropolitan areas (58). Unfortunately, systematic analysis of rural housing needs and Government efforts is not available. Rather, we must depend upon case studies that relate to a rural context.

When assessing Government housing efforts in rural areas, we are concerned with two categorical programs: 1) the rural housing program administered by the Farmers Home Administration and, in some cases, 2) the public housing program administrated by the Department of Housing and Urban Development (59). The following text explores the effect of new and rehabilitated Government-assisted housing on the mental and physical health of rural Americans.

There are important differences in rural and urban housing conditions that can affect health status, particularly physical health. First, the predominant urban housing problem is overcrowding. The effects of crowding have been more extensively investigated than other measures of housing quality. As a result, crowding has been identified as the major housing characteristic that influences health in urban areas (60). Crowding bears a psychological relationship to stress, which affects mental health (61).

By comparison, in rural areas inadequate waste disposal and water supply are the most prevalent housing problems (62). This is not to say that overcrowding and deteriorating structural conditions do not exist and are not important. However, inadequate sanitation can have a serious effect on physical health state. Evidence of the adverse effect of inadequate sanitation on infant mortality and infectious disease can be found in the studies conducted by the Tufts-Delta Health Center in rural Mississippi (63). However, the researchers in this program emphasize that poor housing and sanitation are only a part of the health problem. Social conditions involving family and neighbor relations, economic deprivations, and inadequate nutrition have significant effects on health status.

If we accept the premise that inadequate housing can have an adverse effect on health, then the primary issue becomes the effect of improved housing on the health status.

At the outset, we want to emphasize that simply by improving the physical structure and the design of a dwelling, we cannot expect health status to automatically improve. In some instances, when urban slum dwellers were relocated in better housing, health status actually declined (this was particularly true for elderly persons). In other studies in urban areas, there are no differences following improved housing or, if there are differences, they are either slight or transient (64). These results emphasize the necessity of defining the circumstances under which housing improvement efforts are initiated, including the health status of the person, the physical characteristics of the inadequate housing, and the type and location of the improved housing. To date, the only systematic analysis that includes each of these components was conducted in an urban area (65). This study conducted by Wilner, Walkley, Pinkerton, and Tayback separated physical health problems from social psychological adjustment in persons relocated from urban slums to high-rise and low-rise public housing. By studying the relocatees over a 10-year period, the research team identified several directional trends that confirmed the premise that improved housing affects health status. First, the incidence of morbidity in specific diseases declined among persons living in improved housing, especially children (66). Second, the psychological state of the persons relocated to improved housing improved; general morale was elevated and stress was diminished (67). Unfortunately, there presently exists no analysis of this sort that relates housing quality and health state in a rural context. Consequently, we cannot assess the effect of such stress-causing phenomena as urbanization, relocation, and changing social conditions in rural areas.

A review of existing literature on housing and health reveals three major distinctions that should be made in assessing the effect of improved housing quality on health status.

First, we should define the effects of each measure of housing quality (overcrowding, deteriorating structure, and inadequate waste disposal and water supply) on both physical and mental health status. Each of these housing quality deficiencies can be alleviated in several ways (e.g., additional space can reduce stress, installation of a toilet can improve sanitation, etc.) that would reduce the incidence of disease. Second, there should be a clear definition of the potential effects on health status that results from various types of housing improvement programs. Such improvement programs would include: (1) improvement of the existing dwelling, (2) relocation to improved housing in an area outside the original community, and (3) relocation to improved housing in the community. Third, housing quality is only one example of the array of factors that affect health status. The social processes that affect the family are particularly important. Housing quality improvements are needed, but such improvement programs should be deliberately used as opportunities to alter some of the aspects of the social environment.

The following sections are efforts to develop these three propositions. A conscious attempt has been made to relate these issues to the role Government could assume to improve the quality of the physical environment, especially in rural areas.

Population Density and Crowding

Overcrowding in the dwelling unit has been reported to contribute to the spread of infectious diseases and affect the response of individuals, as well as society, to many of life's stresses (68).

Secondary attack rates of tuberculosis have been found to be over 200 percent higher for people on relief living in overcrowded dwellings than for all economic status groups living in less crowded structures—one person or less per room (69). Studies have shown that overcrowding is associated with the frequency of disabling illness lasting a week or longer (70), the number of respiratory infections in infants, infectious childhood diseases (71), skin diseases, and the number of home accidents (72). Overcrowding interacts with home heating and ventilation to produce increases in morbidity and mortality in the young and the aged (73, 74).

Overcrowding also conditions personal and group behavior and mental health. Doubled-up families in multistory buildings tend to develop higher levels of emotional illness and hostility (75). In the 167 metropolitan areas in which rioting occurred during 1967, 24 percent of all dwellings occupied by nonwhites were overcrowded, as compared to 8.8 percent of the white occupied units (76). Obviously, overcrowding is not the single element that produces a "culture of poverty"; more likely, crowding heightens the effects of other deprivations, each reinforcing the other. All these forces tend to shape the personality of the slum dwellers.

Overcrowding affects privacy and often results in family members spending more time outside the home (77). When recreation is not available families have been observed to show aggravation of any predisposition to neurotic behavior (78). When overcrowding forces children to find activity space outside the home, children's study habits suffer and parental supervision and control is reduced (79, 80, 81). Weakened supervision and exposure of children to the life of the street may, in turn, contribute to the development of many of the social problems of youth assumed to be characteristic of high density slum communities around the world (82).

Cassel (83) argued that there is a considerable amount of confusion concerning the health consequences of crowding and the narrowness of migration theory. To support that conclusion, a brief review of morbidity rates would be appropriate. Death rates for all causes in the United States were higher in urban areas than in rural areas prior to 1950. By 1960, however, the ratio had reversed, and since 1960 the ratio of rural to urban deaths has been steadily increasing. Thus, although cities have been increasing in size since 1940, death rates have fallen more rapidly in these crowded circumstances than in the more sparsely populated rural areas. Part of this phenomenon may be due to the improved medical care and sanitation in the cities, leaving an older, more susceptible population behind in the rural areas. While the rural excess in both incidence and mortality rates from typhoid fever, for example, may well be due to differences in sanitation, and the more effective immunization programs in cities account for the lower urban rates of diphtheria and pertussis, the rural excess in the incidence of scarlet fever can hardly be due to either of these processes, as there are no adequate means to prevent the occurrence of streptococcal infections. Similarly, as far as the migration hypothesis is concerned, this could not explain the excess mortality rates in children, both black and white, male and female.

Even from the fragmentary illustrative cases, population density and/or crowding does not inevitably lead to poorer health status. Crowding under certain circumstances may be associated with certain factors which in themselves can influence health—such as poor housing—but the relation of crowding to disease situations may be a reflection of factors other than crowding, per se.

An important factor influencing health consequences is the human environment associated with housing. Holmes (84), in his studies on tuberculosis in Seattle, has shown that the disease occurs most frequently in "marginal" people; that is, those individuals deprived of meaningful social contact. He found higher rates of tuberculosis in those ethnic groups that were distinct minorities in the neighborhoods in which they lived, in people living alone in one room, in those who had multiple occupational and residential moves, and in those who were more often single or divorced than in the general population.

Cassel argues for the importance of the social environment under conditions of increasing population density and urbanization. The rapid urbanization of rural areas in the United States, particularly when it is associated with deterioration in housing, is usually accompanied by increased death and disease rates.

The situation or environment as a determinant of crowding is a factor described by Schmitt (85), who distinguishes between inside and outside density. Inside density refers to the number of people per unit of living space within a residence, whereas outside density refers to the number of people per unit of space as a larger environmental unit within which the inside density unit is embedded—for example, street, neighborhood, or census tract. Rural areas are often characterized by high population densities within a home but with few people immediately outside the home.

Altman (86) describes another aspect of the environment—the richness of environmental resources. Two homes with equivalent space and density can differ enormously in the way space is laid out, in the interior decor, and in the quality of facilities in general. An environment that is poor in resources might be more susceptible to the effects of crowding.

There are also interpersonal determinants of crowding. Much has been written about personal space, privacy, and territoriality. Central to these concepts is the idea that people establish boundaries around themselves to maintain their psychological integrity, protect their environment and space, and manage interactions with others. Control of interpersonal interaction is accomplished in a variety of ways, including manipulation of the physical environment, verbal and nonverbal communication, etc. Regarding the use of the environment, we open and close doors, arrange furniture in certain ways, establish seating patterns around tables, etc.

Where the cost of controlling interaction is high, where contact with other people is continuous, where environmental resources are limited, there can be a social and psychological breakdown.

The implications are that the popular conception of the negative effects of crowding seem largely an issue of too many people in too little space and consequently massive low cost housing programs are generated that are designed to provide more space per person or per family. Altman suggests that if environmental richness is also a factor, then more attention should be directed toward interior spatial planning and design.

Previous research on crowding has generally lacked a theoretical perspective (87). Moreover, there has been a tendency to view crowding in terms of spatial considerations alone as well as a failure to distinguish between physical condition (density) and the psychological experience (crowding). Personal and social variables do have a direct bearing on an individual's perception of spatial restriction as well as on his attempts to cope with this constraint.

Alterations in the Physical Environment that Affect Health Status

As mentioned earlier, sanitation (adequate waste disposal and clean water supply) has a significant effect on physical health status. It seems clear that any housing programs that provide basic water and sewer facilities will stimulate the improvement of physical health status. Furthermore, since rural families are in the greatest need of adequate water supply and waste disposal, a program to provide such services would have an important influence on health.

Although few people in this country die of direct exposure to the elements because of inadequate shelter, there are health problems associated with heat and cold. Heat and cold are especially critical problems for older people who live in inadequately insulated dwellings (88). Tolerance of older people to cold and heat has diminished and, as a consequence, their sickness rates have increased. Several other health problems can be related to physical deficiencies: lead poisoning from paint, accidents (falls, burns, etc.), and vermin. By improving the quality of the physical structure, these problems can be reduced significantly. It should be noted that improving the structure of a dwelling would probably have a less important effect on health status than would improving sanitation.

The Physical Environment and Mental Health Status

A relationship between mental health and inadequate sanitation and physical structure of the dwelling has not been completely developed. While both housing qualities may be interpreted as stressful, (89) crowding has a stronger influence on mental health. Crowding (living conditions that require people to interact with and relate to others in ways that are not desirable to them) can contribute substantially to accelerated intellectual and physical deterioration of older people, to increased aggression, to withdrawal and sexual abnormalities among young adolescents, and to the general poor mental health of adults. The disparity between the number of people in a dwelling, whether urban or rural, and the capacity of the dwelling to contain them and allow them to perform important human activities can be shown by a variety of physiological and psychological processes.

It is recognized that adequate physical layout of the dwelling cannot cure mental ills already in existence (such as schizophrenia), but that it may prevent their further development, in the sense that physical layout does act as a reinforcing agent to personality trends already structured. Neither can adequate physical layout of the dwelling produce (in the sense of originating them) new and desirable personality traits. But an adequately planned and structured physical layout can be an end or objective. As such, it should be flexible, to permit the flow of the process of adjustment and readjustment.

There are two factors of physical layout that may be considered in relation to crowding: 1) privacy in the dwelling as related to mental health, and 2) circulation in the dwelling as related to the mental hygiene of its occupants.

When discussing privacy we assume that freedom to be by one's self is a value; and that hindrances to its realization lead to frustrations, irritation, and resentments. Thus privacy becomes a value. Privacy is needed for thinking, reflection, reading, study, and for aesthetic enjoyment and contemplation. Intrusions on the fulfillment of personal desires need to be shut off in order to avoid the internal tensions that are built up from frustrations, resentments, and irritations of continual multiple contacts with others. Thus, the physical factor of circulation within the dwelling, although related to the factor of privacy in some obvious respects, also plays a part in the mental health of occupants.

Ease and freedom of circulation within the dwelling relieves cramped muscular conditions and attendant irritations. It facilitates the normal performance of family functions, an easy flow of sequences of overt behavior without interruptions to freedom of movement, or unwanted and unexpected intrusions on a train of thought.

Historically, government housing planners have viewed "housing" in terms of quantity of units. Emphasis has always been placed upon producing "units" to meet existing "needs" (90). Often housing needs are not "units" but clear water supply, additional bedrooms, or bathroom installations. Too often the only possible result of government housing efforts are new three-bedroom, single-family units or new two-bedroom apartments. Families are expected to conform their housing needs to the product the government produces, rather than the government's dealing with the people to determine what improvements are needed.

To assess local housing needs adequately, Government housing efforts must move closer to the people with housing problems. The quality of improvements must be given the same consideration as quantity. Programs must be designed to deliver the type of housing service that conforms to the individual lifestyle of the family.

The Effect of Housing Relocation on Health Status

One of the more important aspects of our environment that affects health is the presence of members of the same ethnic group, background, economic level, etc. (91). Numerous studies conducted in urban areas have revealed the detrimental effect on health that results when persons are relocated outside of their old neighborhoods (92). Too often improved housing is available only if a family is willing to leave the social environment with which it is familiar. Relocation means breaking social ties which underlie the mental well-being of the individuals in the family. Generally, mental health is related to the degree to which people feel they have control over their destiny. From a mental health point of view, unless people feel that they have some control of their envionment, the likelihood that improvement programs will positively affect health is remote.

People must be involved in the decisionmaking process. Historically, government housing programs have not adequately involved people in the two most important decisions: 1) location of the residence, and 2) design of the living space. The process of developing and implementing housing improvement programs must radically change to involve people at these two crucial points.

Housing as Factor Within a Total Service Delivery System

As mentioned earlier, housing problems are but one factor that affect the health status of people. To deal effectively with health problems, many social, economic, and physical factors must be considered simulatneously. Under the existing government system such an undertaking would be complex. The efforts of the Tufts-Delta Health Center to attack rural health problems by initiating housing, social, and economic programs have been complicated immeasurably by the morass of government fragmentation. Too often the goals of the government rural housing program conflicted with the economic development program objectives or the welfare program requirements.

If we expect to see the quality of life improve in the future, then an expanded view of the way services are delivered by government to the people must be constructed.

Evaluation

The architects and planners of our physical environment have seen their task, as if schooled in noblesse oblige, as that of designing environments within which other men should be content to live. Thier buildings and cities have evolved most often from idiosyncratic, intuitive fantasies in which spaces and forms are molded by aesthetic principles. Architects are encouraged to conceive individual buildings in terms of their visual qualities—almost as sculptures (93).

Buildings that meet sculptural criteria are good—and necessary—if the environment is not to become even uglier than it is.

But they are not good enough. Architects must learn to attend to human behavior and to design to human needs.

It is not clear that while our behavior can obviously modify the environment, the environment can also modify our behavior, at all temporal and physical scales, for individuals and for societies. This is a kind of feedback loop that in good circumstances is responsible for the evolution of the behavior of the species and its physical environment as well.

The loop can be interrupted at several points. If individuals are under stress or in a condition of poverty or illness, it will be much harder for them to change their environment because they will lack access to suitable political power and authority, to actual tools, money, and time.

Under just such conditions, lives are most vulnerable to being distorted by outside forces —the inconvenient arrangement of the city or house, the impoverished sensory and social sterility of public housing or hospital, the imposition of limited housing opportunities by political or economic forces.

If we are to live in full health in whole, life-supporting environments, we must radically reorient our goals. We must concern ourselves with the quality of life and the quality of life's settings.

Our architecture and city planning schools are as backward as our building industry. Architectural education has been directed toward producing famous idiosyncratic architects, and formal, monumental buildings. We must instead train architects to ask questions, solve problems, and study the results of their work. Evidence of this approach has begun to germinate throughout the United States.

Architects are responsible for guiding the evolution of our society by their control over the evolution and design of buildings that are the containers and shapers of our culture. There is no tradition in the practice of architecture in which architects are expected to evaluate publicly their own or other architects' work.

Only careful scrutiny of working buildings in use can produce an evolution in quality of building types. There has never been a necessary steady progression of design quality or appropriateness in our public projects—housing, hospitals, schools, or our private offices, factories, etc.

We must institute and sponsor, from the Federal level, innovations in architectural education that focus upon research and evaluation. We must require that all federally and State-sponsored construction be preceded by detailed analysis of program requirements for each building. Therein, design solutions should be related as hypothesis to the eventual behavior of the population to be housed.

Every building must also have a followup evaluation study performed by the architect or other capable analyst, which is directed toward identifying and solving malfunctions in the design as well as noting where the structure successfully supports the use and behavior of its inhabitants. The American Institute of Architects (AIA) has proposed to the House Banking Committee an argument for postconstruction evaluation of all federally assisted projects where evaluation funds would come from Federal allocations. Architects, then, need to be selected for their programing ability so that contracts can be awarded and monitored in two stages, programing and design.

Our environments are for the most part designed and built by a few for use by many. Rarely do people ever have the opportunity to influence significantly or even modify the form of their shelter. This practice guarantees that in the absence of evaluation procedures, whatever omissions or mistakes are made by the designer will be repeated and will become the burden of all to live with.

This magnification of error has for many years continued unquestioned and unchecked. Our contemporary urban crises, social and physical, are in part of the legacy of this practice.

Federally sponsored building or rebuilding projects should require a maximum of user participation and control in the design and later administration of all building efforts.

Such projects also should be required to distribute architectural contracts over as large a group of individual design firms as possible. These designers must be bound by contract to work with local potential or present users.

The more designers, the less monotony and the less multiplication of errors. Having more designers per large project also facilitates working in small groups with neighborhood groups or user committees.

The argument can always be made that changes in procedures, particularly professional practices, will consequently result in higher costs. Over the past 10 years newly formulated community design centers have attempted to function in more pluralistic methods. Scott Ferebee, Jr., president of the AIA, states, in a dedication address (94) that the profession must rededicate itself to the fundamental mission of improving the quality of the Nation's man-made environment in service to their users. Archibald Rogers, first vice president of the AIA, calls for experimentation with the design process (95): "How one puts a community together, socially as well as physically, is a design issue."

It is not yet evident that changing processes will effect increased costs as there are an increasing number of professionals who argue that the traditional process results in floundering, ambiguity in decisionmaking, and the architect's projection of his own values. The author's experience is that user involvement, particularly in housing projects, does not increase the costs but produces more satisfactory results from the users' viewpoint. There are clear signs that architectural education is changing towards the ends described herein. Each year during the Environmental Design Research Association (EDRA) (96) conferences, there is considerable student research in the area of housing satisfaction and housing need.

Toward Homeostasis

Housing today represents a producer-oriented and supply-dominated system. The supply structure includes within it industry and government procedures, "facilitating beneficiaries," such as FHA, FmHA, and the rich, in order to provide housing for the poor.

Direct subsidies go to commercial financing institutions, land developers, and construction companies; whole subsidized fees go to legal, architectural, and management firms.

The policy alternative requires a greater balance between supply and demand factors; a system oriented toward people, toward the development of human resources, and toward the development of service procedures that can be controlled by the people who need to be housed.

Direct subsidies to users in combination with a network of decentralized services could increase the autonomy of low income people without establishing complex regulatory mechanisms that affect the lives of the poor or the process by which housing for the poor is created.

For interest groups on the supply side, housing is an investment channel and a consumption product. For most people on the demand side, housing constitutes a basic human need for shelter, for privacy, and for a personalized place to raise a family and meet with friends.

The present government housing delivery system treats low income families as depersonalized and manipulated objects, often as no more than statistics. While lip service is often given to the need for user participation in the government housing process, the reality is that low income families have very little input into the location, planning, or design of new projects. Rather, the crucial decisions are made by professionals who often have very little knowledge of, or contact with, their client group. Earlier we noted the beneficial effect on mental health that results when persons feel they have control of their destiny. If government housing efforts are to be directed toward the improvement of the quality of life of low income families, it is essential that these families participate in those efforts. The government should urge policy requirements that will enable professionals to involve users meaningfully in the housing planning and design process.

The Extent of Housing Need

In discussing housing needs, particularly in rural areas of America, we are hampered by an agreed-upon definition as to what constitutes housing need, or even what constitutes decent housing. Definitions of "substandard" housing, which may be dilapidated or lack essential plumbing facilities, is an extremely narrow one. The Douglas Commission called this measure of quality "hopelessly inadequate" and pointed out that it leads to "a gross understatement of housing needs" (97).

It does not consider, for example, the adequacy of heat or of light and ventilation or of the amount of living space available—both in terms of numbers and size of rooms. It fails to take into account the cost of housing, though it can be argued that a household that shorts its food, clothing, and medical budgets in order to occupy a "standard" unit also exhibits a dimension of housing needs.

We are also hampered by the fact that we do not bother to collect any detailed information on housing except once a decade.

Relationship Between Man and His Residential Environment

Funds have not been available to determine how deficiencies in the residential environment affect physiological health, emotional stability, and well-being. As a result, decisions about environmental programs are sometimes ill-advised and result in effects that are the opposite of those that were intended. The effects of environmental deficiencies on populations such as the aged and rural and urban poverty groups are as little understood as is their effect on the typical middle-class family. Not only are the health effects of a single environmental stress inadequately understood, but the health significance of multiple stresses on one individual, a family, or a neighborhood is largely unknown. Yet, it is the accumulated stresses of noise, overcrowding, lack of basic sanitation, etc., that have created the current rural housing crisis.

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A Rationale for Government Intervention in Housing: Diversity in Community Building Codes Acts to Constrain the National Effectiveness of the Housing Technical Community

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Summary

In any review of the attitude of the technical community toward the structure and functioning of the current building regulation system, the salient thought that emerges is that the attention of the practicing architect and engineer is focused on his own local problems. Generally speaking, he is interested in national policy and activity only insofar as they affect his local problem. As his area of operation expands, he becomes more cognizant of the scope of the code problem, and becomes more concerned on a national basis.

Other members of the technical community, including academic and governmental employees, are likely to have a broader view.

The practitioner's first reaction to proposals for Federal Government intervention in the code system is strongly negative—he has had unfortunate experiences with governmental redtape and bureaucratic autocracy which cause him to be antagonistic to Federal control. Upon reflection he will agree that a single national code would be ideal in theory, but foresees all sorts of difficulties in practice. He is likely to support only those kinds of activities that he sees as offering some possibility of alleviating his difficulties at the local level. He is generally favorable to activities that will develop solutions to technical problems in the area of building technology and translate these studies to the operational phase of code administration. He considers his problems to be largely of a local nature; it is these problems that concern him most.

Attitudes of Building Professionals toward Building Regulation

Professionals who are required to deal with building codes and similar regulations are unanimous in support for more uniformity in such regulations. Any professional, whether architect, planner, or engineer, complains about the absurdity of today's situation wherein each jurisdiction in which he proposes to work has its own peculiarities of building regulation. However, the average professional is resigned to this situation because he has come to expect it as a way of life; generally he has worked out some accommodation with the system. Once professionals have adjusted to life as it is, they hesitate to embark upon any crusade that might endanger the working arrangements they have reached. Many, though espousing the cause of code uniformity, hesitate to enlist in the forces that are advocating such a policy for fear of upsetting the applecart and making enemies among those who have the power to stop or delay their work.

Mandatory code uniformity entails the centralization of code regulation at some level higher than the locality, and professionals recognize that any degree of centalization is running in the face of popular opinion which, at the moment, seems to be supporting local option and local control as a means of overcoming bureaucracy and redtape at higher political levels.

Code Uniformity

Why do professionals regard building code uniformity as desirable? The answer is obvious to any practitioner working in different areas, each of which has its own code jurisdiction. Every time a new jurisdiction is entered, it is necessary for the professional to become acquainted with a new set of regulations—regulations which will be a controlling factor in his design work. Needless to say, the process of becoming knowledgeable about a different code involves effort and time. The amount of time varies, of course, with the format of the code. If the new code is written in a familiar format, the process of developing familiarity with the code is accelerated, but even in these cases it is necessary to exercise considerable care to make certain that vital points are not overlooked. On the surface, a small matter such as a differing definition may appear to be minor, but in fact, a small difference can be of major significance. Changes in numbers—such as design loads, fire resistance requirements, sound transmission reduction requirements—can change the structural requirements and increase or decrease costs.

It might be assumed that through the efforts of the various model code groups a greater degree of code uniformity could be found in codes, particularly in view of the fact that many local jurisdictions profess to have adopted one of the model codes. The report of the Douglas Commission, however, makes it very clear that model codes are seldom adopted in their entirety and/or without modification. Thus the wise practitioner seldom accepts statements that indicate the local code is in exact conformance with the latest edition of the model code. Normally this requires some periodic legislative action which is often overlooked by the local body.

The Cost of Code Variations

Accordingly, the architect or engineer working in a new area must become acquainted with the local regulations. The cost and time that can be charged to this task is uncertain. Some individuals talk of "taking the code home over the weekend to become acquainted with it"; others talk about 1 to 3 days of intensive study at the beginning of a new project. But this is only the beginning. As any individual item comes up during the design process, the code has to be searched for pertinent regulations. This process is repeated time and again at a considerable cost in professional time. Although, as mentioned above, professionals are not able to place either a time or dollar cost on this part of the design process, they are unanimous in their agreement that it is costly to get acquainted with a new code, and that this expense contributes nothing to the betterment of the health, safety, and welfare of the public.

Other Code Problems

Although architects and engineers credit the movement toward code uniformity as a movement in the right direction, they are quick to point out that a single building code is only one part of the answer to more effective building regulation; equally important are three other factors: (1) the elimination of the building regulations which emanate from governmental bodies other than the building departments of cities and counties, (2) the establishment of a system and procedure that will assure uniform interpretation of code provisions, and (3) a rational system for evaluation of new products and techniques.

Multiple Layers of Building Regulations

More often than not designers are plagued with multiple codes or regulations in a given area. For example, where public buildings are concerned, the local or State fire marshal usually has considerable power to impose additional requirements which the designer must meet if the building is to be built. In school buildings the state board of education may have its own set of rules; some regulations for the building of hospitals, nursing homes, sheltered care centers, and the like, are promulgated by the State board of health; frequently this same board has control of individual sewage disposal systems. More recently some of the regulations issued in the area of environmental pollution controls have impinged on building activities. This is particularly true in the case of regulation of emissions from power plants and similar installations. As conservation of energy becomes a more critical issue, we can anticipate new building requirements that will exercise control over insulation requirements, thermal comfort levels, lighting levels, and glass areas, and establish limitations on allowable heat losses.

This enumeration of certain added building regulation is by no means a complete list; only some of the more common extras have been noted.

Federal Regulations

Any discussion of "extra" regulations that must be faced by architects and engineers would be incomplete without mention of those imposed by agencies of the Federal Government on projects in which the buildings are to be owned or used by the Federal Government or to be financed in some degree by the Government. As examples of this type of regulation one may cite the Minimum Property Standards of the Federal Housing Administration and the regulations relating to the construction of hospitals growing out of the Hill-Burton act.

Some of these de facto building regulations go beyond the avowed purpose of building codes, that is, of "protecting the health, safety, and public welfare" unless a rather liberal interpretation of the term "public welfare" is accepted. For example, the regulations of the Federal Housing Administration have two purposes beyond the "health and safety" aspect. As an institution that is concerned with maintaining a healthy condition for lenders in the mortgage market, the FHA must be concerned with the quality of the product upon which loans are to be made. Accordingly, FHA must adopt a conservative approach and must assume that any owner can default, thereby leaving the property to the FHA. This being the case, the property must have a reasonable value on the resale market. Thus FHA regulations are aimed at protecting the value of property in order that the financing process can be stablized.

In another aspect of its responsibility, the FHA is charged with improving the housing of the nation—in this regard, history reveals that housing standards as exemplified by the FHA Minimum Property Standards have moved upward over the life of FHA. Most of the improvements will have to be charged to bettering the "general welfare" of the public—items such as expanded and more specific storage requirements fall in this category.

The term "public welfare" is now being interpreted in yet another way. Originally, codes were concerned mainly with the welfare of the occupant of the building; now the term is being expanded to include consideration of the public at large—regulations concerning energy consumption are a case in point.

Local Interpretation of Building Codes

Despite the problem of varying building codes in different jurisdictions, and despite the problems of multiple and overlapping regulation in any one geographical area, the professional is faced with a still more serious impediment to the building process—local interpretation of building regulations.

By their very nature, certain parts of building codes are imprecise in their content. Therefore, proper interpretation of the intent and meaning of the code is an essential part of a successful administration of the code. The ultimate functioning of any building code system devolves to the effectiveness and fairness with which the code is interpreted. It is obvious that the final result can range over a wide degree of satisfaction and dissatisfaction.

Local control of code interpretation can be troublesome for the design professional in more than one way. The designer may find himself faced with a ruling which he feels is not consistent with the code, or he may have the problem of excessive delay on the part of the code official in reaching any decision. Sometimes these actions may be taken because the code official has a very personal view about the way the code is to be interpreted—he has come to regard himself as the community's guardian in matters of building control and chooses to make his rulings in light of his own personal beliefs rather than in accordance with the law.

Sometimes rulings may reflect a desire to protect local enterprise and to "keep foreign enterprise out." Or perhaps the code official feels it is his duty to "upgrade" the new buildings built in his jurisdiction. Occasionally delay may be caused by the lack of knowledge on the part of the code official—he finds himself without the necessary knowledge to make the proper decision and is hesitant to reveal his shortcomings by seeking help and advice.

At other times, conflicts may arise because of the nature of the individual making the rulings —he may be the type who likes to "throw his weight around" or he may be unable to divorce his personal animosities from his technical decisions.

It is apparent that in all these cases the personalities of the people involved play a large part in the functioning of the process. Code interpretation must be done in an atmosphere of reasonable discourse—each side must make an effort to understand the opposite point of view.

Unfortunately, in many communities the professional finds himself dealing with an inspector or building official who has not had formal training equivalent to that of the professional with whom he must work. The building official may be a competent tradesman of long experience, but his experience may not lend itself to the process of evaluation and interpretation of building regulations—he may be more inclined to judge all buildings in the light of past experience rather than with regard to the written regulations. To be blunt, lack of knowledge of new materials and new techniques can create a problem, and this problem can become a major obstacle when it is compounded by certain types of personalities. Unfortunately, some building officials in this position adopt a very defensive attitude toward their rulings and it becomes difficult to consider differences on a rational basis. Needless to say, these personality conflicts do not occur on only one side of the table—some professionals by their own nature are completely unsuited to carrying out negotiations with building officials.

When conflicting personalities clash, rational, logical, impartial code interpretation is likely to fall by the wayside.

When the local code is subject to interpretation by the local building official, and when there is no recourse to a higher authority, serious problems can arise. Honest differences about the interpretation can result in a serious impasse. Of course the owner (or his representative, the designer) does have recourse to the courts, but this is a time-consuming and costly process and is seldom suitable when a quick decision is required. Furthermore, the professional is not in a good position to contest unfavorable decisions because he (the designer) knows that in the future he will undoubtedly need further approvals from the same office. Thus it is often more expedient to accept a ruling involving a relatively minor change than to fight the decision and endanger the future development of the project.

It is clear that the design professions not only seek greater uniformity in codes, but they are also greatly desirous of developing a code system that will engender more uniformity in the interpretation of the code.

Education for Code Interpretation

The enumeration of the various aspects of code interpretation serves to point out the importance of this problem in the view of the professional community. Professionals are also in agreement that a properly designed educational program could go a long way in helping to alleviate code interpretation problems. Some of the organizations of code officials and a few universities have made a start toward the development of educational programs for the code administrator. These have proven to be extremely useful, but they have largely been unable to approach the problem of interpretation of the technical parts of codes because of the lack of uniformity of the codes under consideration. It is practically impossible to teach a subject in which there are as many textbooks as students. It is clear that the need for educational programs in the area of understanding the technical provisions of codes forms a substantial reason for the advocacy of code uniformity.

Codes and New Construction Techniques and Materials

Nearly all codes contain some provisions for the acceptance of nonstandard materials and construction techniques. The processing of requests for approval of such code deviations at the local level has been slow and largely unsatisfactory. It is in this area that the local official is most severely handicapped. He is called upon to make judgments of products and systems primarily on the basis of presentations prepared by the proponents of the new, although in some instances he may have proponents for the status quo as well. He is called upon to assess the validity of the various claims and the supporting test data and to distinguish between fact and propaganda. Oftentimes he must listen to pleas of "vital to progress" and cries of "destruction of a segment of the industry." The nature of this process is such that the code official may find himself in a most peculiar position. When the only documentation received is on the part of the proponent, he finds himself acting as the advocate for the opposition as well as being the judge of the case. Under these circumstances his impartiality and objectivity are bound to be questioned.

The building official, particularly the official in the small community, finds himself ill-prepared organizationally (and perhaps personally) to cope with this situation. He needs help.

He needs some type of mechanism to assist him in these judgments. Appeal boards are often not adequate in this regard—the building official needs aid in the form of competent technical assessment. Smaller communities usually are neither organized nor financially capable of obtaining the necessary help.

The national code organizations offer some assistance in this area by providing procedures for the evaluation of new materials, etc.—most of these requests, however, are initiated by the proponents of the new material or system.

Some States that are operating statewide codes have set up State agencies which can assist in this process. Two types of assistance are possible: The State agency may make the decision, or it may only provide technical assessment of the point in question, leaving the decision to the appropriate appeal board or code official.

In at least two States the engineering colleges of the State have been incorporated into the evaluation process related to the acceptance of new materials, products, and systems for building.

Approaches to the Improvement of Building Regulation

A number of efforts are underway with the purpose of eliminating the constraints on the building regulation system currently extant in the United States. These include the advocacy and development of State codes and the advocacy and experimentation with codes that are largely performance-oriented. The opinion regarding the usefulness of these movements is not nearly as solidified as is opinion regarding the fundamental problems.

State Codes

The demand for uniformity in codes has resulted in a number of States withdrawing building code control from local jurisdictions and establishing some form of a statewide preemptive building code. It appears that much of the impetus for the introduction of statewide codes has come from the desire of the State to limit local control in order to accommodate the introduction of industrialized housing. For this reason a number of codes have been limited to the field of industrialized housing; others have been for housing in general; still others have been for building other than housing.

Response to this movement has been varied. The majority of professionals agree that it is a step in the right direction, but point out that it is just that—a step. One professional concerned with code regulation in relation to industrialized housing opined that the State codes had largely been ineffective in reducing red tape—that in many instances it appeared that State codes have only served to add one more layer to the approval route. It is apparent that much more experience is required before the suitability of the State code system can be fully evaluated.

It should also be mentioned that a State code does not automatically solve the problems of multiple codes jurisdictions or of code interpretation.

Even if the most favorable results with respect to administration are forthcoming, it must be realized that it is conceivable that each of the 50 States could have a different code with the result that interstate reciprocity would not be greatly improved.

However, despite the fact that professionals credit the State code with being only a step in the right direction, they do see in the State code the opportunity for making progress.

For example, with a single code to interpret and enforce, the opportunity exists for organizing effective informational and educational programs among code administrators. When the State is regulated by a single code, the education of the code administrator and building officials can move into the area of technical interpretation of the clauses of the code. Under a continuing education program of this nature, the possibilities of uniform code interpretation are greatly enhanced. Misinterpretation of code clauses due to misunderstanding of code provisions can be largely eliminated and pet prejudices of code officials may be forced out into the open.

The State code also offers the opportunity for the devising of a system of appeals which would permit the designer to approach a higher authority if he feels he has been unduly restricted by a local ruling. Such a system may serve to ameliorate many of the conflicts which occur between personalities. Under a State system the board of appeals could have access to an impartial technical authority—as mentioned before, at least in two instances States have vested this responsibility in engineering colleges of the State universities—which would be charged with preparing technical "briefs" needed by the appeals board.

The technical community also sees the State code authority as a means of developing a mechanism whereby building booms in any given area could be accommodated.

Once a cadre of competent code officials has been developed, it would be possible to put into operation an exchange program for building officials. Through such a program it would be possible to augment the staff of the building department laboring under an overload with officials from neighboring areas where the pressure was less severe. In this manner the pace of plan evaluation and building inspection could be adjusted to the community's need.

State code authorities also offer the opportunity for administering building controls in communities that are too small or have too little building activity to maintain a fulltime building regulatory activity. The administrative procedures and staff of the State authority should be organized in such a manner that such services can be furnished to the communities that require them. Through proper organization, a maximum degree of local control commensurate with the needs of the community can be exercised. Such an arrangement will facilitate the imposition of statewide controls.

One of the chief functions of the National Conference of States on Building Codes and Standards (NCSBCS) has been to foster State code activity. Indications are that at this time over a score of States have adopted some form of State code. It must be recognized that the success of this activity depends upon the voluntary action of the legislatures of the individual States. However much progress is being made in the adoption of State codes, it is apparent that this program is doing little to increase interstate uniformity.

A Single National Code

Generally speaking, the technical community is unable to separate the subject of a single national code from the idea of Federal dictation and control. When they are able to divorce the subjects, most professionals concerned with the designing of buildings on a multi-State scale will agree that the ideal situation would be one in which a single code would be in effect throughout the nation. However, while agreeing that this situation would approach the ideal, they are also very careful to state the limitations which they feel must apply to any such approach.

Conditions for Acceptance of a National Code

Assuming for the moment that it would be legally possible to achieve a single code for the Nation, it is necessary to outline the conditions which would make such a code acceptable to the technical community. In the first place, it would be vitally necessary to develop a system that would guarantee that the national code would not become a roadblock in the way of the inevitable changes which will occur in building technology. Single monolithic authorities without competitors are inclined to be slow of change—in fact, to be slow in all activities. Safeguards to prevent this stagnation must be built into the system.

The technical community is very concerned about who would "write" such a code. They are very chary of any regulation which might come forth from a Federal bureau as an edict. They have long felt that their expertise in the building field has not been properly employed in the development of building codes. Because—next to the public at large—members of the design professions are the persons most affected by building regulation, it seems logical that their input should be exploited more fully. Along with concern for their own interests, they are insistent that all facets of the building industry be considered.

To be of the most service to the Nation in regulating the building industry, the technical community visualizes the code as having a hybrid nature. The code should be founded in the performance concept as such an approach attacks the building problem in the most rational way. At the same time, the code could not be considered complete without a prescriptive section for the most common materials, structural systems, and building types. For most routine building, particularly in the residential field, the prescriptive code would be the basic working document. For those cases which did not fall into this category, the performance code section would establish a procedure and a basic set of criteria for evaluation. Also, before giving wholehearted support to the idea of a national code, the technical community wants to be assured that the mechanism by which the code will be administered will meet its needs for rapid and flexible response. Basically, the administrative system should have the possibility of local response combined with the right of appeal to higher echelons. Such a system should also permit the possibility of a central approval being accepted for multiple areas within the United States, providing, of course, that special local conditions have been considered in the evaluation process.

Constraints to the Development of a National Code

Concern sometimes has been expressed that a single code (either at the State level or the national level) could not encompass local needs. The differing requirements for wind loads, snow loads, earthquake hazards, foundation conditions, etc., are cited. These issues should provide no obstacle to a single code. Such problems have not affected the effectiveness of the model codes—the areas of different requirements are easily delineated by a series of maps or other devices.

There are a number of political and social considerations that will arise in any move toward a national code. Among these is the existence of the general antipathy toward Federal bureaucracy and Federal control. This feeling of the design professionals has been alluded to previously. Other elements of the technical community will also have to be reassured in this regard. Also, the opinion of the general public is not to be considered lightly. A carefully prepared and continuously presented informational program designed to meet the requirements of all segments of the building industry and the general populace will be essential to the success of the project. This is particularly true in view of the current trend toward a more active consumerism, along with the expressed Federal policy of returning more power to the States. The mere suggestion of a preemptive Federal code is bound to raise the hackles of the "States' righters" just as State code stirs the ire of those that favor local option. There is growing professional opinion, however, which considers that the time has come when the larger concept of the general improvement of the efficiency of the building industry must take precedence over historic political concepts which are not suitable to our times.

A major societal problem which enters into the picture is that of finding a method of utilizing the code systems that have been developed in the United States. Historically, the model code organizations have depended rather heavily upon the "sale" of their product—a code—to code jurisdictions. Recently there has been a greater emphasis on the services that code organizations can render to their members. In some instances these services have been expanded to inspection activities, quality control measures, and certification.

Educational programs for code officials have taken on new importance. Evaluation of nonstandard constructions and materials are available as a service to members and to industry. Many of these activities could be continued and expanded. Hopefully, the revenue from such activities and services would be augmented sufficiently to support the continued viability of the major code organizations.

After a time, a merger of these groups might be feasible. The combined code for one- and two-family dwellings developed by four model code groups is evidence that such cooperative work is possible. The fact remains, however, that the place of the code officials' organization in the new code system must be considered carefully; if this problem is ignored, heavy opposition can be expected from this quarter.

It also seems that it will be necessary to assure the local building official that he is an essential part of the proposed system and that he will remain an employee of the local government (or at most he should become an employee of the State, but be locally based). Undoubtedly some upgrading of building officials will be necessary, and this will become a part of the program; it should be recognized, however, that a great majority of plan examination and building inspection activity at the community level can be done in a manner little different than is the present practice. A system which would furnish an evaluation service for the out-of-the-ordinary case would relieve the local code official of this problem. He would be able to obtain the services upon request.

Federal Intervention in Code Matters

Should the Federal Government intervene in building code matters? This question is moot—Federal intervention is already a fact. The question of further intervention is debatable, however. Any assessment of the professional attitude toward the promulgation of a Federal building code would undoubtedly result in an "unfavorable" answer. Even though professionals support the idea of a single code, they are willing to do this only after stipulating that such a code should not be dictated by the Federal Government.

To assess the feeling of the technical community with regard to Federal dictation in code matters, one need only recall the rebellion when a partial attempt to change the status of the "Guide Criteria" for Operation Breakthrough was attempted.

In view of the current attitude toward Federal intervention, it seems that the only possible route for such activity will be through some of the mechanisms already existing. At the moment, Federal control over building activities can only be exerted in an indirect manner. This can be effective when the Federal Government has a substantial part in the financing of the building activity. This enforcement can be rather benign, as in the case of the application of the Minimum Property Standards of the FHA, or it may be more forceful as exemplified by the withdrawal of support for activities in San Francisco because of the use of an outdated regulation in that city's plumbing code. Perhaps these measures could be augmented to some degree by some ploy on the regulations of interstate commerce, although just how this might be useful is not clear at the moment. The withholding of the revenue sharing funds might be successful, but it is doubtful if such an approach would be politically expedient at the present time, since the local governments are even now objecting to some conditions tied to the use of these funds.

The other method open to the Federal Government is persuasion. The activities of the National Conference of States on Building Codes and Standards is an attempt of this nature. The conference has been promoting the use of State codes; apparently it is making some moves toward the preparation or adoption of a model code which may be recommended to their members. To date, this approach has resulted in a number of States moving to State codes, but the movement has not been as rapid as desired, nor has the program resulted in the desired degree of reciprocity among the States. In the final analysis the State legislators are the individuals who have the say, and they generally are inclined to resist anything that smacks of expanded Federal control.

Faced with this problem and considering its great fear of monolithic control, the attitude of the technical community seems to be one of compromise. It seems to be saying, "Let's find a way to have all States and localities adopt one of the model codes without change." This procedure is regarded by the professions as offering an acceptable degree of code uniformity without incurring the dangers they see in Federal control of a single national code. They are inclined to think that some degree of competition among the various model codes is healthy and is of benefit to the building industry.

Growing out of past experience and current attitudes is the conviction that no effort toward Federal intervention in the code picture is likely to be successful unless all parts of the building industry are participants in the process. Professionals do not purport to have all of the knowledge in this area, but they will not accept the proposition that codes are to be written only by code officials. They are equally insistent that other governmental agencies cannot appropriately promulgate codes without help from the professions and from industry.

At the same time it appears that the attitude of the professionals would give support to more activities of a fact-finding nature upon which code regulations and rulings could be based. It is in this area of "assisting the industry" that the Federal effort can be most useful and successful. One logical area of Federal activity lies in the support of further study of the performance concept. Once again, however, acceptance of this work will only come about through the participation of all facets of the building industry during the study process.

It is also apparent that some means must be found whereby unification of codes can be accomplished by the Federal Government, while the control of code administration remains in the hands of the States. Whether or not such can be accomplished remains a question.

3 Market Barriers

Land Use Controls as a Barrier to Housing Assistance

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Introduction

The purpose of this paper is to analyze the relationship between Federal housing policies and programs and local land use and related controls and to suggest ways in which certain Federal initiatives may be taken to enhance the housing opportunities of lower income persons in metropolitan areas.[1]

Any Department of Housing and Urban Development (HUD) housing program to aid lower income households will disproportionately aid minorities because they are represented in the lower income strata in numbers greater than their ratio to the majority population. For example, in the existing FHA programs alone, unassisted sections 202 and 207 housing is 95.5 percent and 87.7 percent occupied by white households while low rent public housing for families is occupied only 50 percent by whites.[2]

Federal court decisions have forced HUD, through project site selection criteria, to avoid subsidizing housing on sites that have the purpose or the effect of reinforcing racial concentrations.[3] Minority groups have also sought the opportunity provided under sections 235 and 236 housing programs to overcome local land use and related controls to reside in nonghetto areas, and in this respect they have found support in decisions of Federal courts.[4]

The body of law created by these decisions would be applicable with greater force to any program under which State or local governments subsidized the construction of housing. As the President has observed, local officials "operate under the same antidiscrimination strictures that apply to Federal officials." [5] The public official at any level of government who selects or approves sites for lower income housing operates under the constitutional ground rules of the equal protection clause.

Where racial discrimination is not the motivation or the effect of site approval or selection, somewhat different rules apply. These rules need not be discussed at length at this point other than to observe that some State courts have begun to question whether localities can ignore regional or statewide needs for housing—particularly housing for lower income households—in the application of land use and related controls.[6] The policy issue here is an amalgam of legal, urban planning, housing market, and civil rights questions.

An assumption, which we believe needs no proof, is that any subsidy for new construction that limits the occupancy of what is produced to households of a certain income (even if the income is close to the median for the metropolitan area) will classify such housing in the public mind as "subsidized." To the even less knowledgeable public, it will be perceived as "public" housing even if privately owned and managed. This perception brings in its wake all of the political and public relations problems concerning local acceptance of such housing. Housing whose construction is in some way stimulated

* This paper was submitted to HUD on June 20, 1973.

[1] The submission of this paper by the Potomac Institute does not imply an endorsement of the Department's termination of housing programs authorized by existing legislation during the period of the policy evaluation.

[2] Compare Table 130 with Table 105, 1971 HUD Statistical Yearbook.

[3] *Gautreaux* v. *Romney*, 332 F. Supp. 366 (N.D. Ill. 1971), 448 F. 2d 731 (7th Cir. 1971); *Shannon* v. *HUD*, 436 F. 2d 809 (3rd Cir. 1971).

[4] *Parkview Heights Corp.* v. *City of Black Jack, Mo.*, 467 F. 2d 1208 (8th Cir. 1972); *Kennedy Park Homes Assn.* v. *City of Lackawanna, New York*, 436 F. 2d 108 (2d Cir. 1970); *Southern Alameda Span. Sp. Org.* v. *City of Union City, Calif.*, 424 F. 2d 291 (9th Cir. 1970); *Dailey* v. *City of Lawton, Okla.*, 415 F. 2d 1037 (10th Cir. 1970).

[5] Statement by the President on Federal Policies Relative to Equal Housing Opportunity (June 11, 1971). Pres. Docs., June 14, 1971, at 892.

[6] *National Land and Invest. Co.* v. *Easttown Twp. Board of Adjust.*, 419 P. 504, 215 A. 2d 597 (1965); *In re: Appeal of Kit-Mar Builders*, 439 Pa. 466, 268 A. 2d 765 (1970); *In re: Appeal of Girsh*, 437 Pa. 237, 263 A. 2d 395 (1970); *Bd. of County Supervisors* v. *Carper*, 200 Va. 653, 107 S.E. 2d 390 (Va. 1959). These issues are currently raised before the New Jersey Supreme Court in the appeals involving *Southern Burlington County NAACP* v. *Township of Mount Laurel*, 119 N.J. Super. 164 (Sup. Ct. 1972) and *Oakwood at Madison* v. *Township of Madison*, 117 N.J. Super. 11 (Sup. Ct. 1971). For a useful collection of State and Federal citations see Bellman and Baker, "Summary of Recent Court Challenges to Exclusionary Land-Use Practices" (National Committee Against Discrimination in Housing, September 1972).

but that may be occupied by households paying market rents or prices is less likely to be the object of hostile treatment by host communities.

Established national housing policy clearly does not contemplate the Federal reinforcement of economic stratification of metropolitan areas. Generally stated, that policy calls upon Federal officials to weigh the need for economically integrated communities against the legitimate objectives and values inherent in local self-government. It is assumed in this paper that HUD, in evaluating existing programs and suggesting new or revised programs, intends to assume some responsibility for assuring that local communities respect more than a narrow concern for their immediate fiscal and social integrity in their local housing and land use policies.

This has become a matter of increasing concern because of the "antigrowth ethic" that has developed, particularly in localities that control the vacant land on which most of the Nation's future residential development will have to occur.[7] This new mood often strengthens a preexisting hostility to housing for lower income people, extending that hostility to housing of all kinds.

In these circumstances, HUD's primary role should be to intervene, in effective ways, to achieve greater residential mobility for lower income households than would be possible if the housing market—highly regulated by State and local government in regard to location—were left to function in traditional ways. The status quo produces a dysfunction between residential location and jobs, a costly and exclusionary system of low density sprawl, and a reinforcement of racial and economic segregation in metropolitan areas. In addition, the rapidly rising inflation in the initial and occupancy cost of new and used housing in suburban areas means that most American families are being priced out of all new housing except mobile homes.[8]

One significant intervention involves the construction of subsidized controlled occupancy housing in newly urbanizing areas, although not necessarily on a project-by-project basis as under the existing programs. There simply is no other way, in view of escalating costs of new housing,[9] to assure that the huge metropolitan housing developments required for the foreseeable future will serve more than the upper half (or less) of the housing market.

The negative spatial impact of this pattern of development needs no extended comment. We accept and endorse the report of HUD's Land Use Subcommittee that "considerations related to a national urban and/or land development policy should focus primarily on the differential growth patterns (and their implications) now occurring between central city and suburban areas."[10]

Land use controls do not produce housing. Land use controls constrain and guide development. Communities that are not under economic, political, or legal pressure to provide sites for lower income housing tend not to plan or zone to accommodate it. The recommendations in this report, particularly in the third part, are based on this reality. In the present state of land use planning and zoning in the United States, and for the foreseeable future, the regulation of land uses will remain largely ad hoc and, in many metropolitan areas, increasingly unreceptive to housing.

It is possible that no single public program alone may significantly alter this pattern. If true, this nevertheless is no reason for not pursuing policies that in concert could moderate metropolitan demographic disparities. This is a major legitimate concern for public policy since it is public policy that establishes the character and sequence of urban development.

A number of possible initiatives are indicated in this report. They are organized into four sections:

I. Relevant State initiatives.

II. Relevant local initiatives.

III. Federal initiatives—HUD as lead agency.

IV. Possible initiatives of other Federal agencies.

Each subsection concludes with a recommendation addressed to the Secretary.

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[7] The emergence of this "antigrowth ethic" is described in Task Force on Land Use and Urban Growth, Citizens' Advisory Committee on Environmental Quality, *The Use of Land: A Citizen's Policy Guide to Urban Growth* (T. Y. Crowell Co., 1973).

[8] "The fact that the median price of new conventionally built housing approaches $30,000, and the minimal rental for new apartments is rarely below $175 per month, suggests that one need not be a trained housing economist to know that new housing is 'off limits' to the majority of American households." Report of the Land Use Subcommittee of the Advisory Committee to the Department of Housing and Urban Development. *Urban Growth and Land Development: The Land Conversion Process.* (National Academy of Sciences, National Academy of Engineering, Washington, D.C. 1972).

[9] The cost of housing in the past two decades has increased over 91 percent, second only to the cost of services, according to the Bureau of Labor Statistics. See *N.Y. Times,* June 11, 1973, p. 1, col. 6.

[10] Op. cit., n. 8 at p. 10.

Relevant State Initiatives

In the absence of Federal incentives, the States themselves have developed two major approaches to providing a more equitable pattern of urban growth. These include, on one hand, the establishment of a State urban development corporation in New York with powers to preempt local building and zoning regulations if necessary; and, on the other hand, a comprehensive special housing permit law in Massachusetts that allows the developer of proposed subsidized housing to appeal to the Commonwealth in the event of local disapproval of his project; and the passage in Florida of a State land and water management act that, among other objectives, permits State approval of developments of "regional impact." All of these initiatives contemplate a supervening role for State government in local land use decisions.

These initiatives should be contrasted with the regional tax-sharing law enacted by Minnesota, a different and as yet untested modulator of local exclusion of housing.

These two major approaches, State supervision of certain land use decisions and tax sharing, are most relevant to any Federal concern with equitable housing policies.

This section also discusses State initiatives that should be induced by the Federal Government: the creation of regional or metropolitan growth management institutions. In the absence of such institutions capable of requiring localities to assimilate needed urban development on a sound basis, the "antigrowth" ethic will seriously affect national housing objectives.

New York Preemptive Powers

The creation of the New York Urban Development Corporation (UDC) in 1968 [11] seemed to promise a new method of assuring a better distribution of lower income housing. Its power to preempt local zoning and building codes was widely believed to provide a model for responsible State action. The New York UDC claims to have become the largest single user of section 236 funds.

Because of the high visibility of the UDC, recent New York State legislation to limit sharply its power to operate in suburban areas takes on national significance.

[11] A general background on the New York Urban Development Corp. and its powers may be found in W. Reilly and S. Schulman, "The State Urban Development Corporation: New York's Innovation," 1 *Urban Lawyer* 129 (1969).

The recent law, passed by a 2-vote margin in each house of the New York legislature, would permit any town or incorporated village to veto UDC residential projects even though such proposed projects complied with preexisting local zoning and building regulations. With respect to towns and villages, accordingly, the New York statute goes beyond a mere repeal of the preemptive power over zoning and building codes. In this regard, UDC is now left subject to potentially greater constraints than private developer of subsidized developments under current Federal law. Such developers, of course, cannot wipe away local zoning and building codes, but they are not subject to such a veto when complying with local codes.

The operative provision of the new law, which the Governor has announced his intention of approving, is:

> Notwithstanding any inconsistent provision of this act or of any general or special law, no plan for a proposed residential project in a town or incorporated village which has not been affirmed by the corporation prior to May first, nineteen hundred seventy-three, shall be affirmed if, within thirty days after the public hearing held pursuant to subdivision two of section sixteen of this act or within thirty days after June first, nineteen hundred seventy-three, whichever date is later, the local governing body of such town or village submits in writing to the corporation formal objections to the proposed residential project, unless and until such objections are withdrawn . . . .[12]

The law does not define the term "formal objections," nor does it require that any reasons for such objections be given.

Many towns and villages in New York are quite large, and they rarely are the older core urban areas. The law also adds $500 million to the UDC bonding authority. To that extent it represents a "tradeoff" that will enable a continuing level of activity in core cities unaffected by the foregoing limitation.

The UDC proposal to provide a "fair share" of subsidized housing—actually only 100 units in each of nine towns—in Westchester County is widely believed to have precipitated the new legislation and the Governor's support of it. This was the first instance in which the corporation had announced its intention to preempt local regulations without the prior agreement, tacit or otherwise, of the local government bodies. The preemptive power, it is commonly believed, has seldom been exercised; actually it has frequently been exercised with local governing body con-

[12] §3, Assembly Bill R.R. No. 187, 7323-B (1973-74 Reg. Sess.), amending §15 of Ch. 174, Laws 1968.

sent to enable more efficient or innovative developments.[13] Presumably this will still be the case where a local veto has not been exercised. In other words, the usefulness of the preemptive power continues as a technical matter but not as a political matter. It is no longer available to strengthen the corporation's bargaining position with suburban communities, which heretofore may have "consented" to UDC activity to maintain their own bargaining position. It therefore remains to be seen how many localities that have the new veto power will choose not to exercise it or, probably more important, how many towns and villages UDC will even attempt to deal with.

A 5-hour debate in the assembly and a 2-hour debate in the senate featured, according to one source who was present, considerable reference to the racial exclusion expected to result from enactment.[14] If it could be shown that such exclusion was the motivation or the known effect of such an enactment, a question arises as to whether this legislation has any force or effect.[15] Without an examination of the transcript of debate, no definitive answer can be suggested.

Nevertheless, the prominence of UDC, the fact that it has become the chosen vehicle for substantial Federal subsidies, and the increasing role of State action in the housing and land use area, all indicate that serious consideration should be given to the use of Federal influence to evaluate and possibly challenge such legislation. If racial exclusion were involved, the question would be presented as to whether the Federal Government can supply funds to an entity whose operations are restricted in accordance with a State policy intended to, or inevitably having the effect of, limiting the residential mobility of minorities. In this connection, it should be noted that the U.S. Department of Justice has recently moved against Parma, Ohio, which passed legislation neutral on its face but allegedly motivated by a desire to exclude subsidized housing.[16] UDC's situation may be analagous because of the chilling effect of the new law on proposed developments outside core cities.

[13] Statement by Stephen Lefkowitz to Exclusionary Landuse Clearinghouse (National Urban Coalition), December 10, 1970, pp. 2–3.

[14] Telephone interview May 30, 1973 with Richard Callanan of the New York Urban Development Corp.

[15] See *Reitman* v. *Mulkey*, 387 U.S. 369 (1967); *Hunter* v. *Erickson*, 393 U.S. 385 (1969).

[16] Civil Action No. C–73–439, N.D. Ohio, April 27, 1973. In November 1971, the voters of Parma passed an initiative measure requiring a majority referendum before city approval of any subsidized housing project.

We raise this question without answering it. But it is a question that cannot be ignored, regardless of the form of Federal housing subsidies that may be involved.

Recommendation #1: The Secretary, in conjunction with the Justice Department, should evaluate the "local veto" provisions of the New York law to determine if the intent or the effect of such law is racially discriminatory; if this conclusion is reached, the Attorney General should be requested to seek injunctive relief to set it aside.

Recommendation #2: HUD should support Federal legislation to provide special Federal financial assistance for State or metropolitan development corporations with preemptive powers equivalent to those available before May 1973 to the New York Urban Development Corporation.

Massachusetts Zoning Appeals Act

A different approach has been taken by Massachusetts in the 1969 enactment of its zoning appeals law.[17] This law established a novel permit process that leaves local land use and building codes unchanged. It circumvents these regulations to promote specified types of housing required to benefit the State and the region. Unlike New York, periodic attempts to repeal this measure have been losing rather than gaining momentum. The law was adopted after a study concluded that discriminatory zoning practices in Massachusetts were motivated by economic rather than racial concerns.[18]

Under this law a developer of proposed subsidized housing may apply to a local zoning board of appeals for a single comprehensive permit, combining separate approvals from the building, health, and planning authorities. If this comprehensive permit is denied, the developer may appeal to the State Housing Appeals Committee, which may reverse the denial as "unreasonable" or "not consistent with local needs." The law establishes a "local needs" requirement that is, in effect, a general and annual low and moderate income housing quota for each city and town. Thus, a local board must grant the permit unless this quota has been met or there are sufficient relatively standard planning objec-

[17] Mass. St. 1969, C. 774 (Mass. G.L.C. 40 B §§20–23, "An Act Providing For The Construction Of Low- and Moderate-Income Housing in Cities And Towns In Which Local Restrictions Hamper Such Construction").

[18] The report of the Legislative Research Council which studied the problem that led to the creation of C. 774 is described by the Supreme Judicial Court in its opinion, n. 10.

tions to the project. In contrast to New York's creation of a corporate public entrepreneur, Massachusetts has given this new tool to local private or public entrepreneurs to enable them to carry out their projects more effectively.

The initial hope that the introduction of this novel direct State power on behalf of developers would spur municipalities to take action on their own has not been achieved, although there have been some local board approvals of proposed housing, particularly housing for the elderly. Significantly, such acceptance as has been won at the local level for the new system seems to be based in part on the fact that initial appeals have involved projects that primarily will benefit existing residents of the localities in which they are to be built.[19]

Three projects have been constructed as the result of local comprehensive permits. An important test of the system has recently been won in the Massachusetts Supreme Judicial Court.[20] It is now expected that the new process will be used more frequently by developers. Even in the absence of a definitive ruling, the number of appeals to the State Housing Appeals Committee had risen from three in 1970 to 19 altogether by June 1972. Practically all of the active applications for permits have come from metropolitan suburbs, suggesting that in this instance the assumptions of State legislators were correct: most suburban representatives opposed the act and many conservative core city representatives supported it in the hope that it would not impact their areas and would require suburban assistance to help relieve core city pressures.

In upholding the law, the Massachusetts Supreme Judicial Court made the following observation:

> The legislative reports which promoted c. 774's passage demonstrated how local restrictive zoning regulations have set up, in fact if not intentionally, a barrier against the introduction of low and moderate income housing in the suburbs. Moreover, this barrier exists at a time when our housing needs for the low and moderate income groups cannot be met by the 'inner cities.' This housing crisis demands a legislative and judicial approach that requires 'the strictly local interests of the town' to yield to the regional need for the construction of low and moderate income housing. Chapter 774 represents the Legislature's use of its own zoning powers to respond to this problem.[21]

[19] Barr, The Massachusetts Zoning Appeals Law: Lessons of the First Three Years (unpublished, August 1972).

[20] *Bd. of Appeals of Hanover* v. *Housing Appeals Committee*, 294 N.E. 2d 393 (Mass 1973).

[21] Id.

Although the Massachusetts statute has ambiguities—some of which have been clarified by the Supreme Judicial Court opinion—it provides a more useful model for State action than any other existing State legislation. It is more than a procedural statute to tidy up the zoning laws; it responds to a State policy of encouraging a better distribution of lower income housing. In this respect it is compatible with but superior to the State land use policies contemplated by the National Land Use Policy Act (see Section IV infra).

Recommendation #3: The Department of Housing and Urban Development should prepare and disseminate a model State statute patterned on that of Massachusetts as a guide to State action under National Land Use legislation; any program for allocating Federal funds to States for housing should require a similar State policy as a component of eligibility for such funds.

Florida Land and Water Management Act

While Massachusetts chose to develop a State appeals system limited to low and moderate income housing questions, Florida has adopted legislation that enables the State to influence all land use decisions that will have a "substantial" impact outside the local jurisdiction where the land is located. The Florida Environmental Land and Water Management Act of 1972 [22] grew out of concern with water quality and recent recurrent periods of drought that threatened the adequacy of water for the State's burgeoning population.

Under the law the Governor and cabinet are empowered, among other things, to adopt standards to decide whether certain land development activities are "developments of regional impact." Such standards were not to go into effect until reviewed and approved by the State legislature. "Development of regional impact" is defined under the Florida law to include any development "which because of its character, magnitude or location, would have a substantial effect upon the health, safety or welfare of citizens of more than one county." The Governor and cabinet may hear and rule on administrative appeals from development orders by local governments in regard to developments of regional impact.

As in the case of the American Law Institute Model Land Development Code on which it is based, the Florida law is process-oriented and

[22] S.B. 629, 1972.

does not make normative choices as to whether, for example, lower income housing in suburban locations is a desirable goal of State policy.

Regulations under the law, as approved by the legislature, regarding "developments of regional impact" do not pertain specifically to subsidized housing because the requirement of substantiality under the statute may not be met except by the largest of developments—and these are the least desirable to promote under more contemporary standards that favor "scattered site" development. In addition, there were obvious political constraints in legislative review of the proposed regulations.

The Florida law is probably consistent with the laws to be encouraged under the administration's original National Land Use Policy Act (see Section IV). As such, it appears to be an example of the relative ineffectiveness of this approach to the problem of local resistance to lower income housing.

Minnesota Regional Tax Sharing Program

A dominant reason for the local exclusion of lower income housing—or housing generally—may be found in the prevailing assumption that such land uses have a negative impact on the local tax base. According to the Land Use Committee of HUD's Advisory Committee, however, "we do not know the extent to which exclusionary practices are based on legitimate fiscal opportunity costing by local governments, or on local discriminatory practices." [23] Another study has tentatively suggested that racial—or, more properly, social—prejudices rather than fiscal calculations explain exclusionary land use policies:

> By surveying American metropolitan areas, the study produces significant evidence that clustering is aggravated by the imposition of public land use controls—such as zoning—in the suburbs. It also suggests that such controls are not typically imposed for fiscal reasons, i.e., to increase the taxable value of real property in the jurisdiction and to exclude low income residents who would heavily burden the jurisdiction's public services. Finally, the study finds that income group clustering is greater the more heavily nonwhite are the low income groups involved. These findings thus raise but do not resolve the question whether clustering results to a degree from racially motivated public controls.[24]

With these qualifications in mind, it nevertheless appears desirable for HUD to promote State policies that neutralize the fiscal impact of various land use decisions, particularly decisions regarding residential rather than nonresidential uses. Localities commonly compete with one another for those uses that are regarded as having a positive rather than negative impact on local cost-revenue projections.

The most innovative approach to this issue is Minnesota's 1971 metropolitan fiscal disparities law.[25] The law guarantees every unit of government in the Twin Cities area—whether a city, village, township, school district, county, or special district—a share of the region's growth in commercial/industrial property tax base, regardless of where this growth occurs in the seven-county area.

This is accomplished without changing the autonomy of some 300 independent taxing units in the metropolitan area.

The law works entirely within the preexisting framework of local government. No additional tax is imposed. No metropolitan taxing agency is created. All localities continue to make their own policy decisions on levying property taxes.

Each community continues to have a tax base, the only difference being that beginning with the 1972 valuations (which are used for taxes payable in 1973) a community's valuation was to be made up of two parts, that which remains local, or not shared, plus its assigned share of the region's growth over 1971.

None of the existing tax base of a community is shared. The share portion was to be 40 per cent of the net growth of commercial/industrial valuation after 1971. All other valuation, which includes all residential properties, will continue to be used exclusively by the governmental units where the buildings are physically located.

All communities are to contribute 40 per cent of their net growth in commercial/industrial valuation and all communities receive back an assigned share of the growth.

Each community's share is to be determined basically by its population but adjusted so that a community receives a larger share if its property valuation is below the metropolitan average per capita and a smaller share if its valuation is above average.

A unique feature of the law is that it introduces base sharing as a separate and distinct concept from revenue sharing.

[23] Op. cit., n. 8 to Introduction at p. 20.

[24] Branfman, Cohen and Trubek, "Measuring the Invisible Wall: Land Use Controls and the Residential Patterns of the Poor," 83 *Yale L.J.* 483, 484 (1973).

[25] Ch. 24, Minn. 1971 Extra Sess. Laws.

The law maintains fiscal responsibility, since no jurisdiction can levy against its share of the region's growth anything it is not willing to levy against its own resident/voters.

If more people move into a community, that community's share of the region's growth of commercial/industrial tax base also increases under the law. Consequently, it can become a major modulator of the "antigrowth ethic" referred to in the Introduction.

Unfortunately, the administration of the law was enjoined in January 1973 by a lower Minnesota court on the ground that it "fails to pass the test of constitutional uniformity requiring that the burden of a tax must fall equally and impartially upon all persons and properties subject to it."[26] An appeal is pending.

Regardless of the technical limitations that may, or may not, impede this approach to overcoming fiscal zoning in Minnesota, this law provides a useful model for other States, particularly within their metropolitan areas. Neutralizing the fiscal impact of residential development, particularly residential development for lower income households, may not entirely neutralize local exclusionary policies. But it can pierce the veil of fiscal rationales for such actions, and make a fiscal subterfuge far less handy.

Recommendation #4: The formula for grants under the Better Communities Act or similar legislation providing for metropolitan area entitlement grants should be increased on a demonstration basis for any metropolitan area that has a qualified tax sharing law in effect for the area patterned on the Minnesota example.

Metropolitan Growth Management Agencies

The fragmentation of governmental jurisdiction and power among a multiplicity of semiautonomous political entities within metropolitan areas has rendered a coordinated attack on these problems difficult, if not impossible. Operating within its constitutional restraints, the Federal Government has sought to induce interjurisdictional cooperation in the solution of metropolitan problems by conditioning certain categories of its financial aid on comprehensive areawide planning.

The State governments, whose legal powers to achieve areawide coordination are virtually unlimited, have, by and large, been guilty of nonfeasance. Generally speaking, their permissive statutory devices have been ineffective in meeting the problems of metropolitanism. In terms of the metropolitan problem, their duty may be viewed as bridging the gap between Federal financial inducement and local intransigence.

Ideally, some form of metropolitan government is in order. From a realistic point of view, however, it is quite clear that current political attitudes are not receptive to this thinking. A more palatable alternative is planning machinery that, while sensitive to the legitimate values in local autonomy, effectively compels a comprehensive, rather than a haphazard, piecemeal approach to metropolitan area development.

With the new sensitivity to ecological problems has come a better appreciation that highways, sewer and water lines, large recreation areas, and other major facilities are region-structuring elements that should guide development rather than respond to it. The location and staging of industrial and commercial facilities and lower income housing are other major ingredients in a region-structuring plan.

Planning without a bite tends to be less responsible planning. The metropolitan plan should serve as the constitutional framework within which local land use plans and any possible State land use decisionmaking takes place.

In operative terms this means that the regulatory character of the metropolitan plan should require that all local plans and the efforts of local implementing legislation and capital facilities projects of local governments or special districts conform to the metropolitan plan.

Given the importance of coordinating statewide and metropolitan area developmental programs, there should be State review of the metropolitan plan to insure against any latent conflicts between statewide and regional policies that may have been overlooked during the period of plan formulation. However, where a conflict does arise and it cannot be resolved by agreement, the State might be vested with a veto power (to be exercised by the Governor and his cabinet, i.e., the State planning committee) over all or any part of the plan in the interests of the general welfare of the State as a whole. State approval of the metropolitan plan as a condition precedent to its official promulgation would also be desirable as would a State mandate to the planning commission to rework its plan to conform to State recommendations or directives.

To guard against an unbridled assumption of the metropolitan function by the State, the State legislation should clearly indicate that the State veto power can be exercised only when statewide

[26] *Village of Burnsville* v. *Onischuk et al.* (No. 73749, Dist. Ct. Minn. January 29, 1973).

interests are affected. The power should not be capable of exercise in relation to concerns indigenous to the metropolitan area itself.

Provision must also be made for appeal to the courts in regard to the relations between constituent communities and the metropolitan planning commission.

To cover those situations where local inaction may thwart planned areawide development (e.g., a housing authority failing to begin a project within the time specified by the plan, a local legislature failing to enact a zoning ordinance requisite to effectuation of the plan), the metropolitan commission must be vested with an initiative power. Accordingly, the legislation might empower the commission to order noncooperating governmental units to take affirmative action in appropriate circumstances.

The closest model of this initiative is found in the Metropolitan Council of the Twin Cities Area, whose jurisdiction covers a seven-county area in the Minneapolis-St. Paul area encompassing almost 2 million people and half the population of the State.[27] The council, created in 1967, prepared a development guide, the first component of which significantly dealt with sanitary sewers. The council has power to review, and in some cases suspend, the plans of local government and local special purpose agencies.

The fiscal disparities legislation previously described was proposed by the council. It has also reproposed a metropolitan housing agency after the original proposal was not acted upon in the 1971 legislature.[28]

This highly abbreviated discussion of metropolitan planning suggests simply one pattern among many possibilities to design ways to manage urban growth more effectively. This "regional ideal" should be regarded as the next goal of Federal policy, building on the existence of regional councils of government (COG) stimulated by the Federal Government and the A–95 process.

COG's have proved to be only the first step toward viable region-structuring planning. In the words of one observer, additional Federal pressure on COG's "coupled with the growth of regional single purpose agencies, and the increasing 'visibility' to State legislatures of new regional governing responses, will lead to the evaluation (or replacement) of the COG into a mechanism which can plan to deal with regional problems and implement those plans." [29]

Consequently, the Federal Government must move beyond its primary concern over the coordination of its grants, to a concern for the promotion of equitable and environmentally sound urban growth management in the Nation's metropolitan areas. One example of the price for failure to do this is becoming evident in the ultimate impact on housing availability of the sewer moratoriums around the Nation. Sewer lines and sewage treatment plants are region-structuring facilities; but they can also be convenient means to discriminate against needed additional urban development. Pumping Federal resources into a competitive and fragmented system of metropolitan governance may permit the recipients to undercut not only the effectiveness of Federal resources going to their neighbors but will reduce the effectiveness of the Federal housing subsidy dollar (in whatever form) as land costs drive up housing costs. Housing allocation plans adopted by such institutions would have more effect than such plans adopted by existing A–95 agencies.

The Responsive Communities Act now under consideration may provide a vehicle for Federal inducements to create effective metropolitan growth management institutions.

Recommendation #5: The Secretary of HUD should commission the drafting of model State metropolitan growth management legislation along the lines indicated; and generous demonstration funding under the Responsive Communities Act should be made available to States and regional agencies whose enabling legislation qualifies under the model within three years passage of the act.

Relevant Local Initiatives

Emerging from the patterns in New York, Massachusetts, and Florida is a common theme that allowing local communities unilaterally and exclusively to select the kind of development they desire, without conscious consideration of the social impact on the larger region, seriously weakens the chances for achieving social objectives important to the State as a whole. This the-

[27] A description of the Twin Cities Council legislation is described in Bosselman and Callies, "The Quiet Revolution in Land Use Controls," p. 136 ff. (Council on Environmental Quality 1971).

[28] Id., p. 151. A bill to allow the Metropolitan Council to act as a housing and redevelopment authority was recommended for approval by the Minnesota House Metropolitan Affairs Committee on May 3, 1973. Under the bill the Council could not plan or propose any housing project within a municipality until the municipality asked the council to do so. See Minneapolis *Tribune,* May 4, 1973 ("Met Council housing project bill gains").

[29] Moguloff, "Governing Metropolitan Areas: A Critical Review of Council of Governments and the Federal Role" (Urban Institute 1971) at p. 115.

sis has, of course, been most forcefully impressed politically by ecologically minded interests that wish to prevent damaging or profligate development that many localities would otherwise permit for fiscal reasons. But many interests that wish to promote socially needed urban development have come to the same conclusion; that is, that local land use policies should be responsive to the interests of a wider constituency. Closely allied to the concerns of both social and environmental interests is the realization that controlling metropolitan development requires a sophistication in the balancing of interests that is in very short supply in the existing highly fragmented and decentralized system of land regulation.

Most urbanizing localities follow exclusionary polices that partake of one or all of the following techniques: (1) underzoning for residential uses; (2) large-lot residential zoning and/or excessive minimum cost or floor area requirements; (3) underzoning for multifamily housing and/or excessive ceilings on allowable bedrooms; and (4) discrimination specifically against subsidized housing. Developers and others have frequently been required to resort to the courts to overcome these restrictions.

Challenges to local land use controls in the State courts have usually been based on the principle that such regulations must take into account more than the welfare of the local community in order to be authorized under the State's zoning enabling act or, if authorized, to be constitutional under the due process clause of the 14th amendment. The denial of rights to a racial minority is usually not the thrust of such challenges. Rather it is the alleged unreasonable restraint on the use of property, and the classic plaintiff has been the owner or potential developer of land.[30] In this context the cases, particularly in Pennsylvania, take on the aura of regional planning considerations as central to the local exercise of the police power in a reasonable fashion. This has encouraged a recent trend to mount challenges to exclusionary zoning on areawide or countywide bases.[31]

[30] *National Land and Investment Co.* v. *Easttown Twp. Board of Adjustment*, 419 Pa. 504, 215 A. 2d 597 (1965); *In re: Appeal of Kit-Mar Builders*, 439 Pa. 466, 268 A. 2d 765 (1970); *In re: Appeal of Girsh*, 437 Pa. 237, 263 A. 2d 395 (1970); *Oakwood at Madison* v. *Twp. of Madison*, 117 N.J. Super. 11 (Superior Ct. 1971); *Bristow* v. *City of Woodhaven*, 35 Mich. App. 205, 192 N.W. 2d 322 (1971); *Lakeland Bluffs Inc.* v. *County of Will*, 114 Ill. App. 2d 267, 252 N.E. 2d 765 (1969).

[31] See *Southern Burlington County NAACP* v. *Township of Mt. Laurel*, 119 N.J. Super 164 (Sup. Ct. 1972); *Commonwealth of Pennsylvania* v. *County of Bucks*, 22 *Bucks Co. Law Rep.* 179 (1972); *Accion Hispana, Inc.* v. *Town of New Canaan, Conn.*, Cir. No. B 312.

Appropriate remedies to permit an individual project to go forward are not difficult to frame. But when the entire scheme of land use regulation is invalidated, the remedy becomes more difficult. How much lower income housing is enough? Where shall it be located? What kind of regulation will effectively encourage affirmative action? These are planning and economic questions that courts are not well equipped to handle. As a result, litigation has been of great assistance to a few sponsors and has proved an effective way to illuminate the basic conflicts. But it is only a predicate for institutional reform that must flow from new legislation and administrative procedures. This section deals with major local legislation and its potential relevance to HUD.

Development Timing

Serious questions have arisen in connection with the increase in the possible use of development timing controls by localities, a technique likely to flow from the recent opinion of the New York Court of Appeals in *Golden* v. *Ramapo*.[32] In that case, the court ruled that New York's zoning enabling act, which is similar to that of most States that followed the standard model, permitted the town of Ramapo to time development permits in relationship to the availability of public facilities such as sewers, drainage, recreation, roads, and firehouses. The town adopted a special permit system, applicable only to residential development, that prohibited all such development unless the land was in suitable proximity to these services. At the same time, the town also committed itself to provide these facilities over an 18-year period.

Although the court specifically dealt with the exclusionary implications of this technique—and observed that Ramapo did permit a modicum of public housing—little attention was focused on the zoning of uses for which permits were to be given over the next 18 years. No multifamily housing zones as such exist, and by far the greatest volume of land developable for residential use is limited to single family housing on traditionally large lots. Thus, the development timing technique may be used even to pace exclusionary growth.

Critics have also pointed out that allowing one locality power to pace growth over any period it chooses—18 years being a more or less

[32] *Golden* v. *Planning Board of Ramapo*, 30 N.Y. 2d 359, 285 N.E. 2d 291 (1972).

arbitrary multiple of the usual 6-year capital budget—may work against anticipated regional growth requirements and simply shift the burden onto other localities.

Although a new public control over the timing of development is highly desirable if it is linked to a public commitment to the capital improvements necessary to assimilate growth, development timing can provide a new sophisticated tool for the exclusion of housing for lower income households. (This is explained at greater length in a recent publication of the Potomac Institute entitled "Controlling Urban Growth—But For Whom?") Ways to make such a policy more responsive to regional housing needs are spelled out therein, and will not be repeated here.

The question arises as to whether there can be any appropriate Federal influence on sequential development controls attempted by localities when these controls in effect may inflate housing costs by withdrawing large areas of land from development. It seems inequitable for such localities to receive special revenue sharing funds for community development purposes when they are in effect working against regional housing needs.

Recommendation #6: A community that has adopted an exclusionary development timing policy should not be entitled to grants under any program of special revenue sharing for community development. (See related Recommendation #8 in the third section.)

Inclusionary Zoning

The problems of exclusionary zoning have been analyzed and litigated with mounting frequency in the past few years. Some communities have attempted, however, to develop "inclusionary" zoning. Usually this has been a response to the prevailing land use and inflationary trends that prevent suburban areas from providing residential opportunities for moderate income public employees—teachers, firemen, and policemen are often cited as examples in gaining political support for inclusionary ordinances. If developers are providing only housing costing more than $25,000, the household earning under around $12,500—which includes many public employees—may be priced out of new or nearly new housing.

Inclusionary techniques have included relaxation of the existing zoning regulations to promote subsidized housing, and the creation of special incentives for the same purpose. Examples of the first category include the granting of a special-use variance for subsidized private housing, now upheld in New Jersey,[33] the creation of special exceptions and "floating zones," or the exempting of public housing from minimum bulk, height, and intensity requirements as upheld in Massachusetts.[34] As courts come to regard subsidized housing as a land use meriting special treatment in the public interest, the notion that such housing is a "public utility" will have gained acceptance and will merit close attention to analogous methods proposed for siting power plants, for example.

Among incentive measures, the most frequently suggested is the "density bonus." This may be part of a planned unit development (PUD) regulatory scheme under which the developer of more than small-scale residential developments is given freedom from conventional bulk, height, and use restrictions of the standard zoning ordinance in return for municipal review of detailed site designs and other conditions. One condition may be the provision of lower income housing, in return for increases in otherwise allowable densities. A small number of communities have experimented with these incentives.[35]

An ordinance of Fairfax County, Va., in the Washington, D.C., metropolitan area, has received considerable attention. Although a lower State court has held the ordinance invalid,[36] it represents a major effort in a rapidly growing suburban area to develop a balanced growth policy and demonstrates the difficulties inherent in such an attempt. Under the county's amendments to its zoning ordinance, developers of 50 units or more in all residential planned communities, residential planned unit developments, planned apartment developments, multifamily districts (other than highrise), and townhouse zones must include at least 15 per cent low and moderate income housing units. Of this, at least 40 per cent (or 6 per cent of the overall number of units) must be low income units.

The developer may fulfill the requirement by constructing the units outside his development, so long as doing so does not result in "undue concentration" of low and moderate income families in a particular geographic area. The ordi-

[33] *DeSimone* v. *Greater Englewood Housing Corp.*, 56 N.J. 428, 297 A. 2d 31 (1970).

[34] *Cameron* v. *Zoning Agent of Bellingham*, 260 N.E. 2d 146, (Mass. 1970).

[35] A number are described in Brooks, Lower Income Housing: the Planner's Response (ASPO Planning Advisory Service, July–August 1972).

[36] *DeGroff Enterprises, Inc.* v. *Board of Supervisors of Fairfax County*, (No. 25609). The appeal was argued in the Supreme Court of Virginia in June 1973.

nance is keyed into the availability of Federal subsidies. If these are not available after bona fide attempts to obtain them, the developer is relieved of the obligation and may proceed to develop entirely market rate housing.

Fairfax is the only Washington jurisdiction with a decrease (to 3 per cent) in its black population, mostly because of the large immigration of whites; the black resident population is in great need of housing. Although racial considerations moved the church-related coalition that first pushed for this ordinance, the opportunities for a black immigration from the central city would not be greatly increased even were the ordinance successful since at best it would produce only 1,000 units a year. The "scattered site" policy inherent in this approach makes affirmative marketing difficult, in the view of many observers, because relatively few blacks want to live in racially "isolated" situations and the costs of affirmative marketing for a handful of units are uneconomic for many developers.

In addition, the design of existing federally assisted housing programs tends to discourage developments of widely mixed incomes under a single "package" mortgage that covers projects that appeal to middle income and lower income occupants. As a model, the 15 per cent and 6 per cent figures are too high for HUD to subsidize in many metropolitan areas even though they may be too low in relation to needs in a locality. It is also unclear whether the sites chosen for upper middle income housing, populated by two-car households, are desirable for lower income households more dependent on public facilities, such as transportation. Thus, a "mechanistic" policy applying this standard to every subdivision of over 50 units, were it workable, could result in the placement of lower income units in undesirable locations.

In another part of the Washington, D.C., metropolitan area, the Montgomery County (Maryland) Board, elected in 1970 in part on a platform pledging more moderate income housing, is still considering ways to implement that pledge through the county's zoning regulations. Under study are provisions requiring moderately priced dwelling units in every moderate and large site residential development, with accompanying density bonuses. Unlike the Fairfax approach, Montgomery would not tie its program into available Federal subsidies. Developers would be required to price units according to a moderate income schedule on an unsubsidized basis.

It is apparent that "inclusionary" zoning has proven to be a difficult concept to implement on a volume basis outside the context of large scale developments such as HUD-guaranteed new communities. (See Recommendation #10.) The difficulties of predetermining land uses through zoning are not limited to subsidized housing, which explains to a large extent the preference for "negotiated" land use controls that are more common in recent years.

The question arises as to the entry point for Federal influence in regard to local land use policies. What incentives can be devised to encourage localities to develop an inclusionary rather than exclusionary policy?

From time to time, direct incentives to "sweeten" the acceptability of subsidized housing have been suggested. For example, H.R. 9688 considered in 1971 by the Housing Subcommittee of the House Committee on Banking and Currency proposed "incentive grants" to localities that accepted subsidized housing.

The following questions pose serious limitations to such grants:

1. As the courts strike down some of the local barriers to subsidized housing, is it wise to provide incentives to localities to encourage them to do what they may, in any event, be legally obligated to do?

2. If Federal incentive grants become limited or unavailable, would the housing programs become crippled?

3. If the incentive grants are tied to subsidized housing (as usually proposed), what about those families with children of school age who move into older unsubsidized housing in close-in suburbs?

4. The central cities have housed the poor or near poor for generations without such incentives. It seems ironic that areas that are likely to be gaining major industrial and commercial developments are thought to need help to do what central cities have been doing without such help. (If gilding the ghetto is questionable, is not gilding the lily even more so?)

5. Might the incentive grant in effect unnecessarily subsidize localities that mount a low tax effort with a high tax base? One suburban community cited in an Urban Land Institute report [37]

[37] Teska, R., "Who Pays For What: A Cost-Revenue Analysis of Suburban Land Use Alternatives," *Urban Land* 3 (March 1971).

can "break even" (that is, no deficit on the cost of schooling) on new single-family, four-bedroom homes only if they have a market value of $100,000. This is because that locality has an extremely low assessed valuation, and a high tax base, and spends more per student on education than any other locality in its metropolitan area.

We believe there are more effective ways in which HUD can stimulate a more inclusionary land use policy on the part of local communities. One method is suggested in the third section of this paper infra, with respect to the housing component of special revenue sharing for community development. Another relates to HUD encouragement of larger scale planned residential developments that are subject to requirements regarding social-economic mixing. (See Recommendation #11.)

In addition, it can be assumed that HUD has very likely been paying for exclusionary planning through the 701 Planning Assistance Program. Accordingly, we suggest that at the least the Department withdraw its financial support for urban planning that is not responsive to a full spectrum of regional housing needs.

Recommendation #7: Urban planning financed with Federal funds should adhere to the following general guidelines:

- Local plans should require the locality to demonstrate responsiveness to regional housing needs;
- A local plan should provide for housing for employee households with existing or anticipated jobs in the jurisdiction;
- Plans that do not adhere to these guidelines should be financed by non-Federal sources.

A recent report by a Task Force on Land Use and Urban Growth to a Presidential committee has described a "new mood" in many urbanizing parts of America. This new mood is changing our traditional "growth ethic" to a "no-growth" ethic:

> Once, citizens automatically accepted the idea that growth—in numbers of people, in jobs, in industries—would ease the public burden by increasing the tax rolls and spreading per capita costs. Now they have doubts. They seem to be expressing the belief that larger size means not only lesser quality but also higher costs. Pressed by inflation, they listen carefully to arguments about the hidden costs of growth.
>
> The new mood reflects a burgeoning sophistication on the part of citizens about the overall, long-term economic impact of development. Immediate economic gains from job creation, land purchases, and the construction of new facilities are being set against the public costs of schools, roads, water treatment plants, sewers, and the services new residents 'require.'[38]

To the extent that this "new mood" results in conflict with national housing policy, HUD at the very least should not be subsidizing planning techniques that give effect to it. And despite the fact that the "new mood" focuses on large scale developments, HUD policy should promote such developments as the most promising method of increasing housing choice.

Federal Initiatives—HUD As Lead Agency

This section sets forth recommendations concerning HUD's potential role as "lead agency" in reducing the impact of land use and related regulations as a barrier to the provision of housing assistance to low and moderate income families. In 1970 HUD proposed legislation to protect federally assisted housing against prejudicial local zoning. Such legislation, although sponsored by the Department, did not obtain a hearing in the Housing Subcommittee of the House Banking and Currency Committee. Since it is unlikely that such legislation would obtain favorable consideration in 1973, attention will be focused on how some of HUD's potential housing approaches should be fashioned to discourage local barriers, against the placement of low and moderate income housing outside areas of economic and racial concentration. Special emphasis will be placed on community development revenue sharing, utilization of State housing finance agencies, and the new communities and planning programs. In addition, recommendations will be made in connection with subsidies for larger scale residential developments, metropolitan housing allocations, and special problems relative to housing allowances.

Community Development Revenue Sharing

The three major legislative efforts regarding community development revenue sharing are:

- The 1973 administration bill (Better Communities Act) H.R. 7277 (hereinafter referred to as the "administration bill").
- Chapter III of S.3248 as passed by the Senate on March 2, 1972 (hereinafter referred to as the "Senate bill").

[38] Op. cit., n. 7 to Introduction.

• Chapter IV of H.R. 16704 as reported by the House Banking and Currency Committee on September 21, 1972 (hereinafter referred to as the "House bill").

These bills will be examined from four aspects: eligible recipients and fund allocations, eligible activities, application requirements, and local share of financing. The analysis will focus on how this type of legislation should be structured to reduce barriers to free location of low and moderate income housing.

1. Grant Recipients and Allocation of Funds: Both the House and administration bills have a similar provision concerning grant recipients—namely cities, counties, or other general purpose political subdivisions or a consortium thereof. The Senate bill permits a local public agency to be designated by a general unit of local government to undertake the community development program in whole or in part.

The Senate provision permitting a city to designate another agency to administer the program is a desirable one from the standpoint of initiating innovative or potentially controversial housing projects. (See below on the broadening of a local agency's powers to include housing.) The political heat would be removed from the city council to a body that it only indirectly controls; this might prove advantageous to elected officials facing protests against location of the housing facility. The optional nature of the Senate provision is also desirable, as in some cases the general unit of local government might be in a stronger position to resist such protests than a local public agency.

Concerning fund allocation, all three bills would provide funds to "metropolitan cities," generally defined as a city with over 50,000 population in a standard metropolitan statistical area (SMSA). However, the House bill introduces the "urban county" concept providing allocations to counties with a population of 200,000 or more exclusive of the population of the metropolitan cities therein—approximately 90 counties. The administration bill also includes urban counties as grant recipeints.

The inclusion of urban counties seems a desirable provision in the light of our basic recommendation, as it is these counties that have often been the source of the greatest resistance to low and moderate income housing. Under our recommendations set forth hereunder, these counties would not receive any community development revenue sharing funds absent a positive effort to provide low and moderate income housing.

2. The Application Requirement: Both the House and Senate bills set forth detailed application requirements. Relative to housing, the Senate bill requires that the application contain, among other things, the actions to be taken during the forthcoming 3-year period to meet the community's housing replacement and relocation needs (especially those of low and moderate income families), to prevent and eliminate slums and blight, and to upgrade neighborhood environments through renewal, code enforcement, and other community improvement programs. The application also must include a description of activities for the next 2 years, including any requirement for federally assisted housing units and rehabilitation loans. The House bill likewise requires a detailed application, including the formulation of a program to provide an adequate supply of standard housing in a suitable living environment, particularly for low and moderate income individuals residing in or employed in the community or who may be "reasonably expected" to reside in the community. The administration bill rejects the application concept in favor of the submission of a statement of community development objectives and the projected use of upcoming funds with no specific mention made of housing.

If community development revenue sharing is to be utilized to achieve balanced placement of low and moderate income housing then the detailed House or Senate application procedure must be utilized. There must be an ascertainable commitment of the community to provide low and moderate income housing within the limit of funds made available to it. Performance would be judged against this commitment in the application. The application must also set forth the specific method of utilizing revenue sharing to provide housing assistance. (See below for an outline of these methods.)

3. Eligible Grant Activities: All three measured contain seven basic permissible uses of special revenue sharing funds. Acquisition of deteriorated or blighted property appropriate for rehabilitation and the subsequent disposal thereof heads all lists. The bills also include authority for historic preservation, urban beautification, and open space conservation. Concerning housing, the Senate bill specifically provides grants or loans for rehabilitation or property conservation. Such power is included within the general authority for rehabilitation in the House and administration bills. Although the Senate bill contains several more eligible expenditures, none is specifically related to the provision of housing. Accordingly, all three lack the necessary incentives for a community to provide low or moderate income housing, a necessary provision if the barriers to such housing are to be removed. To remedy these defects, the following recommendations structure a community development revenue sharing bill to achieve such goals.

A community development revenue sharing bill should require the provision of low and moderate income housing in conformity with both the community's overall development plan and HUD's Project Selection Criteria. In other words, the price of community development revenue sharing funds is an action program to provide housing for low and moderate income families. HUD's site selection criteria assure project location so as to avoid racial impaction. This recommended housing-community development linkage also goes far in assuring that a community has zoning provisions or other ordinances encouraging the provision of such housing.

In order to make the foregoing recommendations financially feasible, HUD should provide funding for lower income housing on a level of the cumulative contract authority utilized in fiscal year 1972 for the section 235, section 236, Rent Supplement and Public Housing Programs—approximately $578,000,000.

There seem to be two methods to tie those housing funds with community development revenue sharing.

- The authorization now contemplated for the Better Communities Bill could be increased by $578,000,000 with an earmarking for the housing component. Accordingly, such funds would be distributed by the same formula (population, poverty, and housing overcrowding) as now contemplated for community development revenue sharing.
- Enactment of a separate housing revenue sharing bill that would allocate funds in a similar, but not necessarily identical, manner to the Better Communities Bill. The rationale for a different formula is that communities may have different needs for housing funds than for other community development activities, and some wealthier localities should in effect be enabled to "catch up" on their deficient supply of lower income housing. Any separate bill would have to be carefully drafted to assure the dovetailing of housing and community development revenue sharing.

Assuming that the programs are not continued in their present form, local communities should be granted the maximum flexibility concerning the utilization of housing revenue sharing funds. Today's housing programs are bottomed on guaranteed interest subsidy for up to 40 years. Unless Congress commits itself to revenue sharing payments for such a period, then this approach would not be feasible. However, Congress should guarantee housing revenue sharing funds for a reasonable period, 5 to 10 years, so that communities can enter into lease arrangements for private housing for terms of that length or otherwise enter into assistance commitments.

The following discussion sets forth several illustrations as to how housing revenue sharing funds might be utilized to further the dispersal of low and moderate income families.

Shallow Subsidy—Capital Grants: A community could use its funds to establish a program of no-interest second mortgage loans to either purchasers of a single family home or developers of moderate income multifamily projects. Such mortgages could have a significant effect in reducing monthly payments or rents. Such a no-interest second mortgage interest loan, coupled with a first mortgage loan from a State housing finance agency at its below-market rate (e.g., 6 per cent), could reach the moderate income market.[39]

Under this shallow subsidy program, there would not be the great economic gap between the subsidized and the nonsubsidized family that exists when a section 236 project is placed in a middle class neighborhood. Accordingly, it should be easier to locate such units throughout a community. This approach provides great flexibility in a multifamily project. For example, each unit need not receive the same $5,000 no-interest loan. Some units could receive the economic equivalent of a $10,000 no-interest loan, and oth-

[39] Assume $20,000 mortgage; State HFA loan at 6 per cent:

$15,000 at 6%—40 years	$82.54	
5,000 no-interest loan	00	$82.54
Comparison with market rate:		
$20,000 at 8%	$139.07	per month to amortize
Amortization under this plan	82.54	
Savings under this plan	56.43	
	4	
	$226.72	less monthly income needed under shallow subsidy plan

It will be observed that this shallow subsidy approach enables a family with $225 less monthly income to live in a unit carrying a $20,000 mortgage. This would be a significant program for moderate income families.

ers a $2,000 no-interest loan. In our example, a section 236 family could afford such a unit if the owner were paying only 6 per cent interest on $10,000 and no interest on the other $10,000.

Leasing Program: The community could also utilize its special revenue sharing funds to lease standard existing units. This would in essence be a locally administered housing allowance or Section 23 program. The community should be allowed to lease units under a flexible rent scale to enable it to lease in all portions of the community. The leasing of existing units for low income people should be operated in tandem with the production of new units for moderate income families utilizing the shallow subsidy mechanism set forth above. Otherwise, there well may be no units available to lease under this version of the housing allowance.

Tax Abatement or Other Operating Subsidy: The community could use its revenue sharing fund to abate the taxes of low and moderate income owners of single family homes, or the owner of multifamily units that rent to a given proportion of low and moderate income families. Likewise, it could utilize such funds to pay other operating expenses on such units. The locality must provide such assistance on units located throughout the community to accomplish the ends addressed in this paper.

If it is determined to continue the housing subsidy programs in substantially their present form, then such programs should be administered in tandem with community development revenue sharing. Accordingly we recommend the following programmatic changes in the way housing subsidies are now allocated:

- Allocation of housing subsidy funds should be roughly in the same proportion as community development revenue sharing funds.
- There should be included in the annual application filed by the community development agency a plan for the utilization of Federal housing subisdy funds in its area.
- The community development agency should have the authority to instruct the HUD office as to the allocation of up to 80 per cent of the subsidy funds to assure coordination between housing and community development activities.
- If the community development agency does not assure that housing is provided in conformity with HUD's present selection criteria, then HUD can withdraw all community development revenue sharing funds to that loacality.

This should prove a strong incentive for the local community to exercise its zoning, building code, and other powers so as not to impede the location of low and moderate income housing on an unfettered basis.

4. Local Share: Under the Senate bill, the Federal share would equal 90 per cent of the total net program cost, except that the Federal share of any rehabilitation grants or relocation payments would be 100 per cent. The local share would either be in cash or in donated property or services. Under the House and the administration bills, the Federal share would equal 100 per cent.

In order to utilize revenue sharing as a prod to the local community to remove land use barriers, a community must first participate in the revenue sharing program. For that reason, we favor 100 per cent Federal funding so that a community could not fail to participate on the grounds that the local share presents too onerous a requirement.

Recommendation #8: In essence, no community should be allowed to receive the benefits of community development revenue sharing funds absent a specific program to make low and moderate income housing available throughout its jurisdiction. This should provide the incentive to all communities to háve a meaningful housing program. On the other hand, our proposal would not divert community development revenue sharing funds to housing, but envisions a new housing revenue sharing funding source.

State Housing Finance Programs

This discussion sets forth the Federal requirements and guidelines to be imposed on State or metropolitan housing finance or development agencies receiving Federal assistance to reduce the impact of land use regulations as a barrier to the provision of housing assistance. Although there are now 28 such agencies on the statute books, only a handful have really been in effective operation (Massachusetts, New York, New Jersey, Michigan, Illinois, and West Virginia). However, their experience provides some guidance to the type of Federal requirements that should be imposed, assuming widespread utilization of the State housing finance agency and the desire to reduce local housing impediments.

By and large, State housing finance programs have been successful in placing units in suburban locations. A McKinsey and Company, Inc. study points out that a review of the production of three State agencies showed that about 60 per cent of their units went to the suburbs.[40] However, the McKinsey study notes that these were units essentially for middle and moderate income families with only 10 per cent for low income families. Several factors explained this result. First, the only way that a project financed by a State housing finance agency can reach even moderate income families is through a section 236 "piggyback." It can only reach low income families if a rent supplement is added to the section 236 subsidy. As such double subsidy has been relatively scarce, there has not been the deep subsidy available to combine with State programs to house low income families.

The second reason, more relevant to this inquiry, is that State housing finance agencies, as an operational arm of a State government, are more subject to local pressure not to locate low income projects in areas where low income housing does not exist. Massachusetts, with its unique law, is an exception to this generalization. The experience of the New York State Urban Development Corporation, already discussed, is the latest and most dramatic example of this problem. In discussions now taking place about the expanded role of State or metropolitan agencies, the objection is often posed that they would be subject to irresistible political pressure not to locate assisted housing in areas where strong local opposition exists.

State programs should not be so structured as to unduly favor the local developer over the multistate developer. It is important that the large multistate developer of low and moderate income housing continues to participate in subsidized housing programs in that such entities are less subject to local pressures not to build housing in a location where it may be unpopular. If large scale reliance is to be placed on State housing finance agencies, HUD should promulgate some basic procedures and forms to be utilized by all State agencies receiving Federal assistance in any form. This does not mean that there should be minute Federal regulation of State housing finance agency procedures; there should be general processing similarity so that a multistate developer will not be inhibited from operating outside his jurisdiction.

[40] *New Directions for State Housing Finance Agencies*, McKinsey and Company, 1973 (pp. 2–3).

Our recommendations to meet this problem assume sufficient Federal leverage to allow the imposition of the necessary restrictions. This leverage could come in the present form of "piggybacking" section 236 and rent supplement subsidy onto the agency loan or such possible measures as the Federal guarantee of State housing finance agency bonds, Federal payment of agency administrative expenses, or an additional allocation of funds for the agency on a revenue sharing basis to be utilized to subsidize further housing units consistent with the methods set forth above.

Recommendation #9: Federal assistance to State or metropolitan housing finance agencies only assist projects that are in compliance with locational requirements set forth in applicable judicial doctrine as to project location, and with HUD Project Selection Criteria. If an agency follows a pattern of refusing to assist projects, otherwise worthy but opposed by neighbors or the locality, or if such agencies only make loans to projects that would cause racial impaction, then Federal assistance to such State housing finance agencies should be terminated. (See related Recommendation #1.)

Large Scale Development and Lower Income Housing

The major assumption of this subsection is that it is likely to be easier, from a planning, political, and economic standpoint, to introduce a greater socioeconomic mix into housing if it is being developed as part of a much larger scale development. As already noted in the second section, those localities experimenting with "inclusionary zoning" have commonly applied such requirements only to planned developments at some scale larger than the usual subdivision. This may be proposed because localities may believe that the larger developer is more sophisticated in using Federal or State programs to subsidize housing, or that the additional costs entailed in providing submarket rental or sales housing can be more readily transferred to other purchasers in subdivisions of larger scale.

Special attention will be given to opportunities inherent in the New Communities Program as established pursuant to Title VII of the Housing and Urban Development Act of 1970 and opportunities under Title X of the National Housing Act.

The New Communities Program: An obvious way to preclude restrictions on the free location of low and moderate income housing is to start with a clean slate—a new community having no neighbors who may feel threatened by such housing. HUD, under Title VII, can and does seek to assure that low and moderate income housing is included within those new communities whose obligations are guaranteed by HUD. This is in accordance with the statutory mandate set forth in section 712(a)(7) of the Housing and Urban Development Act of 1970 to the effect that new communities must "make substantial provision for housing within the means of persons of low and moderate income and that such housing will constitute an appropriate proportion of the community's housing supply." The draft regulations are equally specific in requiring a housing mix. Section 32.7(d) requires that there be a "substantial amount of housing for people of low and moderate income during each major phase of residential development." In addition, a new community developer must include "reasonable assurances" that the unit planned will actually be provided.

The concrete embodiment of HUD's policy is set forth in the project agreement negotiated with each developer. Agreements with the developers of Jonathan and Cedar-Riverside, two "paired" new communities in the St. Paul, Minn., area, do not require the developer, in meeting the foregoing requirements, to integrate housing on a "unit by unit basis." Each project agreement, however, contains a schedule containing the number of low and moderate income dwelling units to be provided in each year of the development plan, together with 1 year, 3 years, and long term development plans. Practices emerging in the HUD New Communities Program, particularly with respect to the social ingredient of new community development, thus are taking on great significance for modern land use planning.

There is some indication that performance is bearing a relationship to the promise. For example in Cedar-Riverside, construction has begun on about 1200 residential units, 500 of which will be for lower income people. In Jonathan, contruction has been completed on single-family detached housing for lower income families on tracts contiguous to similar housing built for middle and upper middle income families.

New communities are not without their problems relative to the placement of low and moderate income housing. There has been little assurance under the present program that subsidized units will be available for new communities. HUD has experimented with new community "set asides" to a relatively limited extent (e.g., $4 million of section 236 contract authority in fiscal year 1971). However, under the section 236 program, HUD has attempted to cut down on the set-aside concept, because it proved to be a growing limitation on its flexibility in allocating subsidy funds. Thus, the best plans for low and moderate income housing in new communities can founder from the lack of funds for subsidized units.

Recommendation #10: Any housing subsidy program should be coordinated with the New Communities Program to allow the administrator thereof to have available subsidy funds to allocate to new communities. For example, section 7(d) of the Better Communities Act provides the HUD Secretary with discretion to allocate 10 per cent of the funds made available under that act. Assuming the adoption of the revenue sharing concept for housing subsidies, the Secretary should be given an equal percentage of funds not specifically allocated to either States or localities. However, of that 10 per cent the Secretary should be required to commit a stated percentage to Title VII new communities so that the new community developer can be assured of a given number of subsidized units. (Note the analogy of this suggestion to that set forth above concerning the allocation by a locality of its special revenue sharing funds for housing in conformity with its overall community development plan.)

Another problem concerning the new communities program is that it cannot be effectively utilized for large scale developments that are purely residential. Such developments, often designated as planned unit developments (PUD), have become increasingly prominent. The PUD developer has much the same flexibility as the new community developer in that he is usually free from strict zoning requirements relative to use, bulk, height, and setback, thus allowing flexibility in placement of housing, supporting recreational facilities, etc. Title VII cannot be utilized to guarantee the obligations of the PUD developer because of the requirement that the new communities have a strong economic base in addition merely to providing residential facilities. Section 712(a)(2) requires that a new community be "economically feasible in terms of economic base or potential for economic growth." Section 32.6(a) of the regulations is more specific in requiring that a new community must include most, if not all, of the basic activities and facilities normally associated with the city or town: ". . . industry, commerce. . . ."

It seems desirable that Title VII assistance should be made available to the large PUD developer even though the PUD development does not have all of the attributes of a full-size city. This would provide the leverage for low and moderate income housing to be placed in such developments. A recent paper [41] points out that in one typical PUD, the average income of a family residing in a three-story townhouse approached $19,000 a year, far beyond the range of any low or moderate income family. Our recommendation is directed to serving a greater income mix in the PUDs.

Recommendation #11: Title VII, and its accompanying regulations, should be amended to permit large planned residential developments with supporting recreational and public facilities to receive assistance, provided that such developments include lower income housing.

Title X: At the present time, HUD does have a mechanism that can be utilized for large scale land development: Title X of the National Housing Act. Title X provides mortgage insurance for land acquisition and improvements undertaken by private development entities. The mortgage term is 10 years. Eligible improvements include water and sewer lines and sewer disposal installations, steam, gas and electric lines and installation, roads, streets, curbs, gutters, sidewalks, and storm drainage facilities deemed necessary and desirable to "prepare land primarily for residential and related uses or provide facilities for public or common use." The principal obligations of a mortgage under title X may not exceed the lesser of (a) 75 per cent of the estimate of the value of the property upon completion of the land development, or (b) 50 per cent of the estimate of the value of the land before development, and (c) 90 per cent of the estimated cost of such land development. The maximum mortgage amount for any single land development undertaking is $25 million.

Title X, enacted in 1965, is regarded as the precursor of HUD's new community program. Title X has not been a widely used program in its 8 years of existence. The 1971 HUD statistical yearbook indicates that only four projects with 1,595 lots were insured in that year. Unlike title VII, regulations do not impose any requirement for the inclusion of low and moderate income housing, even though one section (205.86-CFR) refers to "New Community Criteria."

Recommendation #12: HUD should encourage utilization of the Title X program to a greater extent than present to encourage large residential projects. In so doing, it should impose on the Title X developer the same type of requirement for a housing mix that it does on the new community developer.

The Housing Element in Comprehensive Planning: The Housing and Urban Development Act of 1968 added the requirement that all comprehensive plans funded under section 701 must include a "housing element." The statute requires that the consideration of housing needs take into account all available evidence of the assumptions and statistical bases upon which the projection of zoning, community facilities, and a population growth is based, so that housing needs of both the region and the local community will be adequately covered in terms of existing population and projected growth.

Section 3 of Chapter IV of the Section 701 Handbook [42] sets forth the specifics of how the housing work program is to be prepared for a planning agency. The housing goals requirements seek (a) to assure that housing concerns become an integral part of community planning, (b) to eliminate discrimination in housing, (c) to develop housing growth policy assuring an adequate supply of different types of housing, and (d) to assure that all housing receives equitable delivery of public facilities.

Missing among the goals is any specific direction that low and moderate income housing be located throughout the jurisdiction. HUD does require that the housing work program, including any zoning and subdivision legislation prepared or revised using comprehensive planning assistance, must promote equal housing opportunity. However, there are no specifics as to how this should be done or mention of the broader question of equitable or "fair share" placement of low and moderate income housing. This omission seems quite surprising in view of the fact that the handbook was published in March 1972 after Dayton, Washington, D.C., and other fair share plans had become a reality. According to a recent NAHRO study,[43] initial housing elements submitted to HUD in compliance with the 1968 act requirement are, not surprisingly, disappoint-

[41] "Some First Returns on Planned Unit Development," Michael S. Levin, Barton-Aschman Associates, Rutgers University Conference, June 4, 1973.

[42] *Comprehensive Planning Assistance Requirements and Guidelines for a Grant,* March 1972 (CPM 6041.A).

[43] Housing in Metropolitan Areas: Roles and Responsibilities of Five Key Actors, Mary K. Nenno, NAHRO, 1973 at page 53.

ing. This background helps to explain why the comprehensive plan has often been used as a tool to impede the construction of low and moderate income housing throughout an area rather than further it.

Recommendation #13: HUD should require in the housing element of the comprehensive plan a strategy to achieve freedom of location for low and moderate income housing. Assuming our recommendations on community development housing are adopted, the comprehensive planning agency should coordinate its efforts with the agency administering the revenue sharing fund to assure a consistent community approach.

Metropolitan Housing Allocation Systems

Unless the system that produces subsidized housing is subjected to effective regional planning, HUD's project selection criteria (or its equivalent in the hands of localities) will merely give a gloss of formal rationality to a locational policy that is, for the most part, accidental. Regionalization, however, implies that local communities give up some measure of exclusive control over land-use and urban growth policy within their jurisdictions in return for the diminution of the developer's power over location of his projects. The courts and HUD have found ways of accomplishing the latter without completing the former.

Some movement toward this approach is evident in "fair share" housing plans adopted in some metropolitan areas. Attitudes toward these plans vary with the observer. Too some critics they are sophisticated wolves in sheeps' clothing—designed to "force" suburban communities to accept people they do not want. Some members of the black community point out that since four-fifths of the households in many metropolitan areas are no longer able to afford new unsubsidized housing, "fair share" plans are merely ways to rationalize the dilution of scarce housing subsidies that should go to central city residents. Planners point out that these approaches basically recognize that scarce resources must be allocated all the more deftly to make the greatest contribution to overcoming racial and economic separation in metropolitan areas, and that location is as critical as production in most communities.

In addition, "fair share" plans can assist the scattered site policy of locating and designing housing that departs from the sterile "projectitis" of denser central city areas.

The most advanced development of "fair share" housing plans has occurred under the auspices of the Miami Valley Regional Planning Commission in Dayton, Ohio.[44] The commission, basing its plan on the overall need for lower income housing in its region, allocated over 14,000 units in a five-county area. Importantly, the Miami Valley plan also sets limits on the number of subsidized units each area of the region would be required to absorb, and the commission has prevented development from taking place in one community that had already exceeded its allocation. It has aggressively used its power to coordinate Federal programs, granted under Federal legislation and regulations of the Office of Management and Budget (Circular A-95), to condition approval of a community's Federal open-space grant on the acceptance by it of subsidized housing.

The Metropolitan Council (Minneapolis-St. Paul) developed a housing allocation plan to guide the development of lower income housing. The plan assigns priorities to areas that have an adequate range of services, such as sewers, shopping, employment opportunities, mass transit, and highways. Low priorities were assigned to rural and undeveloped areas. Implicit in this approach is the goal of assigning housing obligations to those communities with the best fiscal base for absorbing new lower income residents. The Metropolitan Council may ultimately be aided in its program by the unique system for regionalizing the tax base, discussed in the first section of this paper.

Budget Bureau Circular A-95 is an outgrowth of legislation that reflected the view of Congress that proliferating Federal categorical grants should be subject to some areawide overview by an agency with comprehensive planning capability. The review under the statute[45] is concerned with "the extent to which the project is consistent with comprehensive planning developed or in the process of development for the metropolitan area, and the extent to which such

[44] Although the Dayton example has received the most publicity because it is in the implementation phase, different approaches have been taken in other metropolitan areas. These are described in Brooks, M. "Lower Income Housing: the Planners' Response" (American Society of Planning Officials 1972). p. 23ff.

[45] Sec. 204 of the Demonstration Cities and Metropolitan Development Act of 1966 as amended, 80 Stat. 1262; 81 Stat. 108. Regulations under A-95 are based on Title IV of the Intergovernmental Cooperation Act of 1968, 82 Stat. 1103.

project contributes to the fulfillment of such planning." The federally assisted projects that are the subject of this review generally include housing and urban development and open space land projects, planning or construction of hospitals, airports, libraries, water supply and distribution facilities, waste treatment works, highways, transportation facilities, law enforcement facilities, and water development and land conservation projects. Water and sewer waste treatment facilities have drawn active attention, and the regulation has been broadened to include civil rights as well as planning, aesthetic, and environmental considerations.

This system is embryonic but does enable a regional commission to delay or prevent Federal funding of a project that will reinforce patterns of racial and economic segregation in a metropolitan area. For example, if a locality has been financing an exclusionary pattern of urban growth with the use of Federal water and sewer facility grants, a regional review might condition such grants on the acceptance by that locality of some subsidized housing. The likelihood that this will happen depends on who controls the regional review.

Unfortunately, minority interests are seldom represented on these agencies, whether they are regional commissions or councils of government. Active review to determine whether a balanced local growth policy is being followed is the exception rather than the rule.

Ideally, regional reviews ought to prevent the "eviction" of suburban minority households through public action or rezonings that stimulate private development. It is not unknown for some suburban communities to regard minority enclaves as the most "suitable" areas for commercial and other nonresidential development, or appropriate sites for public buildings or roads.

The proposed Better Communities Act has left Circular A-95 in limbo. A-95 was premised on the need for better coordination of categorical programs. With the merger of categories under special revenue sharing or block grants the question arises as to what role remains for A-95. If each community is entitled to some amount of community development and housing funds, and very little Federal guidance or control is imposed on the purposes for which those funds are used, the lack of regional coordination will carry no penalty in the loss of funds. It may follow that there will be less regional coordination or less effective regional planning. (There is a certain "go it alone" flavor to special revenue sharing.)

For the purposes of this analysis, the allocation of Federal housing subsidies in any form, particularly if separation from a special revenue sharing, should benefit those metropolitan areas that have developed an effective "fair share" approach as the result of State legislation or voluntary agreements.

Recommendation #14: Regardless of the future of A-95, HUD should propose legislation allocating housing subsidies to further metropolitan "fair share" plans. (See related recommendation #13.)

Housing Allowance Programs and Dispersal Strategy

One of the immediate surface attractions of a subsidy to needy households to enable them to seek shelter in the existing, less expensive stock is the prospect of making such households "invisible" in the local political life of a community, and satisfying their needs in already built-up areas. This, in effect, supposedly sidesteps the controversial land use control issue as it applies to the construction of new housing.

The following questions must be raised, however, about the potential "dispersal" effects of a housing allowance program:

1. The majority of persons who might benefit from such a program could be persons in standard housing who now pay too much for such housing, and who will not wish to move. This amounts to an income transfer with few spatial implications or impacts on residential mobility.

2. There is a possibility that the universe of actual participants in such a program, as distinct from the universe of eligible participants, may be a more dependent, less "pioneering" group of people who will not be inclined to leave "traditional" residential areas. The self-selection process thus may eliminate more mobile and venturesome households, reducing the dispersal impact.

Assuming, however, that the participants will be inclined to be mobile, for whatever reason, the following potential constraints on such mobility will require special attention.

Dual Housing Market: The tendency of private real estate brokers to "steer" black beneficiaries to racially concentrated areas—or areas undergoing rapid racial change—could convert the program into a "block-busting" tool similar to the special risk section 223 program in Detroit. This will require strong Title VIII enforcement by the Justice Department.

Information or Escort Services: The beneficiary group may tend to be relatively uninformed about housing vacancies.

No Local Option: Federal law and regulations should provide that benefits may flow under the program unrestrained by any requirement of local approval. In other words, the kind of restraints placed on the operation of the rent supplement program, and almost extended to the sections 235 and 236 programs in the committee-approved 1972 housing legislation in the House of Representatives, would seriously undercut a housing allowance program.

Code Enforcement: To avoid in effect subsidizing substandard housing, some code enforcement mechanisms are frequently suggested as an essential corollary to a housing allowance program. Such a code enforcement program might involve the certification of a locality as a whole (which bears similarity to the old "workable program" approach) or a more finely tuned system of unit inspections or spot-checks. The possibility of local frustration of a housing allowance program—that is, an effort to prevent its operation within a jurisdiction—is implied by any local control over a corollary code enforcement activity. For example, a locality might desire to avoid certification making housing within it "off limits" to the beneficiaries of housing allowances. The design of any such program must take account of this possibility.

Recommendation #15: It is highly unlikely that housing allowances, without corollary administrative mechanisms to deal with the foregoing constraints, will significantly enhance residential mobility in metropolitan areas.

Federal Initiatives—Other Agencies

This portion of the report concerns initiatives by other agencies of the federal government that may be stimulated, supported, or altered by HUD representations to those agencies.

The first area concerns achieving a better relationship between the location of housing and jobs, including private sector jobs and government jobs.

Private Sector Jobs

Section 703(a) of Title VII of the Civil Rights Act of 1964 makes it unlawful for an employer to engage in discriminatory employment practices. The Supreme Court has held that any employment practice that has a disparate impact on minority workers constitutes a prima facie violation of section 703(a) and places the burden of proving nondiscrimination on the employer.[46]

The transfer of an employer's facilities could constitute a prima facie violation of title VII if (a) the community from which an employer moves has a higher percentage of minority workers than the community to which he moves, (b) the transfer affects the employment situation of the employer's minority workers more adversely than it affects his remaining workers, and (c) the employer fails to take measures to correct such a disparate effect.

When an employer moves to an area with a lower percentage of minority workers than that from which he came, he may in effect be diminishing the pool of available minority workers depending on the location. He therefore decreases the employment opportunities for minority workers while increasing opportunities for nonminority workers.

More specifically, an employer under the law has a duty of fair recruitment. Locating a plant in an area with few minority residents gives rise to minority recruiting problems. Normal recruiting patterns tend to confine notice of job vacancies to those who reside and work in an area. Unless an employer makes special efforts to institute a minority recruiting program, he will have failed in his duty of fair recruitment.

A transfer may also have a disparate effect on the employer's present minority workers if the ratio of minority employees who are unable to continue employment with the company to those minorities who are able to move is higher than the ratio of whites who are unable to move to those whites who do move. In the conventional employment situation there is this disparate effect: management, which is largely nonminority, adjusts to the transfer easily; indeed, management personnel may live in the area to which the facility is transferred. Other personnel, largely minority, are frequently unable to follow the relocation; commuting may be too difficult, moving may be too costly, or minorities may be shut out

[46] *Griggs v. Duke Power Co.,* 91 S. Ct. 849 (1971).

from suburbia by racial attitudes or by restrictive land use laws. Thus, unless the relocating employer arranges for his minority employees to continue employment, he will in effect be discharging employees on the basis of race.

Title VII is not restricted to eradicating practices that are intentionally discriminatory. Title VII deals with the consequences of an employer's action, not with his motivation. In the words of Chief Justice Burger, title VII condemns "practices that are fair in form but discriminatory in operation." The neutrality of the plant relocation process should not save it from illegality if its consequences are to restrict minority employment.

It should be noted also that the National Labor Relations Board has dealt firmly with the corporate relocation problem. An employer who relocates in order to avoid a union commits an unfair labor practice.[47] An employer who is prohibited from relocating to avoid a union should not be free to relocate his facilities away from minority workers.

If a prima facie violation of title VII is shown to be involved in a proposed plant relocation, an employer may defend the decision by showing an "overriding legitimate business purpose." [48] Corporate moves to suburban locations motivated by the desire of management officials to locate their offices closer to their homes, however, is not a legitimate business purpose in this regard because a distinction should be made between business "convenience" and business "necessity." The other often-asserted reasons (real estate tax benefits, transportation access, space requirements, etc.) do not justify a failure to take steps to assure that the risk of exclusion of minorities from employment is avoided or minimized.

What an employer should do to avoid or minimize a discriminatory impact depends on the facts of a given situation. Section 706(g) of the act provides that when a court finds that an employer is engaging in an unlawful employment practice, it should "order such affirmative action as may be appropriate."

These remedies, insofar as the subject of this paper is concerned, are not likely to include the return of a plant to the central city or the cancellation of a plant relocation. They instead would focus on the housing and transportation of the workers. In this connection, moving and relocation expenses might be appropriate, as would assistance in the search for housing, loans to assist in the down payment on houses, and other subsidies that would assist in improving the availability of housing for the workforce.

It should be noted that although title VII protects only the minority workforce (actual or potential), private employers made conscious of this particular problem would be inclined to offer assistance to the entire workforce—including lower income whites—who wished to follow the job to a new location.

This analysis is not news to the Equal Employment Opportunity Commission.[49] The EEOC, which administers the act, has published guidelines for employer action with respect to testing, sex discrimination, and other employment practices.[50]

Its failure to act in this area may result from a lack of expertise with respect to suburban housing patterns, an expertise that HUD may be able to provide.

Recommendation #16. The Secretary of HUD should recommend to the EEOC that it publish guidelines for employers with respect to the discriminatory impact of job relocation to exclusionary areas, with an offer to assist in the preparation of such guidelines.

Federal Facility Location

Under Executive Order 11512 (February 27, 1970), President Nixon instructed the executive branch, and particularly the General Services Administration, to take into account important factors in the acquisition, assignment, and use of Federal space and facilities. Among the criteria to be considered are the "availability of adequate low and moderate income housing, adequate access from other areas of the urban center," and "the impact a selection will have on improving social and economic conditions in the area." To carry out the purposes of the order, GSA has entered into a memorandum of understanding with HUD under which it agrees to develop, where needed, "an affirmative action plan de-

[47] *NLRB* v. *Lewis*, 246 F. 2d 886 (9th Cir. 1957).

[48] *Robinson* v. *Lorillard Corp.*, 444 F. 2d 791 (4th Cir. 1971).

[49] "It just may be that the physical removal of jobs beyond the reach of minority workers is likewise a violation of Title VII, by bringing about a foreseeable discriminatory effect. I fully intend to investigate this possibility with my General Counsel." From a speech by William H. Brown III, Chairman, U.S. Equal Employment Opportunity Commission, entitled "Corporate Location and the Urban Crisis" in December 1970, reprinted in "Open or Closed Suburbs: Corporate Location and the Urban Crisis" (Suburban Action Institute 1971), p. 15.

[50] See EEOC Guidelines on Sex Discrimination, 29 C.F.R. 1604 on Employee Selection Procedures, 29 C.F.R. 1607.

signed to insure that an adequate supply" of "low and moderate income housing on a nondiscriminatory basis will be available" before a Federal facility is to be occupied or within 6 months thereafter.

Relocated Federal facilities in the area of Baltimore, Washington, Chicago, and Brookhaven, N.Y., have drawn critical attention in connection with this Executive order. It is well known that minorities are disproportionately represented in the lower ranks of the government and least able to follow jobs that are relocated from central cities to the suburbs. Thus a decision to relocate a facility can in effect be a decision to fire even those minority employees and to substitute whites who have a wider choice of housing.

But the problem is not limited to minorities. Lower income whites may increasingly find their ability to move nearer to suburban jobs severely limited by the rising cost of housing. In the Brookhaven case a Federal court declined to enjoin the completion of a huge Internal Revenue Service Center but, noting the inadequacy of housing for the Center's workforce, the court did enjoin the Federal Government from disposing of nearby surplus Federal land until the government developed an affirmative action plan to assure enough housing for low income and minority groups.[51]

The economic benefits to a community that obtains Federal facilities can be large, especially in connection with leased facilities. Arlington, Va., for example, realized an estimated tax base benefit of $20 million from the leasing by the Federal Government of 4.2 million square feet (compared to about 5.9 million in the District of Columbia) at a time when that jurisdiction in northern Virginia was the only governmental unit in the metropolitan area that made no provision for increasing the supply of low and moderate income housing.[52]

If the question of leased space is viewed only in the context of the effects on employees, the location or relocation of Federal facilities in Arlington, depending on transportation facilities, may or may not be discriminatory. But we believe that the Federal Government should not confer tax base benefits—primary or secondary—on localities that lack affirmative housing policies.

[51] *Brookhaven Housing Coalition* v. *Kunzig*, 341 F. Supp. 1026 (1972).

[52] Cassidy, R., "GSA Plays The Suburban Game On a Grand Scale," *City Magazine*, 12 (Fall 1971).

The difficulties of complying with Executive Order 11512 in suburban areas suggests that GSA may in effect be turning back to the central city in the location of Federal facilities. The GSA Public Buildings Service recently directed that a quantified procedure be formulated that could be applied nationally to the evaluation of sites for Federal buildings. Such a procedure has been developed and recently adopted for use.[53] This Area Delineation and Site Evaluation Model may in effect put suburban locations "off limits" for future Federal facilities. In so doing, it may in effect confess the inability of the Federal Government to exercise affirmative action to alter exclusionary local policy with respect to lower income housing.

If this is so, there will be no "leverage" to free up suburban land use controls implicit in the location of Federal facilities. There will be considerable leverage with respect to the redevelopment of central cities, however, as well as some possible reinforcement of racial concentrations.

The implications for HUD policies of this potential major change in GSA policy should be fully evaluated and made public. If this reorientation back to central cities can be articulated as a governmental policy, it may have marked influence on the policies of EEOC as discussed in the preceding subsection.

The public agencies concerned with this aspect of public policy are not well apprised of this apparent shift in government policy.

Recommendation #17: The Secretary of HUD should request of the GSA Administration an analysis of the implications of the Area Delineation and Site Evaluation Model with regard to suburban locations and make such an analysis available to local renewal agencies and regional planning agencies.

National Land Use Policy Act

New communities or other large scale planned forms of urban development will not channel the anticipated population growth in socially and environmentally sensitive patterns unless States reform their existing system of land use controls. In recognition of this, President Nixon in 1971 recommended enactment of the "National Land Use Policy Act of 1971." In transmitting his earlier message on the environment to the Congress, the President observed:

[53] Fuller, S. "Social and Economic Factors in Federal Building Location Decisions: Implementing an Executive Order," 4 *Growth and Change* 43 (Univ. of Kentucky, April 1973).

> While most land use decisions will continue to be made at the local level, we must draw upon the basic authority of State government to deal with land use issues which spill over local jurisdictional boundaries. The States are uniquely qualified to effect the institutional reform that is so badly needed, for they are closer to the local problems than is the Federal Government and yet removed enough from local tax and other pressures to represent the broader *regional interests of the public*. Federal programs which influence major land use decisions can thereby fit into a coherent pattern.[54] [Emphasis added.]

After amendment in committee, the bill ultimately became the Land Use Policy and Planning Assistance Act of 1972 (S.632), and passed the Senate but died in the House of Representatives.

A number of land use policy and planning bills are before this session of Congress. They are:

- S.268, as introduced by Senator Henry M. Jackson and essentially similar to S.632 that passed the Senate in 1972.
- S.924, the administration bill, similar to the Jackson bill except for the administration's proposed sanctions (which were eliminated from the 1972 bill during debate on the Senate floor).
- H.R. 91, introduced by Rep. Charles E. Bennett, which is far less detailed than the Senate bills.

Hearings on the Senate bills have been completed by the Interior Committee and floor action is expected soon on S.268. The House, where land use legislation was reported from committee but never reached the floor in 1972, is likely to consider some kind of bill before the end of the year. The President, in his latest message on the environment, has given high priority to land use legislation.

All of these bills originally provided for grants to the States for the development and implementation of a system of land use controls directed to areas of critical environmental concern, areas impacted by key facilities, large scale development, and land uses of regional benefit. It is our understanding that the concept of encouraging "land use of regional benefit" has been eliminated from S.268 to be reported shortly to the Senate, a crucial omission from the standpoint of HUD. Although the final draft of the bill as reported was not available on June 8, it is our understanding that the regional benefit concept has been limited to "public facilities and utilities"—to exclude housing that may be required to meet regional needs. Subsidized housing very likely would not meet the definition of "public facility or utility" under S.268, such land uses probably being limited to solid waste disposal or sewage treatment facilities.

Closely related is a bill introduced by Senator Edmund Muskie, S.792, to amend the Federal Water Pollution Control Act. The amendment would require State mechanisms to bar public or private development, other than single family residential construction, that does not meet Federal emission and effluent standards or which exceeds the capacity of existing or planned water supply, waste treatment, or transportation systems.

The administration bill from the beginning has been a "process-oriented" measure drafted by the Council on Environmental Quality and borrowing heavily from concepts in the tentative draft Model Land Development Code of the American Law Institute. Such process-oriented legislation would not prescribe or proscribe substantive uses of land—such as prohibiting the development of wetlands. It would simply require States to devise a method of regulating land in areas of critical environmental concern. The legislation assumes that better results will flow from better decisionmaking procedures, an assumption that Senator Muskie attacked vigorously in debate on the measure.

The administration's original approach (S.924) would encourage the States, under pain of losing Federal highway, airport, and recreation facility assistance funds, to reform land use regulatory procedures. Specifically, States would be required: (1) to identify and regulate the use of their "areas of critical environmental concern" (defined to include shore lands, flood plains, scenic and historic districts, and other ecologically valuable or fragile areas); (2) to develop a method for assuring that "development of regional benefit" is not unduly restricted or excluded by local governments; (3) to identify and control "areas impacted by key facilities" (such as major airports and highway interchanges); and (4) to develop a means to control large scale development.

Senator Jackson's original 1971 proposal was more "planning-oriented" than "process-oriented." It would have provided Federal funds to States for planning and classifying land according to several uses, such as residential, commercial, industrial, agricultural, transportation, and recreation.

[54] President's Message on the Environment, February 8, 1971.

When the Senate passed the Land Use Policy and Planning Assistance Act in 1972, it adopted a previously worked out compromise between the comprehensive planning aspects of the initial Jackson bill and the process orientation of the administration bill. The Senate-passed bill, however, at Senator Muskie's insistence, struck out the notion of encouraging "land use and development of regional benefit" in debate on the Senate floor; a severely limited version of it has apparently been reported out in the latest version of the bill. The bill that will be considered by the Senate is still process-oriented, with a planning overlay.

It is fair to characterize all of these legislative proposals as conservationist and antidevelopment in basic orientation. However, any measure dealing with the regulation of land, as distinct from a "development policy," could be so labeled. Regulation of the use of privately owned land must be premised on the achievement of some public good. The public benefit, however, may be so distributed that it aids only a limited number of people; or the burdens placed on the use of land may unduly restrict the rights or opportunities of certain people in relation to the public benefit being sought.

The question arises as to whether these bills would place reasonable burdens on the housing opportunities of metropolitan lower income households in relation to the public benefits accruing from the augmented control over such development. We believe that S.268 as reported will place unreasonable burdens on housing generally and lower income housing in particular.

The administration's approach of encouraging States to develop a method for overcoming the local exclusion of developments "of regional use and benefit" could have ultimately aided the larger scale balanced residential developments discussed in the third section of this paper and could have aided any subsidized housing project if such projects were defined as of regional use and benefit (as in the A.L.I. model code). The Massachusetts Zoning Appeals law, discussed in the first section, is an example of a State method that clearly would meet this test of regulatory reform. It should be understood, however, that both the administration and Jackson bills were so procedural in orientation that the Florida law, also described in the first section would also meet the test even though the application of the "regional impact" portions of the Florida law to subsidized housing is tenuous at best (it would apparently apply to large scale housing developments, whether subsidized or not).

In any event, the potential application of the "development of regional use and benefit" concept to housing of any sort is completely eliminated in S.268 to be reported to the Senate.

The bill also singles out large scale development (e.g., a new community) for special attention, giving it the burden of potential prohibition to protect environmental values but also enabling such development proposals to overcome a locally adverse zoning decision. There is, however, no provision in the bill to encourage a more equitable development policy in the large scale projects where "balanced growth" is likely to be more feasible. In effect, S.268 may encourage the imposition of new regulatory burdens on larger scale developments, while letting the small, conventional piecemeal subdivision continue to ravage the land.

The "lead agency" under the Jackson and administration bills is the Department of the Interior, as the result of a White House decision in 1971. Since that time HUD has had a relatively "low profile" with respect to the consideration of this legislation.

At this writing, a "clean bill," S.268, was due to be reported out of the Senate Interior Committee. Our information indicates that the interests of HUD may be negatively affected by the removal or limitation of the regional benefit concept and the bill's predisposition to encourage far greater restraints on larger scale development than small scale development.

In addition, it is not clear that the bill recognizes the importance of housing (and particularly lower income housing) as a major user of land subject to new regulation. No State land use plan can be regarded as even minimally adequate unless it is accompanied by projections of the housing needed to satisfy anticipated needs in a region. Without at least this component, new State land use regulations may do little more than respond to the most negative "antigrowth" posture of suburban areas, adding to the spiraling cost of new housing.

Recommendation #18: The Department of Housing and Urban Development should analyze S.268 to determine its impact on housing needs and, specifically, to assure that the bill is revised so that:

1. The law requires State housing need planning on a regional basis as part of a State land use plan;

2. The Secretary of HUD takes a leading role in assuring compliance by States with respect to this standard;

3. The concept of encouraging developments of regional benefit is retained, with reference at least to housing required to meet regional needs as projected by the State plan.

Home Finance Industry

Even with a large scale campaign of housing subsidies in one form or another, the vast majority of the new housing stock and the refinancing of the older stock is provided by "conventional sources." The conventional home finance industry is only indirectly influenced by HUD.

In June 1971, shortly after the President's statement relative to equal housing opportunities, then Attorney General Mitchell acknowledged the existence of racial discrimination by mortgage lenders and suggested that this be dealt with by "the regulatory bodies that control these institutions."[55]

According to the Social Science Panel of the National Academy of Sciences Advisory Committee to HUD, "mortgage financing institutions have had separate lending policies for blacks and for whites. They have been timid in developing policies for realizing mixed residential areas."[56]

Although the Federal Deposit Insurance Corporation has recently proposed regulations on Fair Housing Lending Practices to prohibit "redlining" and to require the keeping of racial data by insured institutions, it—and the Federal Home Loan Bank Board—have not yet begun to examine the potential role they might play in assuring that a more equitable housing and urban growth policy develops in metropolitan areas. This would require that lenders obtain nondiscrimination assurances from builders and developers and, in the cases of concerns that have been found in violation of Federal, State, or local laws, decline to extend financing; or that lenders require specific fair housing marketing plans, and that lenders develop their own affirmative marketing program to attract minority customers.

Beyond these steps to assure racial nondiscrimination, however, lies the more complicated question of whether local lending institutions can be effective conduits for subsidies to lower income households generally. Few have participated, for example, in the Home Ownership Opportunity Program under the 1970 Housing Act. Yet the racial and economic stratification of large metropolitan areas suggests that the existing regulated private financing system can no longer remain entirely "neutral" in the face of mounting land and housing prices in sprawling suburban areas and the abandonment of housing and land in some central cities. The redirection of investment into underutilized but adequately serviced central city land could relieve some of the growth pressures on the urban fringe. Financing requirements or incentives might be devised to assure that fringe growth takes place in cluster-type developments that do not waste land and capital for sewers, water lines, roads, and other community facilities.

This is clearly an uncharted sea. The conventional home finance industry has operated in pursuit of functional objectives unrelated to the spatial consequences of its activities. Some questions seem pertinent. Should the Federal Government continue to permit mortgage finance institutions to make loans for expensive housing for well-to-do households in areas that exclude lower income households? Would a requirement that a certain portion of an institution's loan portfolio be set aside for lower income loans result in a better spatial distribution of such households? Should such institutions be required to impose environmental considerations on development loans? Can a metropolitan "pooling" of conventional institutions reduce the exposure of individual institutions on high risk loans in the central city and second mortgage loans to lower income house buyers or rental housing developers in suburban areas?

To ask such questions, to which answers are not readily available, is to suggest that far too little attention has been paid to the manner in which the conventional home finance industry might become a more active participant in assuring a more equitable form of residential growth.

Recommendation #19: The Secretary of HUD should request the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, the Federal Savings and Loan Insurance Corporation, and other relevant Federal chartering, insuring, and regulating agencies to determine whether legislation or administrative regulation can feasibly encourage more favorable conven-

[55] Hearings Before U.S. Commission on Civil Rights, June 16, 1971, p. 362.

[56] "Segregation in Residential Areas" (National Academy of Sciences, Washington, D.C. 1973), p. 19.

tional financing for lower income home buyers and renters in desirable neighborhoods.

The Federal Highway Administration and the Uniform Relocation Act

The Federal highway program has had enormous impact on land use patterns. The interstate program, in particular, with its high ratio of Federal funding, has promoted the development of automobile-oriented suburban and exurban communities.

In so doing, it has contributed to the decline of the economic vitality of the central city and stimulated rapid population dispersal in low density developments on the urban fringe. By providing accessibility to the fringe areas and in effect creating land values where little existed, on the one hand, and taking property off the tax rolls in the central city, on the other, this Federal program generated antagonism from central city residents.

This was particularly the case with respect to the displacement of disadvantaged central city residents who were precluded from moving to suburban localities made more accessible by the highways that displaced them.

Until the enactment of the Federal Aid Highway Act of 1970 and the Uniform Relocation Assistance and Real Property Acquisition Act of 1970, State highway departments were making assurances as to replacement housing that were based on surveys of housing stock within the city. Unfortunately, housing vacancies recorded, or new units contemplated at the time of the survey did not assure their availability at the time of displacement. In addition, this "anticipated" housing stock theory of replacement housing was dependent on the decisions of private housing producers to provide housing within the means of displacees. Generally speaking, the public housing program could not be consistently relied upon as a relocation resource. This was due to competing demands on these resources by displacees from other public works programs, and because, in many instances, highway displacees had incomes too high to permit them to live in public housing and yet too low to enable them to find housing produced by the private market at rents they could afford.

These gaps with respect to relocation housing were filled to some degree by the 1970 amendment to section 101 of title 23, which expanded the definition of highway "construction" to include "relocation assistance . . . acquisition of replacement housing sites, and acquisition and rehabilitation, relocation and construction of replacement housing." This should be read with "houser of last resort" provisions of the Uniform Relocation Assistance and Property Acquisition Act of 1970.[57] In essence, these two acts provide that unless adequate replacement housing is made available within a reasonable time prior to displacement, the project causing the displacement cannot go forward. It would seem that displacement problems caused by the highway program are effectively put to rest.

While time has not permitted extensive experience in providing replacement housing under the provisions of the foregoing laws, it appears that problems have arisen as to which agency is to take responsibility for providing for the construction or rehabilitation of such housing. With a few exceptions, highway departments are not in the housing development business and tend to look to the local renewal or housing agency of the affected locality to carry out a replacement housing program even if financed with highway funds. The local housing agencies, on the other hand, tend to be heavily occupied in carrying out their own programs and funding housing for those displaced by their own activities.

Perhaps one of the most effective approaches to meeting the mandate of the Uniform Relocation Assistance and Property Acquisition Act, and taking advantage of the additional funds for providing for replacement housing under the Federal Aid Highway Act, is through greater reliance on the private housing development industry. In effect, by taking advantage of the loans for planning replacement housing under section 215 of the Uniform Relocation Assistance and Property Acquisition Act, which loans can be made available to limited dividend housing sponsors, for "planning and obtaining federally insured mortgage financing . . . for housing for . . . displaced persons" the front-end costs of putting necessary housing packages together can be met. Then, to the extent that federally insured mortgage financing cannot produce housing and rents sufficiently low to accommodate the displaced families and individuals, highway funds authorized under section 101 of title 23 might be used to provide at one time the subsidy needed to make the housing economically feasible with regard to the displacees. This approach would both satisfy the needs of specific displacees at the time of displacement and would also provide for a replacement of "housing stock" from the

[57] P.L. 91–646, §§205(c)(3) and 206(a) and (b).

local inventory based on highway program activities.

Highway funds should be called on to a far greater extent than in the past to bear the true costs of the highway program, and to contribute to the placement of that housing in otherwise unavailable locations.

Although State highway departments may resist the idea, it appears to us that the Federal Aid Highway Act language already cited would permit the introduction of lower income housing into otherwise exclusionary urbanizing areas by the ancillary acquisition of sites for such replacement housing by highway departments. This could be done as part of the highway program itself [58] with appropriate administrative encouragement by the U.S. Department of Transportation.

[58] As a general proposition State law permits State highway departments to acquire land for replacement housing where such housing is required to permit the highway project to go forward. Even if they did not, however, the effect of Federal statutes is to require States to permit this activity as a condition to the receipt of Federal funds. See §221 of P.L. 91–646 and 42 U.S.C. §4630 and §4625.

This nascent power could enable the provision of needed housing sites in built-up areas as well, perhaps on platforms over the right of way.

The inclusion of the Federal aid highway program in the President's proposed Department of Community Development would facilitate a better "mesh" of these programs. In the meantime, however, HUD should stimulate appropriate initiatives by the Federal Highway Administrator.

Recommendation #20: The Secretary of HUD should request the Secretary of Transportation to report on the extent to which highway funds have been used for replacement housing and the extent to which regulations of the Department of Transportation can be revised to encourage the acquisition by highway departments of sites for replacement housing in suburban and central city areas.

Creating a National Market for Innovation in Building: Alternative Regulatory Mechanisms

By Steven R. Rivkin
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Summary

In recent years, Federal efforts in the field of building regulation have been, as discussed separately, scattered and far less effective than needed. Within the context of considerations previously suggested, this paper identifies three broad avenues by which stepped-up Federal participation in the regulatory process can realistically be achieved, each of which is subject to variation in specific machinery of administration and enforcement to accomplish particular objectives. The broad alternatives are as follows:

- Federal preemption of standards for products distributed in interstate commerce;
- Federal promulgation of a national building code to be administered by state enforcement agencies; and
- Federal coordination and certification of State regulatory programs.

In addition, an effort has been made to define a fourth alternative, representing an "amalgam" approach, by which the third avenue, Federal coordination and certification, would be initially adopted, with standby discretionary authority also provided along the lines of the first two approaches, for implementation as subsequently determined to be necessary. In the final section of this paper, a preliminary set of distinctions between the four alternatives are set forth, to be expanded and supplemented in a separate paper.

All four approaches will require the development of a central Federal authority for implementing the purpose of legislation. While the scale and volume of activity under each approach will require varying levels of appropriations and staff, a single responsible entity will have to be created. This entity is here conceived as an Administration, in all cases under a single responsible head. A status wholly separate from any existing government agency may be appropriate, for the purpose of insuring independence and visibility, or housing within a single government agency may be more desirable. While in the latter instance, location would be preferable within HUD, as the government department most centrally concerned and charged by Congress with specific tasks for increasing the Nation's housing supply, no recommendation here is made with respect to the question of overall independence. To a degree, organizational delegations will be a function of legislative strategy (i.e., which congressional committees have jurisdiction) as well as administrative considerations.

This paper identifies alternative legislative approaches to foster a national market for innovative technology in the construction industry. A separate paper describes the constitutional basis within which such legislation could be enacted, assesses the justification presently available and necessary to be assembled for such legislation, and discusses the practical factors that will bear on a choice among alternatives.

The Problem

Since the beginning of the century and before, localities in the United States have imposed regulations on the materials and methods used in construction of buildings, in the interests of protecting the public health, safety, and welfare. Long ago, State police powers were judicially sustained as superior to private property rights in establishing the basis for local control over building methods, materials, and design. Now the concern has shifted from too little regulation to too much, from too few controls to too many, at the sacrifice of untold opportunities to increase the supply and reduce the cost of building through technological innovation. "The web of restrictive building codes"—in the term often used to describe simultaneously both the multiplicity and the rigidity of building codes—is one factor, and an important one, that frustrates the achievement of national housing goals.

Hence, reducing diversity and facilitating change may now be a proper goal for public policy in building regulation. Because a central perspective is an essential key in achieving the widest acceptability for innovation and in forcing its pace, some role for Federal action is imperative. However, because of the vast scale on which regulation must be applied and the limited value of any one building subject to regulation, a role for local regulation must also be preserved. Thus a balance between centralism and localism must be struck. At the same time, a balance must also be found in the regulatory process between measures that serve the interests of achieving safety and predictability, on the one hand, as reflected in traditional approaches to building, and flexibility and innovation on the other.

Because existing codes are so highly developed, any new regulatory mechanisms and standards will encroach upon and supplement the existing regime of building regulation. Thus, three important issues must be successfully resolved:

1. What is the proper division of authority and functions between Federal and State/local authorities?

2. What is the proper balance to be struck between traditional (specification-type) codes and more venturesome "performance" standards?

3. At what pace can and should new standards-setting and enforcement mechanisms attempt to supplant existing regulatory processes?

These three considerations establish the conceptual framework within which the following analysis of alternative regulatory mechanisms must fit.

Alternative Regulatory Mechanisms

Summary and Overview: In recent years, Federal efforts in the field of building regulation have been, as discussed separately, scattered and far less effective than needed. Within the context of considerations previously suggested, this paper identifies three broad avenues by which stepped-up Federal participation in the regulatory process can realistically be achieved, each of which is subject to variation in specific machinery of administration and enforcement to accomplish particular objectives. The broad alternatives are as follows:

- Federal preemption of standards for products distributed in interstate commerce;
- Federal promulgation of a national building code to be administered by State enforcement agencies; and
- Federal coordination and certification of State regulatory programs.

In addition, an effort has been made to define a fourth alternative, representing an "amalgam" approach, by which the third avenue—Federal coordination and certification—would be initially adopted, with standby discretionary authority also provided along the lines of the first two approaches, for implementation as subsequently determined to be necessary. In the final section of this paper, a preliminary set of distinctions between the four alternatives will be set forth, to be expanded and supplemented in a separate paper.

All four approaches will require the development of a central Federal authority for implementing the purposes of legislation. While the scale and volume of activity under each approach will require varying levels of appropriations and staff, a single responsible entity will have to be created. This entity is here conceived as an Administration, in all cases under a single responsible head. A status wholly separate from any existing government agency may be appropriate for the purpose of insuring independence and visibility, or housing within a single government agency may be more desirable. While in the latter instance, location would be preferable within HUD, as the government department most centrally concerned and charged by Congress with specific tasks for increasing the Nation's housing supply, no recommendation here is made with respect to the question of overall independence. To a degree, organizational delegations will be a function of legislative strategy (i.e., deciding which congressional committees have jurisdiction) as well as administrative considerations, as will also be separately discussed.

Federal Preemption of Standards for Products in Commerce: An apt analogy for this approach is found in the Noise Control Act of 1972, Public Law 92–574, 86 Stat. 1234, 42 U.S.C. §§4901–4918, 49 U.S.C. §1431. By this act, Congress sought to:

> . . . establish a means for effective coordination of federal research and activities in noise control, to authorize the establishment of federal noise emission standards for products distributed in commerce, and to provide information to the public respecting the noise emission and noise reduction characteristics of such products. (Sec. 2(b))

The principal thrust of the legislation is the requirement that the Administrator of the Environmental Protection Agency must establish regulations, where feasible, governing noise emission of products on a specified list and may publish additional standards for any other product where he finds that such standards are "feasible and are requisite to protect the public health and welfare." (Sec. 6(a) and (b)). For such products (designated as "new products," to apply only to products manufactured after the effective date of the act), States and localities are prohibited from adopting or enforcing standards that vary from Federal standards, while their rights to impose other controls on environmental noise are unaffected.[1]

As explained in the Report of the Senate Public Works Committee urging passage of the bill, the line of Federal preemption in the Noise Control Act of 1972 is as follows:

> For any product manufactured after the effective date of an applicable federal standard, authority to establish noise emission standards for the product enforceable directly or indirectly against the manufacturer is preempted. States and cities, however, retain complete authority to establish and enforce limits on environmental noise through the licensing, regulation, or restriction of the use, operation or movement of a product, or concentration or combination of products. (*U.S. Code Cong. & Ad. News*, 92nd Cong., p. 4660)

The distinction recognized in the act—"between burdens which fall on the manufacturers of products in interstate commerce and burdens which may be imposed on the users of such products" (id.)—would not be directly applicable in building regulation, where manufacturers per se are not presently regulated locally, only the "user" —the builder or owner.

Nonetheless, the act's preemption of standard-setting for particular products is a helpful parallel with respect to such identifiable building "products" as manufactured buildings, components, or materials intended for a specific construction purpose. Thus, either by statute or by regulation pursuant to statute, a Federal regulatory standard would be established, it having been found that the particular product is fully adequate to protect life and safety when used in a prescribed fashion and that any local prohibition on such use would constitute a burden on commerce. This approach would be more intrusive on State regulation than the Noise Control Act provisions, in that State and local authorities would be preempted from prohibiting the use of such products for specific purposes, while permitted to establish other standards "not inconsistent with" Federal standards.

Effectively, this approach would "certify" the acceptability of particular products for particular uses. The list of products covered could be spelled out categorically by legislation or, preferably, left to the discretion of a competent Federal regulator or regulatory body subject to procedural safeguards under the Administrative Procedure Act (notice to interested parties, opportunity for hearing, judicial review, etc.) and aided by research and testing facilities. Whenever a Federal standard for a particular product (tailored to a particular use) had been issued, State or local regulations in conflict with such a standard in its area of applicability would be preempted.

Thus, the following might well be included as key provisions of Federal legislation enabling regulatory preemption on a product-by-product basis:

Sec. 1. Short Title: The act could be designated as the "Federal Building Products Standards Act of 197_."

Sec. 2. Statement of Congressional Finding and Policy: The section would express Congress' concern to develop wider opportunities for the introduction of modern building technology by creating a national mechanism to achieve testing and to set selective standards for building products in interstate commerce. While preserving the primary responsibility of the States to protect the safety and welfare of their citizens in building regulation matters, Federal action would be declared necessary to focus national concern for innovation in building, to foster the growth of a national marketplace for innovative construction materials and methods. Concentration of research and testing effort to perfect "performance standards" applicable to building technology would be identified as a national policy, and participation by industries, regulatory bodies, labor, consumers, and the general public in the process of setting Federal standards would be required.

Sec. 3. Office of Building Products Standards: The act would create an Office of Building Products Standards in HUD to implement its provisions. Basic rulemaking and administrative authority would be provided to an Administrator of

[1] "(e)(1) No state or political subdivision thereof may adopt or enforce—

(A) With respect to any new product for which a regulation has been prescribed by the Administrator under this section, any law or regulation which sets a limit on noise emissions from such new product and which is not identical to such regulation of the Administrator; or

(B) with respect to any component incorporated into such new product by the manufacturer of such product, any law or regulation setting a limit on noise emissions from such component when so incorporated.

(2) . . . [N]othing in this section precludes or denies the right of any state or political subdivision thereof to establish and enforce controls on environmental noise (or one of more sources thereof) through the licensing, regulation, or restriction of the use, operation, or movement of any product or combination of products." (Sec. 6(e))

the Office, appointed by the President and confirmed by the Senate.

Sec. 4. Definitions: The following would be among the key terms to be defined by the act:

(a) Commerce. The term "commerce" means trade, traffic, commerce, or transportation—

(1) between a place in a State and any place outside thereof, or

(2) which affects trade, traffic, commerce, or transportation described in subparagraph (1).

(b) Building Product. The term "product" means any manufactured article or good or component thereof distributed in commerce [or material, the preponderant value of which the Administrator has found to have been distributed in commerce during any 12-month period in the 5 years prior to the making of his determination].[2]

Sec. 5. Research, Investigation, Training and Other Activities: The Administrator would be authorized to conduct, and to procure from any source, research into building methods and technology and to investigate criteria by which the effectiveness of particular methods and technology can best be regulated within a performance approach. The Administrator also would be authorized to provide technical and financial assistance to other Federal, State and local agencies concerned with building technology, to disseminate information, to cooperate with other public agencies in research and development, and to provide for educational and training assistance for building regulatory personnel.

Sec. 6. Criteria for Building Regulation: This section would authorize the Administrator, on the basis of the research conducted pursuant to Sec. 5 and other sources, to publish and disseminate criteria for building regulation which, in the Administrator's judgment, will protect the public health and welfare. The Administrator also would be authorized to compile and publish other information pertinent to maintaining the health and safety of the public in building construction, such as standards governing the use and occupancy of buildings.

Sec. 7. Issuance of Building Products Standards: The Administrator would be (authorized to issue) (required to issue within a particular period of time after enactment)[3] regulations governing the use in construction of building products according to specific criteria which he has found protect the public health and safety with respect to the particular building product. The Administrator would be authorized in establishing such criteria to take into consideration the burdens upon commerce in terms of increased costs to consumers and users of more restrictive measures to protect the public health and safety. After promulgation of a relevant Federal Building Product Standard, States would be preempted from establishing or enforcing any other standard with respect to the use of such building product in accordance with the Federal standard, while State building regulations affecting other methods, materials, products, or aspects of construction would be unaffected.

Issuance of Building Products Standards shall be in accordance with procedures of the Administrative Procedure Act; the Administrator, however, may adopt provisions or standards set forth in codes promulgated by national code groups if he finds that such standards satisfy the substantive criteria of this act and have been adopted under procedures which have given diverse views a hearing and which indicate substantial agreement by interested persons.[4]

Sec. 8. Building Products Standard Advisory Committee: The Administrator would be authorized and empowered to appoint an Advisory Committee, empowered in turn to create subcommittees and task groups, to consult with the Administrator with respect to the issuance of any building product standard or any other function assigned to it by the Administrator. The Advisory Committee shall include among its members representatives of industry, labor, national code groups, academia, and consumers, but it shall not have any powers with respect to the issuance of building product standards other than the provision of advice to the Administrator.

Sec. 9. Labeling: This section would authorize the Administrator to establish requirements for labeling building products complying with Federal standards, by which attention would be

[2] The use of the term "material" within the definition of "product" creates the possibility that the Administrator's authority to issue regulations can be extended to basic construction materials, so long as they have been "manufactured" and moved preponderantly in interstate commerce. Thus, if it be a fact that most portland cement used in the United States is distributed in commerce, Federal power could reach standards for the use of concrete in building construction. (The precise definition of "product" is hence likely to be one of the most highly controverted aspects of this legislation.)

[3] The Administrator's statutory authority may be permissive or restricted with respect to the building products to be regulated, and the pace at which such standards shall be issued.

[4] By affording model code groups an opening themselves to write standards for consideration by the Administrator (assuming he finds substantial due process has been observed in their formation) an opportunity for significant cooperation between federal regulation and the code groups is created; thus the code groups themselves might be given a major impetus toward procedural and substantive reform.

called to the applicable standard with which such building product complies.

Sec. 10. Enforcement: The Administrator shall have the power to authorize investigations of manufacturing processes, at such times and under such conditions as he deems appropriate, to insure compliance with applicable Federal standards by manufacturers of building products. Such investigations may include visits to construction sites to insure compliance with applicable Federal standards insofar as they relate to transportation of building products to the site. Such powers shall not preclude inspections by State or local enforcement personnel not inconsistent with this act. Any aggrieved party and the Administrator shall have a right to seek injunctive relief from a U.S. District Court from violations of the Act as he determines necessary to protect the public health and welfare, in accordance with due process.[5]

Sec. 11. Judicial Review of Standards: Within 90 days after the promulgation of a regulation or standard under the act, an interested person may petition for review of the Administrator's decision in the Court of Appeals for the District of Columbia.

Sec. 12. Grants in Support of State Enforcement Programs: In order to effectuate the purposes of this act, and more particularly, to facilitate adoption of Federal standards by State regulatory mechanisms, the Administrator would be authorized to make planning and program grants to State and local building control agencies.

Sec. 13. Incentive Purchasing: The Administrator shall have a fund from which other agencies of the Federal Government may receive credits to facilitate purchase of building products (even if noncompetitive in price terms) that are certified as "significant innovations in building" by the Administrator, subject to such criteria as he deems appropriate, to create initial market demand for federally certified products.[6]

[5] Enforcement through judicial process need not be time-consuming nor costly. Where the issue of state or local non-compliance with a duly promulgated standard is raised, the issues may be ripe for summary judgment without extensive fact finding, and if the parties are in agreement on the nature of the issues between them, necessary facts can be introduced by affidavit. Normal court powers of discovery (e.g., subpoenas) and sanctions for non-compliance would be available.

[6] This power would be in addition or complementary to funds for direct R&D for innovative building, in the budgets of the Administration or other federal agencies.

Sec. 14. Appropriations: In brief, this approach to "federalizing" building regulation would be selective and progressive, emphasizing only the extension of particular Federal standards for proven areas of national importance. State regulation would not be displaced, except to the extent it conflicts with particular Federal standards. Enforcement would remain a State and local responsibility, but "any aggrieved party," as well as the Administrator, would have a ready avenue of judicial relief. Finally, the Administrator's power to adopt provisions of model code groups could produce greater adaptability by the code groups to building code reform.

Promulgation of a Federal Building Code Enforced by the States: At the outset of the analysis of this alternative and of the additional Federal-coordination approach next discussed, it should be emphasized that some form of partnership approach is considered essential. This is so, by contrast to a totally federalized process, for both practical and political reasons. The vast scale on which federalized building regulation would have to apply, displacing extensive building regulation bureaucracies of States and localities, would make complete displacement of State powers impractical, even though a completely Federal process might well be constitutionally defensible. By the same considerations, any overlay of Federal standards upon State enforcement mechanisms must be undertaken with a view to making a partnership approach effective.

Assuming sound comprehensive Federal codes could be devised, it would be unlikely that such codes could be fashioned from whole cloth by any particular target date. Thus, the vastness of the project would make staged introduction advisable. It should be pointed out that the coverage of a Federal code would have to be all-inclusive, rather than merely selective, to protect against shoddy construction, in addition to opening up opportunities for new products and methods.

A Federal building code—here defined as an aggregate of one or more standards and permitted uses with which construction of buildings must comply in particular configurations (as distinguished from the product approach previously discussed)—can be made applicable to the States on either a mandatory or a "leveraged" basis. Mandatory applicability could be achieved by a congressional declaration that all construction of a particular kind is affected by a national interest. Three examples may suffice to illustrate the fashion in which comprehensive standards have been universally applied, although the drafting of a building code's applicability would require careful and unique attention.

- In the Fair Labor Standards Act of 1938, standards promulgated by the Administrator of the Wage and Hour Division of the Department of Labor are applicable to all employees "engaged in commerce or in the production of goods for commerce" (29 U.S.C. §206) with exemptions defined by statute with respect to the dollar volume of goods sold in intrastate commerce and by regulation of the Administrator (29 U.S.C. §213).
- In the Meat Inspection Act, 21 U.S.C. §§601–695, all meat-slaughtering establishments whose products "are to be used in commerce" are affected (21 U.S.C. §603), but products regulated are flatly defined to be those "either in interstate or foreign commerce or [that] substantially effect such commerce" (21 U.S.C. §602), e.g., by competing with those products that are in commerce.
- Similarly, in the Metal and Nonmetallic Mine Safety Act, 30 U.S.C. §§721–740, "Each mine the products of which regularly enter commerce, or the operations of which affect commerce" are covered, although the Secretary of Agriculture may by published rules decline to exercise authority with respect to a class of mines where the effect "is not sufficiently substantial to warrant the exercise of jurisdiction . . . and the record of injuries and accidents . . . warrants such a declination of jurisdiction." (30 U.S.C. §722(a) and (b))

Selection of a mandatory scope of Federal applicability would depend on economic analyses of the construction industry in the United States by value, by proportion of value added at the site and within the State in which the site is located, and by types of construction—upon which practical judgments must be made as to the extent to which a Federal standard is desired to apply. Nonetheless, certain triggers for Federal jurisdiction (substantiated constitutionally in a separate paper) can be suggested. The most comprehensive basis for jurisdiction would be the finding that all construction not undertaken by the owner for his own occupancy is a national concern, because it exerts effect on interstate commerce either directly (as the largest component of a typical family budget) or indirectly (in that local building "casts a shadow" on interstate commerce). Alternatively, all construction to which Federal funds have been committed—either directly or through a Federal mortgage guaranty, etc.—could be made subject to Federal standards only. Additionally, Federal regulation could exempt from any definition of applicability certain classes of construction, either statutorily defined or defined by regulation.

"Leverage" applicability could be achieved by a "carrot and stick" approach in the use of Federal funds, presently typified by a number of pending bills establishing a Federal role in land use planning and policy formation. The Administration bill (S. 924 and H.R. 4862) couples the inducement of Federal program grants with "crossover" sanctions, by which States are penalized in graduated amounts—from 7 percent to 21 percent of otherwise available funds—taken from relevant programs for highways, airport construction, and conservation programs. In the building regulation context, the Federal carrot would be the grant of funds to support training and enforcement by State agencies (a useful inducement, whether or not States have yet adopted statewide enforcement mechanisms) and the stick could be the withholding of funds for urban renewal, model cities, etc., or cutbacks in the availability of federally guaranteed building programs.[7]

The foregoing assessment of the potential applicability of a Federal building code sets the key framework of partnership approaches in which the Federal standard-setting role would predominate. More specifically, the following provisions would have to be embodied in any legislation.

Congressional Findings and Policy: As previously indicated with respect to a product standard approach, legislation would require a finding of urgent need for development of a Federal role in building regulation, articulated in terms of the economic benefit to the Nation of a national market for innovative technology in order to achieve the goals of earlier housing acts. Additionally, legislation would stipulate a role for the States in enforcement of federally defined standards and a commitment for Federal

[7] The Occupation Safety and Health Act, 29 U.S.C. §651–678, which vests standard-setting powers in an Administration in the Department of Labor to deal with conditions of employment nationwide, provides an interesting two-stage model. Without displacing state authority in areas where no federal standard has been set, the act provides for the setting of mandatory federal standards overriding all inconsistent state standards. However, States are encouraged and assisted in developing their own occupational health and safety programs, which when embodied in a plan accepted by the Secretary of Labor, displace ("preempt") federal standards in the same field of applicability. 29 U.S.C. §667.

assistance to States to aid in the enforcement process.

Regulatory Mechanisms: A Federal instrumentality for promulgating codes would be required to be established, and machinery for cooperation and coordination with the States would be needed. At the Federal level, a mechanism similar to the Building Products Standards Administration previously suggested would be appropriate, under the direction of an Administrator, with the assistance of staff, research facilities, and a representative advisory committee. The task of promulgating comprehensive codes would require setting a floor, as well as raising the ceiling, for construction standards. A mechanism for coordinating State enforcement would also be needed, for which three elements in particular would have to be spelled out:

1. A program of Federal technical training and financial assistance that would facilitate integration of State and local enforcement machinery with Federal standards.

2. A set of criteria for the upgrading of State enforcement machinery, embracing the establishment in all States of statewide enforcement mechanisms (with subdelegation to local authorities possible); procedures for expeditious processing of building applications and criteria for meaningful judicial review in State or Federal courts; provisions for making discretionary judgments assigned to State agencies by Federal authority for such questions as application, timing, and exemption from Federal standards; and provisions for upgrading the professionalism of State and local enforcement personnel.

3. A mechanism for accomplishing the review of State performance of functions assigned by Federal statute and providing a hearing for State viewpoints—especially necessary to secure procedural fairness where the imposition of Federal sanctions for noncompliance will be involved. If mandatory Federal codes are developed, an advisory board consisting of a limited number of rotating appointments among nominees by State governors would be an appropriate source of general advice, so long as control over Federal decisionmaking was negated. For a "leveraged" approach, adoption of a grant application procedure would be appropriate, with State agencies required to track Federal guidelines in the initial and subsequent submission of information. If the sanction of withholding funds is utilized, a process of notification, opportunity for hearing, and public report of findings of noneligibility would be required, in which, for practical and political reasons, responsibility for decisions should be exercised by the Secretary of HUD, rather than any subordinate Administrator. In any event, extensive and continuing assessment of performance in implementation would be required to insure the relevance of Federal codes and their effectiveness in application.

Judicial Relief: Provisions of Federal codes must be subject to judicial review in accordance with the Administrative Procedure Act, and States must have a right to injunctive relief where sanctions are imposed. Both Federal authority and private parties must have avenues for judicial review to contest adverse regulatory decisions by State enforcers.

Public Reports: Because of the needs to coordinate Federal and State functions, to stimulate public responsiveness, and to achieve political responsibility, an annual or biennial report of the operations of the program, its goals and its effectiveness, should be rendered by the Secretary to the President and the Congress.

Appropriations: Because of the scale of regulation intended, and the requirement to insure adequate enforcement, significant appropriations may be required.

Effects on Existing Laws: State and local building regulations would be preempted only to the extent that they conflict with this act. (The possibility of Federal preemption followed by redelegation to the States has been noted in connection with discussion of the Occupational Health and Safety Act. See f.n. 7.) Other Federal laws under which funds may be made available for specific purposes would be modified to the extent the Secretary of HUD had determined on the imposition of sanctions in accordance with the provisions of this act.

In brief, this approach would establish machinery for the promulgation, over time, of Federal building codes covering all or a significant portion of construction activity in the United States. State enforcement powers and bureaucratic machinery would be preserved and brought into compliance by the imposition of Federal sanctions. If a mandatory Federal code were adopted, a Federal enforcement mechanism might subsequently be required to the extent that State and local mechanisms proved noncooperative. In any event, significant Federal funding would probably be required to achieve satisfactory State and local compliance.

Federal Coordination and Certification of State Regulatory Programs: Conceptually, this approach differs from the Federal building code approach previously discussed in terms of emphasis and timing, placing Federal authority in a reactive role and putting primary emphasis on the efforts of States to bring their own regulatory programs more into line with national needs. Federal regulatory authority would articulate national needs and goals, and facilitate the development of State regulatory mechanisms in compliance with national policy. A program of Federal sanctions, both carrot and stick, would be appropriate, but the initiative for reform would rest in the States under Federal supervision. Present efforts to promote model State codes would be placed in a more pressured policy framework thereby.

Again, pending land use planning bills suggest useful analogies, at least one of which suggests a very tough approach. S.792, introduced by Senator Muskie as an amendment to the Federal Water Pollution Control Act, prohibits Environmental Protection Agency grants to States for water and air pollution activities unless the Administrator of the Agency has found that applicant States have comprehensive environmental protection permit programs approved by the Administrator in accordance with statutory standards. These programs must embody an adequate process for issuing permits, and must implement an adequate mechanism for overseeing compliance with permit requirements, which must follow environmental protection criteria specified by statute. As sanctions, S.792 embodies both the withholding of funds for other relevant Federal programs and the making of grants to effectuate coming into compliance with the provisions of the amendatory bill.

As defined in the Muskie bill, "process" includes opportunities for public participation in the development of standards, in implementation and review, and in the issuance of particular permits, while "mechanism" includes ways of achieving coordination within relevant State agencies and among States and Federal agencies. The definition of "criteria," specifically set forth in the bill, precludes certification of a program unless State regulation complies with a number of standards set forth in the bill and in other existing Federal legislation (to which might be added, with respect to building regulation, compliance with additional criteria which Congress would authorize a Federal agency to promulgate).

With respect to building regulation, a parallel approach may be feasible. Initially, it should be established that a State will lose Federal funds by a particular date unless it has established a statewide building regulatory system (with provisions, of course, for subdelegation and exemption with respect to particular classes of political subdivision or building construction), embodying specified provisions for public participation in the promulgation of standards, implementation, enforcement, and judicial review. In addition, criteria for the approval of proposed buildings should emphasize adoption of uniform standards throughout a particular State and uniformity with other jurisdictions, initially through adoption of a model code. The pace of reform, however, should be expressly pressed both by statutory provisions and by Federal administrative rulemaking. Specifically, a Federal administrator could be empowered to make rules for the utilization of specific building products, materials, and techniques which must be "substantially reflected" in the criteria utilized by State building regulatory processes.

A key to the effectiveness of this approach would be the requirement, paralleling the provision of the Muskie bill, that Federal certification of State building regulatory programs be of limited duration, e.g., 4 years. Thus, in the first phase after enactment of the legislation, States may be required by a particular time (say, 2 years after enactment) to have in being a prescribed process and program, with regulatory criteria consistent with a model code. Prior to that time, the Administrator (of a Federal Building Standards Administration in HUD) will have completed promulgation of certain specified criteria—probably drawn in the negative (i.e., "No State code may prohibit the use of plastic pipe for the following purposes . . .") to be made applicable for the next ensuing certification period, with the threat of nonrenewal a key sanction to achieve compliance. Such Federal criteria, of course, would have to be adopted under safeguards of procedural fairness and judicial review, and inputs from the States as well as industry, labor, and consumers would have to be fostered through an advisory mechanism.

The requirement that States be responsive to federally imposed criteria would have an organizational corollary for State regulatory mechanisms, that State provisions could be revised by State administrative action rather than awaiting the full legislative cycle (often 2 years). Otherwise, States could find themselves crippled in their programs, faced with Federal sanctions, without an opportunity to comply with Federal standards. In any event, however, the right of States to contest sanctions through litigation would again have to be confirmed.

The "Amalgam" Approach: As a final alternative one should note the possibility of forging "amalgams" among the foregoing approaches. The Occupational Health and Safety Act has previously been identified as one such course, in which total Federal preemption through mandatory standards is followed by selective redelegation to States, under statutorily defined guidelines. In the building code field (where extensive local regulatory structures exist) such a course would seem, for practical reasons, to put the cart before the horse.

To reverse the approach by commencing with a process of coordination and certification, affording the Administrator discretionary authority to issue product standards or mandatory building codes, would have the virtues (to introduce a different metaphor) of a mailed fist in a velvet glove. By this approach, the Administrator could be afforded authority to speed along the process of achieving modernization and greater uniformity by issuing such standards or codes in his discretion. States, by contrast, would have a major additional incentive to change, so as to stave off the requirement of outright Federal preemption.

The Alternatives Evaluated

With varying degrees of specificity, this paper has pointed out three broad approaches to the problem of how a stronger Federal role in building regulation might be achieved. They are: Federal definition of standards for particular building products; promulgation of a Federal building code to be enforced by the States; and Federal certification of State processes, mechanisms, and criteria for building regulation within an overall framework of statutory and administrative guidelines. An additional combination of these approaches, resting on certification but according standby authority for issuance of product standards or codes, has also been discussed. In a separate paper, the legal and practical justification for these approaches, against the background of existing approaches to building code reform, will be assessed.

Nevertheless, certain preliminary distinctions and requisites common to the adoption of each alternative can be usefully pointed out here.

1. Development of building products standards can be accomplished by a Federal instrumentality with minimum participation by the States; promulgation of Federal codes and Federal certification of State activities require ongoing coordination with the States, justify extensive Federal commitments in terms of grants and training support to effectuate compliance, and may require toughly imposed sanctions through the granting and withholding of funds.

2. While the outright development of Federal standards and codes would require the least measure of Federal involvement with the activities of model code groups and traditional interests in the building industry, coordination with these interests may be the key to practical improvement on the scale needed. Thus, preserving and stimulating State initiative in code formation as reflected in the Federal certification of State programs may be an attractive and useful reason for legislation following that course of action.

3. The development of a comprehensive Federal building code (even if administered by the States) would require a Federal reevaluation of traditional building approaches that may well be a distraction from the central aim in view of stimulating innovative measures. Nonetheless, an opportunity to reassess safety standards (dramatically suggested by the recent building collapse in Bailey's Crossroads, Virginia, and a series of fires in high-rise buildings purportedly conforming to local codes) may be required. Moreover, it should be recognized that failures of coordination between Federal and State agencies may subsequently require the development of a Federal enforcement mechanism on a vast scale.

4. In all three approaches, major Federal research initiatives are required, not only in the development of new building techniques, but perhaps, more importantly, in fostering the development of methodology for judging innovative technology persuasively. Thus, the key to success may well be the extent to which a Federal "handle" on performance standards can be achieved, a task that appears justified regardless of the method of greater Federal regulatory involvement chosen. Moreover, the political credibility of any novel departure in regulation may well depend on a prior demonstration that improved regulatory methods are actually in reach.

5. In order to tailor the specific application of desired regulation, as well as to make a political case in support of proposed legislation, extensive statistical inquiries should be made with respect to the retarding effects of existing building regulations, the economic benefits of removing such restrictions, and the most useful targets for building regulation reform.

Creating a National Market for Innovation in Building: Justifying Strong Federal Action

By Steven R. Rivkin*
Nicholson and Carter

Summary

This paper deals with three aspects of the problem of justifying the case before Congress and the public of the need for a strong Federal initiative in the building code field. These aspects bear on the choice among alternative regulatory schemes proposed and analyzed in a separate paper and requiring special enabling legislation.

The three aspects are:

1. The constitutional framework. The paper presents an analysis of recent departures from conventional Constitutional doctrine which relegates regulation of building matters exclusively to the States. Post-New Deal expansion in the concept of interstate commerce has now been extended to a range of purely local matters, limited only by the necessity of a showing of direct relationship to trade and commerce among the States. Recent Supreme Court cases construing the Civil Rights Act of 1964, in particular, indicate a broad scope for Federal power. There is no doubt that any of the four proposed regulatory alterantives would be amply within the power of the Congress to enact and of the Executive Branch to implement.

2. Making the case for Federal action. Despite abundant, widely shared, and highly plausible claims that the prevailing pattern of multiple restrictive building codes drives up the cost of housing, the case remains to be substantiated by careful economic analysis. Yet such hard data are necessary to present the issue to Congress and overcome anticipated objections, and to lay the initial course to be followed by Federal regulation. A number of areas for further fact-gathering are suggested that would be material to this aim. In addition, it is suggested that efforts be made in justifying the need for Federal intervention to coopt existing institutions at State levels working to reform building codes. The principal case for reform should be made in terms of the economic need, rather than the defects of existing administrative efforts.

3. Reflections on legislative strategy. A strong economic case, the availability of Federal grants, and indications that reform will only increase the volume of construction will go far toward minimizing opposition efforts. Care must be given in the initiation of legislation to ensure that multiple committee reviews, if necessary, will not impede passage. Consideration ought to be given to initiating litigation, or threatening its initiation, to attempt to create a momentum toward Federal regulatory intervention as a compromise acceptable to interests that would otherwise rise in opposition to a solely legislative approach.

In a separate paper, alternative legislative approaches have been identified by which the Federal Government can now move to foster a national market for innovative technology in the construction industry. To achieve these ends, Federal roles have been outlined in promulgating standards for the use of particular building products and materials; displacing inconsistent State regulations; promulgating Federal building codes for mandatory or leveraged enforcement by State building regulatory mechanisms; coordinating State regulation within a framework of nationally defined goals; and a combination approach whereby the coordination of State activities can give way to more direct Federal intervention if circumstances warrant overtime.

Each of these approaches represents the creation of a novel Federal regulatory function, requiring specific statutory authorization. Congress would be called upon to create an administrative mechanism (an Administration, either independent or within an existing Government agency, such as HUD) and to provide specific authority for the exercise of Federal powers and the limited displacement of State powers. In addition to authorizing appropriations, Congress would be asked by the executive branch in each year to appropriate funds to accomplish its purposes as expressed in the underlying substantive legislation.

* Reference is made in this paper to a law review article. Because of space limitations, the article has not been included in this volume. The article is: Steven R. Rivkin, "Courting Change: Using Litigation to Reform Local Building Codes," *Rutgers Law Review*, Vol. 26, No. 4, Summer 1973, pp. 774–802.

This paper aims to set forth the legal and practical framework within which the case for such legislation would be made, and to note the relevance of these factors to each of the broad legislative alternatives previously identified. As the first step, an analysis of recent cases is given, by which Federal powers under the Interstate Commerce Clause of the U.S. Constitution (Art. 1, §8, cl. 3) [1] are shown to have ample authority for Federal legislation preempting areas of traditional jurisdiction under State police powers.[2] Subsequently, the paper reviews and analyzes presently available economic and administrative justification for such legislative enactments, essential both to justify the proposal of new legislation and to guide the initial choice of direction by a Federal administrative body once legislation is enacted. In addition, suggestions are made for the kind of additional justification that would be useful to support legislation and to contribute to initial administrative orientation. Finally, certain practical assessments are offered bearing on legislative strategy, continuing and supplementing the preliminary comments offered in the companion paper.

The Constitutional Framework

The traditional statement of assumptions about authority to regulate construction—ignoring latent Federal powers and focusing solely on the authorities of the States—is typically expressed in the single comprehensive document that has come to hold greatest authority for building code lawyers, Charles S. Rhyne's *Survey of the Law of Building Codes*:

> The law of building codes is grounded upon what is called the "police power" of the state. The police power is *the source of all authority to enact building codes.* It has never been very exactly defined, and indeed the United States Supreme Court has said that it is 'incapable of any very exact definition.' Broadly speaking, it is the power of the state to legislate for the general welfare of its citizens.[3] (Emphasis added.)

Rhyne's 1960 study then continues to describe the then prevalent pattern of delegation of these exclusively State powers to municipalities:

> This power resides in the legislature of the states and enables the legislature to pass laws such as building codes. Some states have done so. But most states have chosen to delegate a portion of their police power to local governmental units such as cities, which are formed by the state legislature and can exercise such powers as are conferred upon them by the state legislature. It is under the police power delegated by the state legislature that local governmental units are able to enact building codes.[4]

Insofar as the above thumbnail sketch implies that Federal authority is constitutionally excluded from the building regulation field, it grossly overstates the case in the light of contemporary constitutional doctrine, implemented through a number of key Federal statutes referred to in the companion paper and buttressed by a solid line of court holdings. These developments have occurred in fields that are essentially indistinguishable from the field of building regulation insofar as they touch upon the sweep of Federal power under the interstate commerce clause and powers of a State under which local regulation "for the general welfare of its citizens" is permissible. Changed too is the perception of need for a Federal role, the absence of which made Federal initiatives just as unthinkable in 1960 as its presence makes strong Federal action appropriate a decade and a half later.

It is by now a legal maxim that the reach of legitimate Federal power under the interstate commerce clause is far greater than was once perceived—limited only by the practical requirement of some rational nexus to trade and commerce among the States, either explicitly or impliedly before the Congress in its enactments. Perhaps the most graphic demonstration of this change of attitude is expressed in the recent reenactment of Federal narcotics control statutes. Where originally Federal powers were considered inadequate to reach the possession of narcotic substances, giving rise to an elaborate (and ultimately constitutionally vulnerable) substitute structure to choke off narcotics traffic,[5] now a simple provision of the Drug Abuse Prevention and Control Act of 1970 makes it unlawful to "possess" a "controlled substance" except in accordance with the provisions of the act.[6] In essence, a frank recognition by the Congress that the problem of drug abuse constitutes a national problem underlay the ability of Congress to devise a more rational, comprehensive struc-

[1] Art. 1, § 8 provides that, "The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes . . . "

[2] Amendment X provides that, "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."

[3] Rhyne, *Survey of the Law of Building Codes*, p. 7 (1960).

[4] *Ibid.* at 8.

[5] For example, dating from the early years of the twentieth century, a key Federal statute rested on the device of a factually infirm "statutory presumption" of evidence to equate mere possession of heroin to knowledge of the substance's illegal importation (21 U.S.C. § 174, repealed 84 Stat. 1291 (1970)) as the essential basis for federal authority. See *Turner* v. *U.S.*, 396 U.S. 398 (1970).

[6] 21 U.S.C. §844(a).

ture of control. As a result, mere possession by an individual—about as "local" an act as can be imagined—is now an unambiguous Federal crime.

With a similar perception of need lacking in the field of construction standards, it is not surprising that a similar comprehensive legislative mandate has not been sought or secured.[7] Nevertheless, it has been clear, at least since New Deal days, that Federal powers can be exercised over transactions and types of business activities for which a strong contrary argument can be made on behalf of State powers. For example, in *Wickard* v. *Filburn* (1942) [8] Federal crop controls were upheld as they apply to produce that is grown and consumed entirely on the farm, inasmuch as they cast an appreciable shadow on product markets, and in *U.S.* v. *South-Eastern Underwriters Assn.* (1944) [9] the business of writing insurance on property—never considered previously to be "commerce" between the States —was brought under the standards of the Sherman Antitrust Act. And later cases, especially those identified with the field of civil rights, go quite far to affirm Federal powers every bit relevant to the field of building regulation.[10]

[7] Nonetheless, limited mandates displacing local codes have long existed, typified by the provisions of the Lanham Public War Housing Act, 42 U.S.C. §1521(b), displacing State regulatory powers for certain federally owned or leased lands to be utilized for defense housing.

[8] 317 U.S. 111 (1942).

[9] 322 U.S. 533 (1944).

[10] At this point, two broad principles underlying the sweep of Federal power over conflicting State interests are important to keep in mind. The first is the unambiguous efficiency of Federal power under the Constitution through the "necessary and proper" clause (Art. 1, §8, cl. 18) and the interstate commerce clause, to legislate over domestic economic activity, displacing State authority. As the Supreme Court said in "The Shreveport case," *Houston & Texas Ry.* v. *U.S.* 234 U.S. 342 (1913),

> . . . It is unnecessary to repeat what has frequently been said by this court with respect to the complete and paramount character of the power confided to Congress to regulate commerce among the several States. It is of the essence of this power that, where it exists, it dominates. Interstate trade was not left to be destroyed or impeded by the rivalries of local governments. The purpose was to make impossible the recurrence of the evils which had overwhelmed the Confederation and to provide the necessary basis of national unity by insuring 'uniformity of regulation against conflicting and discriminating state legislation.' By virtue of the comprehensive terms of the grant, the authority of Congress is at all times adequate to meet the varying exigencies that arise and to protect the national interest by securing the freedom of interstate commercial intercourse from local control. At 350–1.

In addition, the Supremacy Clause of the Constitution (Article 6) imposes a reciprocal obligation on the States to yield to Federal power, as follows:

> This Constitution, and the laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, anything in the Constitution of Laws of any State to the Contrary notwithstanding.

A few key examples of the extensive scope of Federal powers recently affirmed by the courts follow, coupled with a discussion of the indications that affirming courts have given as to the requisite connection to interstate commerce.

• The leading edge of modern commerce-clause doctrine was set forth in *Heart of Atlanta Motel* v. *U.S.*,[11] where the public accommodations provisions of the Civil Rights Act of 1964 were upheld in the case of a motel. The Supreme Court cited an earlier holding that "[i]f it is interstate commerce that feels the pinch, it does not matter how local the operation which applies the squeeze," [12] even embracing local activities both in the States of origin and destination. In *Heart of Atlanta* it was conceded that the motel was easily accessible to interstate highways and that approximately 75 percent of its guests came from out-of-State. The Federal act was held to bar all discrimination by the motel, on a finding that the character of its discrimination was precisely envisaged by Congress in passing the act.

• In a companion case, *Katzenbach* v. *McClung*,[13] the act's application to restaurants was upheld (the act applying to restaurants serving or offering to serve interstate travelers or where a substantial portion of its food "has moved in commerce"). The court found that congressional hearings had laid factual foundation for the adoption of prohibitions on such discrimination. The court said,

> where we find that the legislators, in the light of the facts and testimony before them, have a rational basis for finding a chosen regulatory scheme necessary to the protection of commerce, our investigation is at an end.[14]

Two additional pertinent findings necessary to complete affirmative review were also made. First, the lower court had held that the restaurant in question actually did serve interstate travelers, and that its food was substantially imported from other States—the necessary factual triggers for application of the statute. Second, the court supplemented its review of the legislative history by finding a rational relationship between applicability so limited by service (*to* interstate travelers and *by* interstate products) and the constitutional objective of protecting interstate commerce. Thus, in summary, to substantiate the application of Federal controls in a

[11] 379 U.S. 241 (1964).

[12] *U.S. v. Women's Sportwear Mfg. Assn.*, 336 U.S. 460, 464 (1948).

[13] 379 U.S. 294 (1964).

[14] 379 U.S. at 303–4.

particular case, there must be a) legislative deliberation of relevant facts; b) legislative tailoring of controls to relate those facts to particular objectives; and c) a demonstration that the fact of a particular situation fall within the legislative prohibition. (This holding is elaborated upon here because it sets forth the specific categories which justification for building code legislation must fill, steps to be discussed in the second section.)

• The "rational basis" test was given a very wide reading by the Supreme Court in *Maryland* v. *Wirtz,*[15] where a 1961 amendment to the Fair Labor Standards Act was upheld extending coverage under wage and hour standards from employees individually engaged in production for commerce to any "enterprise" engaged in commerce (regardless of the function of the particular employee). The extension of the original act from individual employees to all employees of a particular employer was fought as exceeding Federal powers, but the Court rejected that argument, finding a rational basis in two respects (lower wages in part of an enterprise and labor disruption through strikes both affect interstate competition). Significantly, the Court held that Congress had only to define the class of activity (enterprises engaged in commerce, very widely defined) leaving for courts only the question of determining whether the particular class was within Federal power. In *Wirtz,* the underlying statute was extraordinarily broad,[16] and the result, the Court found, was to eliminate the claim that an enterprise within the class was not covered because the magnitude of its activities in commerce was trivial. The result of *Wirtz,* in building-regulation terms, is that virtually any connection of a construction project with any Federal power (interstate commerce, Federal mortgage programs, urban renewal, etc.) is well within the scope of Federal regulatory power.

• Even a country swimming-hole, 6 miles from the nearest State or interstate road, where there was no special showing that any patrons had come interstate, was held within the Civil Rights Act of 1964, consistent with the interstate commerce clause, by the Supreme Court in *Daniel* v. *Paul,*[17] where the operators used 15 paddle boats leased from out-of-State. Again, the volume of commerce need not be great, once it is shown (or inferred) that the subject of regulation is within a constitutionally permitted class.

• In two criminal cases—*Perez* v. *United States*[18] (loan-sharking) and *U.S.* v. *Dawson*[19] (storage of explosive materials)—Federal courts have upheld Federal criminal statutes involving the most localized subjects. Loan-sharking was revealed in congressional hearings to be tied to the nationwide operations of the Mafia, and possession of explosives (without an explicit legislative finding to that effect) was seen by the court as tied to political terrorism. Once again, these cases stand for judicial deference to the ability of Congress to relate local activities to national problems and legislate to control them.

• Finally, in a recent Supreme Court decision, *City of Burbank* v. *Lockheed Air Terminal,*[20] the U.S. Supreme Court struck down a local Burbank ordinance imposing a curfew on operation of jet aircraft after 10 p.m. at night on grounds that the ordinance conflicted with authority of the Federal Aviation Administration to regulate aircraft noise. Although the powers of the FAA (supplemented by the Environmental Protection Agency) did not flatly preempt State and local noise control, the court read the Burbank ordinance as fouling federally protected airline scheduling. The case is relevant because it indicates a parallel instance where Federal regulation of a problem common to the Nation and the States may be less restrictive than local regulations, with national regulatory concerns being more broadly defined. In building regulation, to achieve the economies of a national market the situation would be parallel.

What relevance do these cases then hold for the alternative legislative approaches previously specified?

With respect to the setting of building products standards, the Civil Rights Act cases make clear that Federal power may be extended to protect products within the scope of statutory or regulatory coverage. The breadth of the building "products" class may even be extended to embrace standards for the use of "materials" which have moved in commerce or in whose use a substantial Federal interest can be shown. (For

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[15] 392 U.S. 183 (1968).

[16] The term "enterprise engaged in commerce or in the production of goods for commerce" was defined by 29 U.S.C. §203(s) to mean "an enterprise which has employees engaged in commerce or in the production of goods for commerce, including employees handling, selling, or otherwise working on goods that have been moved in or produced for commerce by any person, and which—[falls in any one of four listed categories]."

[17] 395 U.S. 298 (1969).

[18] 402 U.S. 146 (1971).

[19] 467 F. 2d 668 (C.A. 8, 1972).

[20] No. 71-1637, October Term 1972 (opinion of May 14, 1973).

example, if the Nation is indeed "running out of wood," standards for wood substitutes would be appropriate as a conservation measure.)

Instead of focusing on the development of a market for specific building products which the building products standards approach would serve, Federal building codes and Federal certification of State programs would both rest on a more comprehensive purpose of the same sort, an explicitly stated national goal of fostering building innovation across the board. This justification would be no different in qualitative terms, only more all-embracing. But the essential requirement would be the showing to Congress, and its acceptance of it, of the case that the costs of construction nationwide must be lowered, and its efficiences raised, by removing blockages to a national market—either through total displacement or purposeful coordination. In each instance, the goal to be achieved could well be defined in terms of the ill-served aim of the Housing Act of 1949 (reaffirmed by Congress in 1968) of "a decent home and a suitable living environment for every American family . . . ."

Archaic local building regulations, like Burbank's equally well-intentioned noise ordinance, will fall where broader Federal purposes are clearly expressed in legislation. (Implicit in the Burbank instance is the damage an unduly restrictive local code can do to the goal of building a national market.) On balance, therefore, Federal constitutional authority would be ample to permit effective Federal intervention in the building field.

Making the Case for Federal Action

Simply put, proving the case for Federal initiatives requires showing that a major national need exists which is not being met (and cannot be met) by present State-based initiatives and other Federal programs. Rather than evaluating comprehensively either the economic case for a national regime of building regulation or the programmatic defects of existing State and Federal programs, this section will attempt to point out guideposts for specialists—economists and administrators, respectively—more deeply involved in their details. This analysis will emphasize the ways in which these considerations have direct relevance to choice among the alternative legislative initiatives that have already been identified.

The Economic Justification: The assumption is that the diffuse pattern of local regulation—under which there exist more than 5,000 separate regimes of building regulation implementing more or less archaic regulatory standards—drives up the cost of construction in the United States. That assumption is logical, widely perceived—and relatively unproven.

There is little doubt that the cost of residential housing in the United States is very high, and rising. Recently, a *New York Times* story reported a Bureau of Labor Statistics report that the cost of homeownership has increased 91.7 percent in the last 20 years,[21] and ABC News found a 30-percent increase in the last 5 years.[22] The same ABC broadcast reported a gap between the cost of the average home ($28,000) and the average family income ($10,000), putting housing ownership out of the reach of about 50 percent of the American population.[23] Nor is it controverted that production falls far short of the Nation's quantitative housing goals, where Congress has authorized steps to achieve 26 million new units over a 10-year period[24] but reported that production in the "brightest" of years has fallen far short of the necessary rate.[25]

That multiple restrictive building codes make a major contribution to this picture of continuing shortage and cost escalation is often asserted on a largely impressionistic and unsubstantiated basis. Journalists have estimated, for example, that the limitation of productivity caused by diverse restrictive building regulations "swells the price on typical houses by an estimated $1,000 to $2,500."[26] Home manufacturers and, in particular, producers of modular assemblies tend to recite code problems as one of their top problems.[27] It is more than likely that Herbert Hoover's 1922 finding, as Secretary of Commerce, that building code defects impose addi-

[21] "Home Costs Rise 91.7% in 20 years, Outstripped Only by Service Industry, "*New York Times*, June 11, 1973, p. 1.

[22] "The Building Innovators," ABC Television Network, April 28, 1973, p. 32 (transcript).

[23] Ibid., p. 1.

[24] 42 U.S.C. §1441a.

[25] President Nixon has reported total production in 1970 of only 1.9 million units, reflecting an outlook which "is the brightest in years." Third Annual Report for Housing Goals, H. R. Doc. No. 92–136, 92nd Cong., 1st Sess. (1971).

[26] "Big Battles Over Rules for Builders," *Business Week*, January 1, 1972, at 48.

[27] Charles G. Field, in an unpublished doctorate thesis at Harvard University reported, out of about 200 firms replying to his 1970 survey questionnaire, that 29 percent of all home manufacturers and 52 percent of modular producers viewed codes as one of their top three problems. Field, *Home Manufacturing and Building Codes: The Confrontation Between Technology and Institutional Regulation* (1971, unpublished) pp. 161, 165, Table 4–2.

tional housing costs of 10 to 20 percent,[28] holds true today; if so, a rough rule of thumb calculation indicates that from 200,000 to 400,000 more units could be built each year—enough of an increment over current trends to add appreciably to the effort to meet the Nation's housing needs as mandated by the Congress.[29] More housing construction could, of course, be translated not only into a greater supply or a lower cost, but also into improved quality.

But because the restrictiveness of existing codes inhibits the development of market efficiencies through which logical cost reduction possibilities might be proven by hard facts, scratch-pad estimates apparently remain only that, even though three "blue ribbon" commissions have, in recent years, endorsed these worthy assumptions.[30] Such authoritative endorsements may count for something when an issue is relatively uncontroversial, but the political influence of interests likely to be deployed against Federal intervention in the building field may well be quite formidable. In that case, bringing together the most meaningful achievable data in the form most relevant to proposed legislation would be virtually mandatory—both to support Administration proposals and to guide their initial implementation.

The aim of such an inquiry would be to indicate the dimension of the problems caused by current code practices and to show how specific reforms could contribute to their solution. The following types of information would appear most useful for these purposes.

1. What are long term trends in the construction industry in terms of costs and efficiencies, and what are their implications for the present and future costs and availability of housing for the American people? This information should be broken down by geography, by components within the construction industry, and by effects on particular types and categories of construction and in terms of particular social and economic categories of consumers.

2. What measures of achievement can be drawn from comparable trends in other countries, and to what extent is improved performance elsewhere attributable to alternative patterns of building regulation or to other factors (such as public subsidies)?

3. What cost benefits can be assigned to the introduction of new technologies, both proven (as, for example, where plastic pipe has been utilized) and potential? Which technologies seem to be the most promising in terms of anticipated benefits from a national market?

4. Are there any suggestions for improved performance in the housing industry to be drawn from performance of other industries? For example, what, if any, technological or economic benefits are suggested by analogy to concentrated, highly automated production in the automobile industry?

5. What are realistic long range housing needs for the Nation, and how can the creation of a national market for building make specific, predictable contributions to their solution?

6. Just how important is archaic and decentralized building regulation in holding down housing industry performance, compared to other factors such as the cost of land and the cost of credit? If a national market for building is created, how likely is it that the consumer will benefit, or would these other cost factors tend to rise to reduce or eliminate any such benefit?

[28] Quoted in U.S. Advisory Commission on Intergovernmental Relations, *Building Codes: A Program for Intergovernmental Reform* (1966) p. 2.

[29] A 10 percent savings on the cost of the average home ($28,000), if translated into additional housing construction, would yield a 10 percent increase over the roughly 2 million units being constructed each year. A 10-year level of 20 million homes could be increased to 22 million were a 10 percent savings so realized and 24 million if the savings were increased to 20 percent (measured against the current national goal of 26 million units).

[30] In 1966 The Advisory Commission on Intergovernmental Relations concluded:

> The existence of many thousands of different local codes imposes burdens on the building industry that limit initiative and innovation in the development of new construction materials and techniques and result in excessive requirements adding to the cost of construction. Nothing short of a major overhaul and restructuring of intergovernmental responsibilities for building codes will suffice to meet the housing and commercial construction needs of late 20th Century America. *Building Codes: A Program for Intergovernmental Reform* (1966), p. 71.

In 1968, the Douglas Commission reported:

> In brief, the facts disclosed by the exhaustive inquiries of this Commission at local, State and National levels, and the problems faced by producers, builders and professional people in the building industry, show unmistakably that alarms sounded over the past years about the building code situation have been justified. If anything, the case has been understated. The situation calls for a drastic overhaul, both technically and intergovernmentally. The National Commission on Urban Problems, *Building the American City*, H. R. Doc. No. 34, 91st Cong. 1st Sess. 266 (1968), p. 266.

And also in 1968, the Kaiser Commission found:

> The existing crazy-quilt of state and local building codes and mechanical codes (like those governing electrical and plumbing installations) has discouraged technological innovation, added to the cost of construction, and increased building time. The President's Committee on Urban Housing, *A Decent Home* (1968), p. 199.

7. If wider markets for building were created, what natural limits would problems of transportation, credit, or training a competent labor force impose on the growth of an industry capable of serving that market effectively?

8. What cost and other programmatic handicaps do existing building regulations impose on the effectiveness of Federal urban programs generally and, particularly, of Federal procurement? What cost/effectiveness increases, if any, in these programs, could be forecast through building regulation reform?

9. What legitimate methods, other than regulation of standards of construction, are available to protect the economic positions of industries and groups that might be adversely affected by building code reform? How realistic is the likelihood that such traditional interests would be damaged, or would reform merely permit the growth of additional market opportunities?

By no means do these areas of inquiry exhaust the field where useful supporting data should be gathered, for what presently would seem to be a largely unproven assumption. More questions can and should be generated for study. Moreover, the answers to such inquiries should play a significant role in the choice among alternatives for a Federal regulatory strategy.

For example, if immediate benefits can be foreseen from emphasizing a small number of proven technologies (such as the technologies proven through Operation Breakthrough), it may very well be that introduction of a Federal products standards program for these technologies would stand the best chance of acceptance by the Congress, as an initial step, and be easiest to administer thereafter. If, on the other hand, the precise efficacy of Federal controls remains unclear, even though general benefit would be anticipated from the relationship of an operating program to a well-funded R&D facility, then a Federal coordination and certification approach designed to upgrade and discipline State efforts might be more sound. Moreover, in any of the avenues identified, such information would be of critical value in identifying initial regulation steps with the highest and most visible payoffs.

The Adequacy of Existing Programs: Seen in terms of apparent motion, such recent developments as the adoption by 27 States of statewide building regulations, the development of a model code for manufactured housing, the increase in consultation among the states in building code matters (largely through the National Conference of States on Building Codes and Standards), and the deployment of HUD leverage to achieve local acceptance of more modern codes —all suggest progress. If, on the other hand, the economic inquiries suggested above show no appreciable improvement (in the context of demonstrating the overall materiality of code problems), then these activities are failing to meet the need. In fact, recent improvements in coordination may constitute more of a barrier than a force for further change, if whatever reduction in diversity has occurred cannot be projected to accelerate.[31] As always in such circumstances, one more Federal program would then seem justified.

In that case, one especially potent justification for Federal initiative would appear warranted, beyond the need for greater uniformity—which, after all, is a goal shared by the model code effort. That need would be to focus the best scientific and technical resources, adequately funded, on developing improved performance standards for measuring the effectiveness of building solutions. Only through a concentrated approach, within the framework of a national commitment to achieve a market for innovation, could appreciable progress be made. A vigorously led, highly visible, and adequately funded Federal agency, charged by law with developing such an approach in the earliest possible time frame, could be far better suited to the task than the widely diffused and underfunded entities that now occupy the field. By contrast to the proposed National Institute of Building Sciences, moreover, a Federal agency with continuing responsibilities to develop and promulgate performance standards would be under a higher incentive to produce early results capable of generating high levels of confidence than one confined to an advisory role.

The results of economic analysis should be dispositive of the issue whether recent administrative improvements are doing any good at all,

[31] As part of the preparation of a thorough case for an Administration proposal, a detailed and objective review of the achievements of the NCSBCS program could be undertaken, along with a proviso-by-proviso assessment of the accomplishments of recent state-wide code programs and of the model code groups. The complexity and magnitude of such a careful effort would probably outrun its utility, however, and could stimulate opposition to any subsequent legislative initiative. Thus, the case for a federal initiative ought to rest principally on a showing of economic need and opportunity, commending existing programs for initiative but asserting that without a major additional infusion of federal talents and resources, locally-based initiatives have and will continue to have a bull by the tail.

and thereby answer the question of whether they should or should not be left to occupy the field. (The question, by analogy, might well come down to whether a losing football team should change its coach or its quarterback, or whether President Lincoln was right in switching generals until he found a winner.) If an urgent need can be shown, the best case for Federal intervention will be made. Then, quickening the pace of State activity would itself be one of the goals of Federal initiative, and could be adopted as a further argument for a strong, complementary Federal initiative at this time.

Reflections on Legislative Strategy

The companion paper concluded with an analysis of the functional differences among the three principal legislative alternatives (supplemented with a fourth, "amalgam" approach), assuming enactment, in achieving their goals of reducing diversity and facilitating change. For the earlier point in time, when the case for a specific legislative proposal must be made to the Congress and the American people, it is also appropriate to draw distinctions between these alternatives.

There can be little doubt that opposition to any central Federal role will be manifest from industries, craft unions, State and local administrations, and possibly from Federal agencies that any legislative proposal would bypass. A prudent legislative strategy would seek to meet and undermine whatever such opposition develops.

For example, assertion of a States' rights position could be effectively negated, in legal terms, by the showings made earlier in this paper. If litigation were to result after passage, its prospects for success would not be good, though it could tie up some aspects of initial administration of the resulting programs; nonetheless, once suits are brought to a close, the Federal program would probably be stronger therefor. In any possible head-to-head clash with the States, the availability of ample Federal grant funding would be a strong force for compromise.

The opposition of industries and craft groups might best be met by the availability of economic projections showing that building regulation reform will not (immediately) displace existing construction activity, only create new market opportunities. (For this reason, it would probably be best for a program of building code reform to be presented as part of an omnibus package program, likely to increase the national volume of building, never by itself.) Enough time for some suppliers to diversify investments into new technologies might be offered, along with programs for worker mobility and retraining (although such programs have never been particularly successful).

For State building bureaucracies (coordinated nationally through the National Conference of States on Building Codes and Standards at the Department of Commerce), the inducements of a flow of Federal funds for planning and enforcement and a greater pace of activity would be counterarguments to likely State resistance and defensiveness over greater Federal initiatives. Possibly some consultative role for NCSBCS with a new Federal administration could be worked out, and for the model code groups as well (whose existing and proposed standards could be given a legislative preference for adoption where they have been shown adequate and developed through procedures satisfying due process requirements).

A final pitfall in the legislative process should be flagged for attention—the jurisdiction of substantive committees in the House and Senate. It is the writer's impression that HUD legislation is initiated in the House Committee on Banking, the House Housing and Urban Affairs Committee, and the Senate Banking and Currency Committee. Because of the major significance of interstate commerce issues, the commerce committees may also have an interest in such legislation and may require a separate review. This possibility, threatening delay and further impedence in the event of controversy, might also be precipitated by inclusion of a role for the Department of Commerce (via NCSBCS), or by its exclusion, for that matter. Without suggesting how the issue might be resolved, it may be highly pertinent to success to insure that any commerce committee reviews strengthen rather than weaken any Administration bill.

On balance, it seems clear that the strength of the economic facts and data that can be marshaled will play a key role in the success or failure of any proposal in Congress. With the market as weak and diffused for manufactured housing as it undoubtedly is, little weighty support could be anticipated from suppliers for that market, although it should certainly be brought to bear on the legislative process. One is left, therefore, with the following nagging question: Who wants meaningful reform, and how strongly, on balance, can the case for a Federal initiative be made? This paper has outlined the nature of the case that can and should be made, but one should be frank to realize that the vision of change may not be sufficient to outweigh the forces of lethargy.

Even while the arguments suggested here are documented by hard facts, one ought to consider how the existing building regulatory structure might be turned toward seeking Federal intervention rather than resisting it. In a law review article published in the *Rutgers Law Review* entitled "Courting Change: Using Litigation to Reform Local Building Codes," the author has suggested how a careful strategy of litigation applying antitrust and constitutional principles can weaken the restrictive aspects of existing codes.[32] Such litigation can be undertaken by private parties as well as by the Federal Government, through the Department of Justice and the Federal Trade Commission. Either prior to, or coupled with, a move toward statutory changes, litigation or the threat of litigation could precipitate a more general recognition of the desirability of improving building regulation through Federal participation.

The Labor Component in the Cost of Housing

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A Breakdown of Cost Factors In Housing: An Overview

The costs of housing can be classified into the following categories:

- Onsite wages.
- Materials.
- Equipment.
- Overhead and profit—including supplemental wage benefits such as social security (FICA) and unemployment insurance, and selling expenses.

The distribution of these costs has been estimated by the Bureau of Labor Statistics in [2]. These breakdowns are presented in Table 1.

As Table 1 shows, onsite labor costs represent about one-fifth of the total construction costs for private single family housing and about one-third of the total construction cost for public housing. As Table 2 from the same BLS study [2] shows, the proportion of onsite labor costs for private single family dwellings tends to vary between 15 and 30 percent. These costs exceed 30 percent less than 5 percent of the time.

Land Costs—Land costs are not included in the above breakdowns, but using statistics presented by the National Association of Home Builders based on a Bureau of Labor Statistics survey, these may be estimated at about 20 percent on a nationwide basis (see [8] p. 217). Thus, if land costs were included at the indicated 20 percent share, the share of onsite labor costs would be 16 or 18 percent for single family housing. Similarly, including 20 percent land cost would reduce the onsite labor component to about 25 percent in the case of public housing data.

The data in Table 2 indicate that while onsite labor costs are not the major cost component in housing, they are, nonetheless, an important component. The BLS study [2] indicates that average hourly earnings for labor in new, private single family houses rose 28 percent (from $3.07 per hour to $3.94 per hour) between 1962 and 1969. Given the average manhours per square foot in 1962 and 1969 (85 and 82 respectively), this represents an increase of about 24 percent in the labor cost per square foot of housing between 1962 and 1969. By comparison, the total cost per square foot of housing went from $11.76 in 1962 to $15.94 in 1969, an increase of about 36 percent. Table 3 presents a comparison of the costs per square foot of housing between 1962 and 1969.

Table 3 indicates that the cost per square foot increased for all components of housing, but that overhead costs increased by more than twice labor costs or materials and equipment costs. The comparison is misleading, however, to the extent that overhead contains some significant wage costs, including employer contributions for social security, unemployment insurance, and fringe benefits such as paid vacations and retirement. Included also in the overhead figure are interest payments for builder loans, which increased fairly substantially over the period 1962–1969.

The Effects of Federal Policies Toward Labor Which Affect Housing Costs and Production

The cost data of the first section suggest that several factors have led to increased housing costs from 1962 to 1969. General inflation was no doubt a primary cause leading to greater wages, materials prices, and interest rates which affect the overhead cost. It is clear that any Federal policies aimed at attenuating rising housing costs will have to move on several fronts if substantial gains are to be made. In the remainder of this paper we consider the effects that Federal policies toward labor have on housing costs. These policies affect not only onsite labor but also the supplementary wage benefits that contribute to overhead costs.[1] Specifically, the paper examines the effect of the Davis-Bacon Act (as amended) on the costs of Federal construction and housing contracts.

[1] In this section we shall take up the question of the Davis-Bacon Act which determines the wage that must be paid on federal construction contracts. Supplementary wage benefits were included in the definition of "prevailing wage" in a 1964 amendment to the original 1931 Act.

Table 1. Percent Distribution of Construction Costs [1]

Type	Year of Construction	Onsite Wages	Materials	Equipment	Overhead and Profit	Total
Private single-family housing	1969	20.4	43.4	0.9	35.3	100.0
Private single-family housing	1962	22.1	47.2	1.0	29.7	100.0
Public housing	1968	32.4	43.4	0 [2]	24.2	100.0
Public housing	1959–60	35.5	45.0	2.5	16.5	100.0

[1] Source: Bureau of Labor Statistics [2].
[2] Equipment included in materials cost.

Table 2. Distribution of Onsite Wage Share of Costs for New, Private Single-Family Houses, 1969 and 1962 [1]

Onsite Wages as Percent of Contract Cost	Percent of Houses Surveyed 1969	1962
All Groups	100.0	100.0
15.0 and under	9.8	3.0
15.1–20.0	41.7	31.7
20.1–25.0	30.0	45.5
25.1–30.0	13.7	16.8
30.1 and over	4.4	3.0

[1] Source: Bureau of Labor Statistics [2].

Table 3. Costs Per Square Foot of Housing, 1962 and 1969

Factor	1969	1962	Percent Change 1962–1969
Labor cost/sq. ft.	$ 3.23	$ 2.61	23.8
Materials and equipment cost/sq. ft.	7.07	5.67	24.6
Overhead and profit/sq. ft.	5.64	3.48	62.2
Total cost/sq. ft.	$15.94	$11.76	35.5

Prevailing Wage Laws and the Davis-Bacon Act [2]

The Davis-Bacon Act and similar State prevailing wage laws (which currently exist in 35 States) require the payment of "prevailing" wages and fringe benefits on government contracts for the construction of public buildings or public works. In the case of the Davis-Bacon Act, the required wage rates are those determined by the Secretary of Labor to be prevailing in the city, town, village, or other civil subdivision of the State in which the work is performed. Numerous other Federal laws incorporate the Davis-Bacon prevailing wage requirement for federally assisted projects. For example, prevailing wage determinations are included in the National Housing Act, the Housing Act of 1949, the United States Housing Act of 1937 as amended, the Housing Act of 1964, the Housing and Urban Development Act of 1965, and the Housing and Urban Development Act of 1968.

The Davis-Bacon Act was enacted in 1931 for the purpose of protecting local wage rates on Federal construction from the competition of lower-wage, nonlocal labor. Amendments to the act included "prevailing" fringe benefits in the definition of prevailing wages, and charged the Secretary of Labor with the responsibility of determining the prevailing wages acceptable on Federal projects.

Specifically, the Davis-Bacon Act provides that workers employed on every contract in excess of $2,000 to which the United States or the District of Columbia is a party for construction, alterations, or repair of public buildings or public works, shall be paid no less than the rates determined by the Secretary of Labor to be prevailing on similar projects in the area for which the work is performed. The rates include prevailing fringe benefits or the cash equivalent of such benefits. In 1971, 35 states had similar prevailing wage legislation.

The Administration of Davis-Bacon: Following is a discussion of the procedures for determination of prevailing wage rates.

The procedure for predetermination of prevailing wages was formalized in a directive from the Secretary of Labor in December 1963. The Secretary's regulations define the prevailing wage as follows:

- The rate of wages paid to the majority of the workers in that classification in the area in which the work is to be performed.

[2] Much of the material in this section is drawn from [6].

• In the event that there is not a majority of workers paid the same rate, then the prevailing rate is that paid to the largest numbers of workers provided that this constitutes at least 30 percent of those employed.

• In the event that less than 30 percent of those employed receive the same rate, then the average rate where the average rate is obtained by adding the hourly rates paid to all workers in the classification and dividing by the total number of such workers.[3]

In determining the prevailing wage, the solicitor of labor is to obtain wage rate information from several sources. The types of information considered include:

• Statements showing wage rates on projects.

• Signed collective bargaining agreements.

• Wage rates determined for public construction by State and local officials pursuant to prevailing wage legislation.

• Information furnished by Federal and State agencies.

• Whenever the solicitor deems that the data on hand are insufficient to make a determination, he may have a field survey conducted in the area of the proposed project for the purpose of obtaining sufficient information upon which to make a determination of wage rates.

Section 1.6 of Title 29 of the Code of Federal Regulations contains two other relevant provisions:

• In making wage rate determinations, projects completed more than 1 year prior to the date of request for the determination may, but need not, be considered.

• If there has been no similar construction within the area in the past year, wage rates paid on the nearest similar construction may be considered.

While these conditions are explicit about many aspects of the procedure for prevailing wage determinations, the Branch of Wage Determination in the Department of Labor has a substantial amount of discretion in making determinations. In practice, it appears that an overwhelming proportion of wage determinations carry union wage rates regardless of area or type of construction. This is often a consequence of the "majority" rule, the "30 percent" rule, and the Section 1.6 authorization of determinations on the basis of the "nearest similar construction." The bias in favor of union wage rates is also likely to be a consequence of the very large number of determinations that have to be made each year and the resulting pressure for expedience in making determinations.[4] This is explained in the next section.

The Branch of Wage Determinations: Between 1945 and 1961, the number of wage determinations issued annually by the Branch of Wage Determinations rose from 3,884 to 49,740. A single determination requires wage rates for anywhere from 10 to 300 job classifications, and 100 classifications per determination is not at all unusual.[5]

The difficulty of making such a large number of determinations was noted in 1962 by Charles Donahue, who was then solicitor of labor. In his testimony before the Roosevelt Committee Mr. Donahue said:

> Unfortunately, I find that the staffing of the wage determination branch has not kept pace with the growth of its work load. At present (1962) the branch consists of only 19 professional and 40 clerical employees. This problem requires immediate attention and we are taking appropriate action to remedy this situation.

In an effort to alleviate the problems of an overburdened staff, the Department of Labor, in 1965, began to issue area wage determinations covering several agencies and projects in an area. This reduced the number of determinations to 25,408 in fiscal year 1965. While this new policy no doubt helped, the basic problem of making accurate wage determinations remained, as indicated by the remarks of Secretary of Labor W. Willard Wirtz in a letter to Mr. Eschwege of the U.S. General Accounting Office on November 29, 1967.

> Determining wage rates under the Davis-Bacon Act for residential work has been a troublesome problem and will continue to be a problem so long as the Department of Labor lacks adequate facilities for collecting wage information in various parts of the country. As you know, wage rates in the construction industry in any area vary from time to time, and up-to-date information is essential. The Department of Labor currently (1967) has a staff of 70 per-

[3] These directives are contained in Title 29 of the Code of Federal Regulations.

[4] In 1970, the responsibility for prevailing wage determinations was moved from the Office of the Solicitor of Labor to the Office of the Assistant Secretary for Wage and Labor Standards.

[5] See the testimony of Charles Donahue, Solicitor of Labor, before the Roosevelt Committee in 1962; U.S. Congress, House Special Subcommittee on Labor of the Committee on Education and Labor. *Hearings, A General Investigation of the Davis-Bacon Act and Its Administration*, 87th Congress, 2nd Session, 1962.

sons engaged in wage determining here in Washington and, also, 5 field representatives handling special matters as required. *These are not nearly enough for accurate determinations,* particularly in the residential field. (Emphasis added.) [6]

In fiscal year 1970, the Department had authorization for 91 employee positions and a budget of $952,000 for wage determination purposes. In fiscal year 1970, about 58,000 contracts totaling about $28 billion were covered by wage determination. The General Accounting Office in several reports between 1962 and 1970 pointed out that because of the problems of making determinations or for other reasons, the Department of Labor prescribed minimum rates that were significantly higher than the prevailing wages in the areas and had substantially increased the costs of construction borne by the Federal Government. The problem is one of substantial magnitude in view of the $28 billion in contracts covered by wage determinations. The next section examines the effects on wages and costs of the Davis-Bacon determinations.

Effects on Wages and Costs: Following is an analysis of GAO and other studies.

To establish a prevailing wage it is necessary to:

- Determine the classes of workers that apply.
- Determine the relevant geographical area or locality.
- Determine which projects are of a similar character to the proposed project.
- Determine what wages actually prevail.

The GAO studies of Davis-Bacon determinations have found in many cases that incorrect determinations were made because of errors in one or more of these four points. For example, in one instance, the Department classified as "ornamental iron workers" those workers used to erect chain-link fences, even though chain-link fences were ordinarily installed by laborers and foremen receiving a much lower hourly rate ($1.25 to $2.75) than ironworkers ($3.65). In other cases, union rates were applied in worker classifications without determining if the union rate was indeed prevailing in that class.

Even though the act requires that wages be prevailing in the "city, town, village, or other civil subdivision of the State in which the work is to be performed," there is evidence from the GAO and other studies that this requirement has been seriously violated. In a study of federally financed construction in New England in 1962, the GAO stated:

> Our review of the determinations by the Department of Labor of minimum wage rates to be paid to mechanics and laborers employed on construction of federally financed building projects in selected New England areas disclosed that many of the rates were improperly established at the higher rates negotiated by labor organizations and building contractors rather than at the lower rates prevailing on private construction in the project areas. Also, wage rates determined for certain crafts in connection with a federally-assisted low-rent housing project in Massachusetts were on a level with the negotiated rates normally paid on commercial-type building construction rather than equal to the lower rates paid on similar private housing construction in the locality. *Our review showed that these unrealistic determinations were based on inadequate information obtained by the Department on wage rates in these areas, and we believe that the Department has not complied with either its own regulations or the intent of the Davis-Bacon Act that wage determinations be based on the wage rates prevailing for similar construction in the locality.* (Emphasis added.) [7]

The GAO report presented several interesting findings about Davis-Bacon determinations in New England.

1. Wage determinations for power equipment operators on federally financed projects throughout Maine were found to be higher than those prevailing in Maine. The Davis-Bacon rates corresponded to union-negotiated rates in Boston, Mass.

2. GAO noted several cases in which regular employees of nonunion contractors worked at or about the same time on private projects and Federal projects and were paid at higher rates on the Federal projects. Comparative wages provided in the GAO report showed that employees working on concurrent projects earned wages on Federal projects that were from 68 to 221 percent higher than on private projects.

The GAO finding is strongly supported by a broader sampling study of Davis-Bacon determinations conducted by Professor Damodar Gujarati in 1965.[8] In an analysis of 372 wage determinations Gujarati found:

[6] Report to the Congress of the United States by the Comptroller General, "Need for More Realistic Minimum Wage Rate Determinations for Certain Federally Financed Housing in Washington Metropolitan Area," transmitted to Congress on September 13, 1968.

[7] Comptroller General's Report to Congress, "Wage Rates for Federally Financed Building Construction Improperly Determined in Excess of the Prevailing Rates for Similar Work in New England Areas" (January 1965).

[8] Damodar Gujarati, "The Economics of the Davis-Bacon Act," doctoral dissertation at the Graduate School of Business, University of Chicago, 1965. Also, see Gujarati's paper, "The Economics of the Davis-Bacon Act," in the *Journal of Business,* XL (July 1967), pp. 303–316.

• An overwhelming number of the wage determinations carried union wage rates. Survey data were almost never used.

• The union rates were frequently "imported" into a locality from noncontiguous counties or from statewide data, in what seems to be a clear contradiction of the language of the act. From 25 to 38 percent of the building construction determinations were based on rates from noncontiguous counties, and 46 to 83 percent of the heavy and highway construction rates were based on noncontiguous county rates. As noted in the GAO study in New England, the Labor Department sometimes went beyond State boundaries for "prevailing" wage data. The tendency to import union rates varied with the size of the county, as noted in the following table adapted from Gujarati's study.

Table 4. Percent of Determinations Based on Out-Of-County Union Rates by County Population [1]

Population	Percent of Out-of-County Union Rates
Less than 2,000	100
2,000– 5,000	94.4
5,000– 10,000	68.0
10,000– 20,000	69.0
20,000– 50,000	57.1
50,000–100,000	39.2
100,000–500,000	39.2
500,000 and over	18.7

[1] Source: Gujarati, "The Economics of the Davis-Bacon Act," pp. 303–16.

The GAO studies also found cases where the Department had misclassified the type of construction. Indeed, in its 1971 report [5], GAO expressed the belief that the Department's use of only three classifications—building construction, heavy construction, and highway construction—represented too broad a set of categories for accurate wage determination. This is particularly the case in building construction.[9] For example, in its study of wage determinations for federally financed housing in the Washington, D.C., metropolitan area [4], GAO stated:

> We found a significant inconsistency in the Department's application of the prevailing wage laws to low-rent public housing projects in the Washington metropolitan area. We noted that most of the minimum wage rates issued by the Department for a low-rent public housing project constructed for NCHA in the District of Columbia were considerably higher than the minimum rates issued for a similar low-rent public housing project constructed in Alexandria, Virginia, for the LHA, the Alexandria Redevelopment and Housing Authority.
>
> In applying different minimum wage rates for these similar low-rent public housing projects within the Washington labor market area, the Department classified the public housing project in the District of Columbia as commercial building construction, whereas it classified the similar housing project in Alexandria as residential housing, which is almost always constructed by private industry at wage rates lower than the wage rates for commercial building construction.

The GAO has also identified deficiencies in the data based used for wage determinations and has also criticized the "30 percent" rule as used by the Department. The GAO studies indicate that the Department has placed undue emphasis on prior determinations and has indicated that this may establish special Federal wage rates higher than prevailing wages. GAO also found, as did the Gujarati study, that union-negotiated rates were applied without obtaining supporting data that such rates were actually paid on the construction projects in the area. In some cases cited by GAO in [5], it is shown that the 30 percent rule has led to inappropriately high determinations. For example, the Department, using the 30 percent rule for carpenters in an area, determined a wage rate of $4.25. This was based on a wage survey in which, of 102 carpenters, only 31 received the $4.25 rate, whereas 71 had rates between $2.50 and $4. The average rate was $3.32, and the $4.25 determination was 28 percent higher than this average. Similar problems were found in the determination of fringe benefits. The GAO also found that the Department did not adequately recognize helper and trainee classifications in its wage determinations.

On the basis of these studies (involving 16 low rent public housing projects, eight military family housing projects, four federally insured housing projects, and one dam constructed by the Corps of Engineers in Georgia), GAO estimated that, as a result of incorrect minimum wage determinations, construction costs were increased from 5 to 15 percent. If this estimate represents a reasonably accurate measure of the extent of error in general, then incorrect wage determinations are costing the Federal Government something like $3 billion a year, given the current levels of Federal construction spending of all types subject to Davis-Bacon determinations.

Data from the 1971 Suspension: Concern over sharply rising construction costs led the

[9] In the 1971 report GAO states that the Department changed its position and has intensified the use of wage determinations for residential-type construction.

President to suspend the provisions of the Davis-Bacon Act from February 23 to March 29, 1971. When the act was reinstated, the Construction Industry Stabilization Committee was established to deal with the problems of rising labor costs in the construction industry. During the period of the suspension, Federal agencies and departments that had gotten bids on contracts subject to the Davis-Bacon prevailing wage provisions were asked to get a rebid without the Davis-Bacon provisions if the contract had not yet been accepted. Thus, data became available which permitted a comparison of bids on identical projects with and without Davis-Bacon requirements.

The Office of Management and Budget asked the Department of Labor to collect these comparative data from the various agencies and departments, and in many cases the reported data are sufficiently detailed to make some useful comparisons.

The comparisons are not entirely of a "controlled experiment" nature, since factors other than the Davis-Bacon suspension affected the change in bids. These other factors include the following:

- The public announcement of initial bids is a source of information to bidders. In particular, the low bidder may have been able to learn that he was excessively low because he had incorrectly understood the provisions of the contract and entered an erroneous bid. The rebidding would give him a chance to correct this error and could lead to an increase in the minimum bid despite the removal of Davis-Bacon minimum wages. Similarly, he may learn that his competitors are not very "competitive" and that he can raise his bid and still get the contract. The effect of information could conceivably go in the other direction; that is, information from the first bid could indicate errors on the high side and could lead to a reduction in the lowest bid even if there were no change in Davis-Bacon minimum wages.
- The number of bidders might influence the change in bids in the sense that more competition may obtain when there is a large number of bidders.
- The extent of unionization will presumably affect the amount of change in bids to the extent that—at least in the short run—suspension of the Davis-Bacon provisions will have little or no effect in areas where high union wage rates are common. In the longer run, nonunion contractors may be more competitive, and this would increase the impact of a Davis-Bacon suspension.

Data from two agencies, the Department of Defense and the General Services Administration, have been analyzed. The Department of Defense reported on a number of contracts that involved jobs ranging from painting and roof repair to heavy construction. The data give the original bid and the rebid for each bidder. The location of the work is also given, and hence it is possible to construct a unionization variable by applying the extent of unionization in the State in which the construction is performed. Similarly, by using the lowest bidder and the next highest bidder on the first bid, it is possible to control in part for the public announcement effect. In cases where the second lowest bidder is quite far from the lowest bidder, we would tend to expect an increase in the low bid on the second bidding round as noted above.

The sample included 76 projects ranging in cost from about $2,000 to over $3 million as indicated by the lowest bids.[10] The percentage change in bids averaged out to a decrease of about .8 percent for the entire sample of 76 bids. The following table indicates, however, that this was significantly affected by the rebidding process and the extent of unionization.

The States with low unionization and bids that are less than 20 percent below the next bidder had an average reduction of 3.476 percent between the first bid and the second bid with the Davis-Bacon provisions suspended. In States with unionization above 30 percent, and when the second lowest bid is more than 20 percent above the lowest bid, the change in bids was an increase of 14.674 percent. The difference between these two numbers is statistically significant (above two standard deviations).

This comparison suggests that information from the first bid is an important factor and confounds the measurement of the effect of the Davis-Bacon suspension. Fortunately, we have a chance to control this problem more directly using data reported by GSA during the period of the suspension. GSA reported on 41 bids and rebids with the Davis-Bacon Act suspended, and on another 15 that were also bid twice but with the Davis-Bacon Act reinstated for the second bid.[11] Hence, for the latter 15 bids (and rebids),

[10] One observation was not used because there was only one bidder (and rebidder) and two or three others were not used because no rebid information was available.

[11] One of the original 42 bids reported by GSA was eliminated because it was obvious that a bidding error had occurred on the first bid and the error was so large as to completely dominate the sample.

the Davis-Bacon Act was in effect for both the first and second bids. This provides a control group to measure the informational affect of rebidding per se.

Table 5. Mean Percent Change in Bid with Davis-Bacon Act Suspended by Extent of Unionization in the State and by the Percent Difference Between Lowest and Next Lowest Bidder

Percent Difference Between Lowest Bid and Next Lowest Bid	Unionization in State		
	Less than 30%	More than 30%	Total
Less than 20%	−3.476	− .462	−2.66
More than 20%	3.667	14.674	5.61
Total	−1.722	1.928	−.809

The mean change in the low bids for the 41 contracts for which the Davis-Bacon Act was suspended was about −5.4 percent. The mean change in the low bids for the 15 contracts where the Davis-Bacon Act was in effect for both bids was about 2 percent. Using the 2 percent increase as a measure of the informational effect of rebidding, the estimated impact of the Davis-Bacon Act is thus about 7.4 percent.

To analyze further the effect of the Davis-Bacon suspension, some ordinary least squares regressions were run. The first simply regresses the percentage change in the bids for the whole sample of 56 observations on a constant and a dummy variable, taking the value 1 when the Davis-Bacon suspension applied and the value 0 otherwise. The estimated coefficient on this variable was about 7.4 percent, as expected from the above calculation of means, and the t-ratio was 1.126, which is significant at about the 25 percent level. When the number of bidders on the second bid is added to this regression, the overall significance as measured by the F-test improves and the coefficient of the Davis-Bacon dummy variable is about 6.5 percent with a t-ratio of about 1.

The picture that emerges from this analysis and GAO studies is that the Davis-Bacon Act, as it has been administered, has raised the cost of construction projects to the Federal Government. The total cost increase appears to be between 5 and 15 percent, and it would appear that in the absence of Davis-Bacon minimum wages such savings could be realized in a relatively short period of time. There is reason is believe that contractors that do not currently bid on government jobs because of the Davis-Bacon provisions would do so in greater number if the provisions were eliminated indefinitely. If so, even greater longrun gains could be expected.

Other Federal Policies

Among the other Federal policies that affect housing costs are those that: 1) encourage or support restrictive work practices; 2) prevent or hinder technological change by means of arbitrary, and in some cases irrelevant, standards and specifications; 3) provide artificial price supports for critical raw materials; and 4) lead to excessive general inflation.

The problems associated with these other policies have been acknowledged in recent years, and some efforts have been made to alleviate them. In 1969, for example, the Government reviewed its policies regarding the lumber industry and found several places where price-moderating activities could be implemented. These included use of Federal timber lands, requests to agencies such as the Department of Defense to reduce demand for lumber when it was not essential, and suggestions for changing transportation patterns. Similarly, efforts have been made through the Federal manpower programs to increase training programs and to facilitate the flow of skilled workers into the construction industry. Through the "Operation Breakthrough" program, efforts are being made to implement productivity increases in housing construction. These policies are discussed in greater detail in Chapter 4 of the 1970 *Economic Report of the President.*

Recommendations for Changes in Federal Policies

The Davis-Bacon Act

As seen in the second section, the Davis-Bacon act as currently administered has led to an appreciable increase in the cost of construction work for the Federal Government. Aside from questions of the desirability of the act per se, much of the problem has arisen because the prevailing wages have not been determined in accordance with the intent or the letter of the law. Clearly, then, changes in the administration of the act are called for. Beyond this, there is a real question as to whether the act should be eliminated either wholly or in part.

The Formula for Defining Prevailing Wages: As noted, the current cutoff point for contracts in which the act applies is $2,000. That is, any contract in excess of $2,000 requires a wage determination. In its 1971 report to Congress, GAO questioned this number and recommended that the minimum be raised to $25,000 or $100,000. This recommendation has great merit, since a large number of contracts are under $100,000, but these account for only a small fraction of the total cost. In GAO's studies, it was found that 45.7 percent of the determinations were for contracts under $100,000, but these accounted for only about .8 percent of the total costs.

This is confirmed by the Defense Department data cited in the second section. Of the 76 projects, 66.5 percent were under $100,000, but these represented only 3.2 percent of the total cost. Thus, substantial reductions in workload and expenses could be realized by the Department of Labor by this change, and the savings could be used to improve the accuracy of the remaining determinations.

The "30 percent" rule is also clearly a source of error in wage determinations. It would seem to be in the spirit of the law to devise a measure of prevailing wages that at the same time did not tend to set an excessively high minimum. Because the concept of the Davis-Bacon-determined wage is to establish a minimum wage that is "prevailing," it would seem reasonable to use a rule which covers all but the lowest paid workers. For example, the minimum wage could be specified as the lowest quartile of the wages in the area—that is, the wage such that 75 percent of the workers in the area made more than this wage. Such a rule would go far to eliminate errors of the kind discussed in "Effects on Wages and Costs," above, and would tend to require more wage surveys.

Importation of wages from noncontiguous counties or from other States appears to be an egregious violation of the law and one that has probably led to many incorrect determinations. Strong efforts should be made to halt this practice, and it would seem desirable to make it explicitly illegal to base determinations on wages from different States or noncontiguous counties.

Greater emphasis of onsite wage surveys is a desirable direction in which to move. In addition, the classifications of workers and types of construction should be broadened. Surveys of such classifications in different geographical areas would be helpful, and greater effort to account for trainee and apprentice-class workers should be made.[12]

It should be noted here that the Department of Labor is aware of these problems and has indicated its interest in correcting them in recent years. In its 1971 report, GAO noted these intentions of the Labor Department but had no firm evidence of how successfully they had been implemented.

The Failure to Administer the Act Properly: In large part, the failure to administer the act properly appears to be attributable to the enormous number of determinations that must be made relative to the staff and budget available to make the determinations. There is a very good chance that progress could be made here by raising the minimum contract price for which Davis-Bacon applies from its current $2,000 to $100,000. As noted above, this could cut the workload by 40 to 70 percent while affecting less than 5 percent of the contracts in terms of total cost.

GAO had suggested in its August 1970 Report that the Department of Labor switch from a cumbersome manual system of making wage determinations to one using automatic data processing. The Labor Department studied this possibility and concluded that the decentralization of responsibility for gathering wage rate data to field offices made the use of an automated system infeasible. This conclusion is hard to accept because there are many instances of "decentralized" systems that successfully employ automated data processing techniques. The solution may involve an alteration in the nature of the decentralization, but there seems to be a strong a priori case for use of automated data processing. The potential savings from more accurate determinations may range from $2 billion to $3 billion annually, and this would appear to justify even a very expensive system of automatic data processing.

The burden of making determinations may be eased by involving the contracting agencies directly in the wage survey and determination process. Efforts to do so were initiated in 1968 and have been at least partially successful. In particular, HUD proposed that the Federal Housing Administration assist the Labor Department in making prevailing wage determinations for

[12] Regulations became effective on January 30, 1972, requiring the employment of apprentices or trainees on certain federal or federally assisted projects and providing minimum wage rates for these employees.

federally assisted residential construction. By October 1970, the HUD plan was in effect and since that time the casual evidence that has become available indicates that the plan has been successful in getting more accurate determinations. It would be very useful to follow up on this plan and to extend it and formalize it where possible. In its 1971 report, GAO suggested the desirability of establishing an interagency committee to collect and exchange up-to-date wage information. An enormous amount of such information is likely to be in the hands of various agencies and departments of the Federal Government, and the benefits from using it for prevailing wage determinations would be substantial enough to justify concerted effort in this direction.

The Desirability of Different Formulas for Different Types of Housing: One of the problems with the determination of Davis-Bacon wages has been the failure to distinguish adequately between different types of construction projects. Thus, it has been the practice of the Labor Department to apply commercial construction rates to residential projects even though the wage rates and labor practices are quite different between these two types. More careful surveys to determine such differences are in order.

Perhaps a more fundamental difficulty with the act is that it often negates the purposes and aims of other Federal programs. As Professor Yale Brozen has pointed out in [1], the Davis-Bacon Act runs counter to the effect of section 221(d)(4) of the National Housing Act, which provides what is in effect an interest rate subsidy for builders of housing for low and moderate income families. Professor Brozen cites cases where such projects have been abandoned because the prevailing wages were set at levels so high as to cancel the effect of the section 221(d)(4) subsidy.

In cases where there is such a conflict between Davis-Bacon and the intent of other legislation, it would be desirable either to suspend or sharply modify the terms of the Davis-Bacon provisions. This could be accomplished by either eliminating the Davis-Bacon provisions from certain pieces of legislation—for example, the bill introduced by Senator Tower in May 1972—or by amending the Davis-Bacon Act itself to allow for exceptions when low rent housing and similar projects are obtained.[13] The former approach would be more expeditious.

[13] The Bill (S.3654, 92nd Congress, 2nd Session) called for the repeal of Section 212 of the National Housing Act and Section 2., Paragraphs (2) and (3) of Section 16 of the U.S. Housing Act of 1937.

The Desirability of Partial or Complete Elimination of Prevailing Wage Laws: The Davis-Bacon Act was passed in 1931, when the country was in a severe economic depression and there was great concern about protecting incomes of workers. The situation has changed dramatically since that time, and there is a real question as to whether the act serves any useful purpose at present. Indeed, there is strong evidence that the act may be harmful because it runs counter to legislation that subsequently has been passed to achieve other goals. Changes in the administration of the act may alleviate the problem, but the record to date does not appear very encouraging in this respect. It has been noted that the act hinders efforts to bring apprentices and trainees into the construction industry, and it often prevents rather than aids contractors from competing on Federal construction jobs in their localities.

The problem of excessively high and rising wages in contract construction has been noted by those who support prevailing wage legislation, but they have often sought other remedies such as the Construction Industry Stabilization Committee for this problem. The evidence seems quite clear, however, that the elimination of the Davis-Bacon Act would have a measurable impact on construction costs, whereas the success of alternative programs seems dubious at best.

Despite the compelling disadvantages in prevailing wage laws, these laws are given strong support by certain groups, and by organized labor in particular. The experience with the 1971 Presidential suspension of the act suggests that it would be difficult to get agreement on repeal of prevailing wage legislation. Nonetheless, it may be possible to get suspension of the act for certain kinds of projects such as public housing or subsidized housing. The economic gains to the country and to the taxpayer of doing so appear to be substantial.

Summary of Recommendations: Following is a summary of recommendations.

- The recommendation put forth by GAO in its 1971 report to the Congress that the minimum contract for which Davis-Bacon applies be raised to $100,000 has great merit. This would reduce the workload of the Department of Labor quite substantially and may facilitate greater accuracy in determinations.

- The "30 percent" rule should be modified in a way which sets a minimum level for prevailing wages.

• The use of wage data from noncontiguous counties or other States in making prevailing wage determinations should be made explicitly illegal.

• Greater use of onsite wage surveys and more detailed classification of workers and types of construction are desirable and necessary for accurate implementation of the act.

• Agencies and departments that are responsible for legislation with prevailing wage clauses should become more intimately involved in the process of wage determination. Efforts that were started along these lines in 1970 should be supplemented and formalized, and regular monitoring of the process should be instituted. An interagency committee responsible for collecting and disseminating accurate wage data would have great advantages in this respect.

• It is hard to believe that some system of automatic data processing could not be used by the Labor Department. Claims that such a system is "infeasible" do not appear persuasive in view of the very large annual savings to be realized by better accuracy in the wage determination process.

• The Davis-Bacon Act runs counter to the objectives of other Federal legislation, and it would be desirable to eliminate prevailing wage clauses from such laws.

Other Policies

Policies that facilitate cost saving technological innovation and the elimination of restrictive work practices would be of great value. The Federal Government has begun to acknowledge that many of its practices and policies tend to raise prices and costs, and some efforts have been made in recent years to correct the situation. At present, many of these efforts tend to be of a temporary and ad hoc nature, and it would be useful to look for more permanent solutions.

Another potential major source of improvement is through greater productivity in construction techniques. This requires effective means of changing outdated zoning and building regulations found in many localities and enlisting the cooperation of organized labor in the introduction of new construction materials and methods that is often hindered at present because of blatant "featherbedding" practices. Much of the testimony presented in [8] deals with these problems.

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Equal Opportunity in Mortgage Lending: Status and Recommendations

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Introduction

More than 5 years have passed since the enactment of title VIII of the Civil Rights Act of 1968, which prohibited discrimination in mortgage lending because of race, color, religion, or national origin, and which imposed an affirmative enforcement duty on all Federal agencies with activities relating to housing and urban development. Yet none of the agencies that regulate banks and savings and loan associations has yet adopted regulations and procedures adequate to investigate and insure compliance with the law.

Instead, they have taken an extremely passive posture, relying mainly on complaints. Reliance solely on complaints is inadequate as a means of enforcing title VIII. Minorities, even if they realized that they had a legitimate cause to complain and knew where to complain, have generally not been disposed to file a complaint because they have had little confidence that the complaint would be resolved in a way that would enable the person to obtain the particular house desired. Moreover, discrimination in home finance can be a very subtle thing. Because so many factors can go into an underwriting decision on a loan, it is very difficult to prove a discriminatory intent in any given particular case. Lenders are now sophisticated enough to know not to tell minority applicants that they will not lend to them because of their race.

Whereas proving discriminatory intent in an individual case is difficult, proving a discriminatory pattern of lending would be easier, assuming appropriate records were maintained. To date, however, Federal regulatory agencies have been unwilling to require appropriate data collection, and they have been unwilling to utilize the existing supervisory mechanism to detect such discriminatory patterns. The regulatory agencies also have been unwilling to require affirmative actions designed to eliminate the effects of past discrimination.

Nor have they acted to prohibit lending discrimination on the basis of sex or marital status, or discrimination against the elderly. Although discrimination because of sex, marital status, or age is not explicitly covered under title VIII, the regulatory agencies have the authority to take action against such discrimination under their own existing regulatory functions. It is important to note that discrimination on the basis of sex or marital status also has particularly sharp impact on minorities. Therefore, such discrimination must be eliminated in order to affirmatively enforce title VIII.

In addition to the financial regulatory agencies, other agencies affect the access of minorities, women, and the elderly to mortgage credit because of the credit guidelines and standards they set in conjunction with their own programs. Although most of these agencies now have written criteria that are basically nondiscriminatory, the extent to which these criteria have been effectively translated into practice remains an open question. In addition, the Veterans Administration still has standards that have a definite discriminatory effect on minorities and women.

The balance of this paper describes various discriminatory lending practices, discusses recommendations designed to overcome such discrimination, and provides an agency-by-agency status report (including, where appropriate, specific recommendations applicable to the particular agency). Finally, there is a brief reference to possible legislation, although all of the basic recommendations of this paper can and should be implemented immediately under existing authority and responsibility.

* This paper was submitted to HUD in June 1973. Although the information contained in the sections of the paper describing various types of discriminatory practices and the general elements needed for a strong nondiscrimination program is still applicable, some of the information contained in the agency-by-agency status report has been superseded by events. These events include the revision of Veterans Administration guidelines relating to counting a wife's income; the promulgation of guidelines by the Federal Home Loan Bank Board dealing with a number of discriminatory underwriting practices and establishing the appropriateness of an "effects" test; and the establishment by the financial regulatory agencies of a pilot program in 18 metropolitan areas to collect data on race, neighborhood, and other variables with respect to mortgage loan applications. Also, legislation has been passed by the Congress prohibiting sex discrimination, including the arbitrary discounting of a wife's income, and prohibiting discrimination on the basis of marital status. Nevertheless, the financial regulatory agencies still have not implemented a nationwide program of data collection essential to the effective enforcement of the Civil Rights Act of 1968.

Description of Discriminatory Lending Practices

A number of recent studies have demonstrated the widespread existence of the continuance of many discriminatory practices by the Nation's mortgage lenders—practices that result in the denial of home financing opportunities to racial minorities, women, and the elderly. The two most important surveys consist of a report released in April 1972 by HUD, and a survey released in March 1972 by the Federal Home Loan Bank Board.

Racial Discrimination in General

The HUD report, which was a preliminary report on returns from a private lending institution's questionnaire, provided an indication of the significant underrepresentation of minorities in loans made by mortgage lenders. The questionnaire has been mailed to 18,456 lenders, and there was a 91 percent response rate.

Lenders were asked to provide a rough estimate of the percentage of loans made to minorities. An analysis was made of responses by savings and loan associations in the 50 cities with the largest minority population. Of the 39 million total population for these cities, minorities constitute a 36 percent average population for all of the cities combined. (The cities themselves range from 16 percent to 74 percent minority population.) However, 29 percent of the savings and loans estimated that they make less than 5 percent of their loans to minorities, and another 31 percent estimated that their loan production to minorities was between 5 percent and 15 percent. A very high 16 percent failed to provide any estimate at all. Only 13 percent indicated that their loan production to minorities was between 15 percent and 25 percent of their loans and only 11 percent of the savings and loans indicated that minority loans totaled more than 25 percent.

In analyzing these figures, the HUD report stated: "Of course minority homeownership is generally less than proportional to minority population, but even allowing for this fact, the figures are striking."

The underrepresentation of minorities in the loan production of savings and loans is caused not only by invidiously discriminatory practices, but also by obsolete practices that, although appearing neutral on their face, have a clear discriminatory impact. A further factor that contributes to the underrepresentation is that lenders fail to market their services in a manner designed to attract minority customers. And even if minorities do happen to seek out a lending institution, they may be discouraged unnecessarily at the oral inquiry stage, so that they never get to file a formal application.

Discrimination Against Minorities Seeking Loans in White Residential Areas

The low number of loans made to minorities does not define the extent of the problem. A practice of discouraging loans to minorities in white residential areas, or of discouraging loans to whites to purchase homes in areas in transition from white to black, has the effect of both causing and perpetuating segregated residential patterns. Even a special program ostensibly designed to help disadvantaged citizens can have certain negative effects unless care is taken to assure that access by minorities to white residential areas is not denied. For example, hearings by the Senate Antitrust and Monopoly Subcommittee (September 1971) documented the "line" of the Boston Banks Urban Renewal Group (BBURG), which restricted utilization of a federally insured homeownership program to one clearly delineated area of Boston. This had the effect of continuing restrictions on the housing options of minorities and fostering harmful speculation and blockbusting.

Application of More Stringent Loan Terms to Minorities

Although it is a violation of Federal law to discriminate on the basis of race in the setting of terms or conditions of loans, 4 percent of savings and loans responding to the survey by the Federal Home Loan Bank Board actually admitted that they require a lower loan/value ratio on loans to minority group applicants, and 4 percent admitted that they require a shorter term to maturity on loans to minorities.

Redlining and Other Types of Neighborhood Discrimination

The arbitrary "redlining" or writing off of entire areas of a city as unacceptable for mortgage credit is a serious problem restricting equal access to mortgage financing and contributing to urban decay. It is true that there are some neighborhoods where rapid decline of property values or a rapid rate of abandonment could justify a practice of not making loans available on the same basis as in other neighborhoods. However, the decay of a neighborhood can be set in motion by the withdrawal of mortgage investment. Thus, such withdrawal can create a self-fulfilling prophecy.

It is a discriminatory practice to redline or otherwise restrict access of a neighborhood to mortgage credit on the basis of the racial composition of the neighborhood or on the basis of the average income of neighborhood residents. Yet in the Bank Board survey referred to above, 30 percent of the responding savings and loans answered "yes" to the question: "Do you disqualify some neighborhoods from lending because they are low income or minority group areas?" Twenty-eight percent stated they require a lower loan-to-value ratio in low income or minority group areas (an average of 12.5 percent lower); 32 percent stated that they require a shorter term (7.5 years shorter on the average), and 11 percent stated that they require a higher interest rate (0.5 percent higher on the average).

In the HUD survey referred to above, 17 percent of the savings and loans stated that the racial or ethnic characteristics of the neighborhood were considered in evaluating loan applications, and 20 percent stated that income levels of neighborhood residents were considered.

In addition, a recent case study of mortgage disinvestment in Bronx County (Devine, Richard J., *Where the Lender Looks First: A Case Study of Mortgage Disinvestment in Bronx County, 1960–1970,* National Urban League, 1973) found that the racial composition of a given area had a significant bearing on the number of mortgages made.

Refusal to Participate in Federally Insured or Subsidized Programs

Many savings and loans and other traditional lenders have abdicated their responsibilities by refusing to participate in insured or subsidized programs that minorities and lower income families rely on most heavily. These refusals are clearly not dictated by business necessity, since the lender is protected by Federal insurance. This abdication of responsibility by traditional lenders, such as savings and loans, has been a factor contributing to the increased default rates caused by scandals in certain FHA programs in Detroit and elsewhere. The vacuum left by the withdrawal of savings and loan associations allowed mortgage companies to come in and dominate the market. In its report on the Detroit situation, the Subcommittee on Legal and Monetary Affairs (House Government Operations Committee) blamed part of the problem on the interim lender nature of mortgage companies—institutions that rely almost entirely on the funds of some other investor, and therefore do not have much of a permanent stake in the transaction. This facilitated the involvement of speculators and other fast buck artists.

Discrimination Because of Sex or Marital Status

The most serious manifestation of sexism in mortgage lending is the widespread practice whereby many lenders routinely discount or totally ignore a working wife's income in computing family income, particularly if she is of "childbearing age." This widespread practice results in the denial of loans to many families. In addition, many families are forced by this practice to accept less desirable homes.

Results from the Bank Board survey document the widespread existence of this practice. Savings and loan managers were asked what credit they would allow for a working wife's income if she were 25 years old, had two schoolage children, and worked full time as a secretary. Fully 25 percent of the savings and loans responded by saying that they would count none of her income. Well over half reported percentages of 50 percent or less. Only 22 percent indicated they would give full credit to her income. A survey released in May 1972 by the United States Savings and Loan League yielded similar results.

The arbitrary practice of discounting all or part of a working wife's income has a sharp discriminatory impact on minority groups, where the wife's income often represents a significant contribution to the family's income. Recent data from the Bureau of Labor Statistics verify this discriminatory effect. The labor force participation rate for nonwhite wives is 52.5 percent, as contrasted with a 39.7 percent rate for white wives. In the key age group, 25 through 34, the corresponding percentages are 59.4 percent and 38.0 percent.

Presumably, discrimination against a working wife's income is based on the assumption that she may have a child and quit working. This assumption ignores changing social conditions, the sharp trend toward increased employment of women, and the increased availability of liberal maternity leave policies. It also assumes that people are devoid of common sense and cannot rationally plan their lives—that they will deliberately quit work or refuse to return to work even if this would mean a loss of their house due to foreclosure.

The one empirical study of mortgage delinquency that dealt with the issue of families with two wage earners clearly does not support those who discriminate against a wife's income. The study by Leon Kendall *(Anatomy of the Residential Mortgage,* United States Savings and Loan League, 1964, p. 66) indicated that, if anything, loans to families where the husband's income accounted for 100 percent of family income actually had a slightly higher likelihood of being delinquent than loans to families where the husband's income was only a portion of family income.

The Bank Board survey also revealed widespread discrimination on the basis of marital status, a practice that has a discriminatory effect on both women and racial minorities. Sixty-four percent of the savings and loans admitted that marital status was used as a factor in evaluating loan applications, and 18 percent indicated that a person's marital status, in and of itself, could be grounds for automatic disqualification. Yet a 1970 study by John Herzog and James Earley for the National Bureau of Economic Research, entitled *Home Mortgage Delinquency and Foreclosure,* found no demonstrable relationship between marital status and mortgage loan risk.

Other Practices that Have a Discriminatory Effect on Minorities

There are a number of other needlessly restrictive underwriting practices known to exist that, although neutral on their face, have a discriminatory impact on minorities. For example, some mortgage lenders use isolated credit difficulties or credit difficulties in the distant past as a bar. This practice has a discriminatory effect on minority families who may have been the victim of harsh credit practices in the past.

Some lenders use the existence of a prior criminal record as an absolute bar. In fact, some use a prior arrest record (12 percent in the Bank Board survey), even if there was no conviction, as grounds for absolute disqualification. Because racial minorities are more subject to arrest, often without cause, than are whites, this arbitrary rule operates in a racially discriminatory manner.

Many lenders tend to discriminate against loan applicants who have not previously owned their own home. Again, this has the effect of perpetuating past discrimination against minorities.

Another practice that has a discriminatory effect is the refusal to count stable income from overtime, production bonuses, or part-time work; this penalizes those who are working the hardest to improve their living conditions.

Finally, some mortgage lenders impose overly restrictive payment-to-income ratios, or use payment-to-income ratios in an inflexible manner. This has the effect of discriminating against those in the lower income range of the market who tend to devote a greater portion of income to basic necessities such as housing.

Discrimination Against Older Citizens

Many lenders refuse to make loans (or impose stringent terms on loans) to borrowers approaching their senior years. The survey released in May 1972 by the United States Savings and Loan League revealed that almost 8 percent of the responding savings and loans use a rule of thumb that the age of the borrower plus the term of the loan should not exceed 65. Many lenders use other similar rules of thumb—that the age of the borrower plus the loan term should not exceed 70, 75, or 80 years. Considering that the average term for conventional loans now exceeds 25 years, it is obvious that a borrower whose age is 50 or 55 may be under a severe handicap in obtaining a loan, and a borrower over the age of 60 may find it almost impossible. The U.S. League survey also revealed that almost 15 percent of savings and loans require, as a general rule, a cosigner on loans to senior citizens.

There is absolutely no economic justification for these practices. In fact, Kendall's study concluded: "Once the 40th birthday is passed, experience improved markedly, and, generally, as age increased, payment experience improved. The most favorable experience was on loans made to individuals 60 years of age and over." (See p. 38)

Even if a borrower is expected to retire during the early years of the mortgage, he or she should be favorably considered where circumstances indicate that there will be sufficient financial resources from cash-on-hand, investments, continuing life insurance benefits, retirement benefits, and similar income to reasonably assure repayment of the loan during the early years of the mortgage when the lender is most exposed to the possibility of financial loss.

General Administrative Recommendations

Regulatory Agencies

The agencies that regulate lending institutions should take vigorous action to implement their mandate for affirmative enforcement of title VIII of the Civil Rights Act of 1968. The banking and savings and loan industries are unusual in that they are already subject to extensive regulation, including regular examinations of lenders by the regulatory agencies. Thus, there is a great potential for effectively dealing with discrimination in mortgage lending by making use of the regulatory structure already established.

The basic elements of an effective "equal opportunity in lending" program are as follows:

Racial Data Collection: An essential foundation for such a program of enforcement is the establishment of a system of racial data collection with respect to loan applications. Without such a recordkeeping system, it is impossible to have an effective system for revealing and measuring discriminatory practices, to enforce nondiscrimination regulations, or to evaluate their effectiveness in increasing housing opportunities for minorities.

Racial data collection should be used for comparative analyses of local, regional, and national mortgage lending practices, as well as being an integral tool for examiners in checking on compliance of individual institutions. The system of data collection must be sophisticated enough to measure discrimination that occurs in many forms, including various types of discrimination based on neighborhood, sex, or marital status, discrimination in loan terms, and so on. Recordkeeping should also include a procedure for obtaining racial data with respect to oral inquiries made in person but which do not result in the filing of a written application.

Prohibiting Sex Discrimination and Other Practices That Have a Discriminatory Effect: Through regulations and guidelines, the financial regulatory agencies should make clear to regulated institutions that the full range of discriminatory practices described in this paper are prohibited. The basic principle should be that once a practice is shown to have a discriminatory effect on a protected group, the practice should be outlawed unless the lender can demonstrate that it is clearly dictated by business necessity. The use of an "effects test" has been applied often with regard to civil rights in both constitutional and statutory interpretation (see, e.g., *Griggs* v. *Duke Power Co.,* 401 US 424 (1971)). A recent example of the use of an effects test in civil rights can be found in the regulations of the Treasury Department implementating the general revenue sharing program (see 38 F.R. 9138 51.32(2)).

Individual lending institutions should be required to publish an explanation of their own nondiscriminatory underwriting criteria and lending policies so that applicants will have some basis on which to determine whether or not they have been treated fairly.

Affirmative Marketing to Attract Minority Customers: Lending institutions should be required to institute affirmative marketing designed to attract minorities and convince them that they are welcome customers. Each lender should be required to indicate its nondiscrimination policy in all of its advertising and public relations material. Further, an essential part of any effective affirmative marketing program would be to advertise in media that reach the minority market. Another critical element of an affirmative marketing program would be to establish working relationships with brokers and other agents who serve members of minority groups.

Lenders should be prohibited from discriminating in the conduct of any aspect of their business, not simply in mortgage lending. If a minority applicant has encountered discrimination when applying for a consumer loan, he or she will be discouraged from subsequently applying for a home mortgage loan. Also, the inability to develop a credit rating in conjunction with smaller loans may be a handicap should the applicant subsequently apply for a mortgage loan.

Obtaining Nondiscrimination Assurances From Builders and Developers: When the marketing is to be done by a builder or developer, the lender should be required to obtain nondiscrimination assurances from such builders and developers, a statement of the marketing plan to be used, and followup racial occupancy reports. It would not be the function of lenders to operate as "policemen," but rather they would obtain assurances that their financial resources were not to be utilized to support illegal practices.

Affirmative Employment Programs: The regulatory agencies should adopt the recommendations made by HUD in its April 1972 report, which stated that "the regulatory agencies should develop standards or advisory guidelines to aid regulated institutions to implement an affirmative equal employment opportunity program especially in those job categories (e.g., appraiser and loan officer) which can influence an association's lending practices." The HUD survey of lending institutions discovered very low levels of minority employment, with the underrepresentation especially severe in such key positions as loan officers and appraisers (where minority employment is only 3 percent).

Enforcement: In the final analysis, a nondiscrimination program such as outlined above will only be effective if regulations and guidelines were vigorously enforced. The key to an effective enforcement program is the utilization of the regular examination process, along with a willingness to impose sanctions where violations persist. Examiners should be trained to make thorough searches of a lender's files, and to make use of available data, in an effort to detect discriminatory practices. The major financial regulatory agencies have at their disposal a range of potentially effective sanctions, including cease and desist orders and termination of insurance.

Agencies that Publish Their Own Credit Standards in Conjunction With Their Programs

In order to further equal opportunity in lending, agencies that administer mortgage loan programs of their own should: (1) Review and revise their credit standards to insure that they are clear and nondiscriminatory (this should not merely be a one time review but a continuing review process aimed at opening up new opportunities); (2) take steps to assure that local underwriters are properly trained in the use of nondiscriminatory underwriting criteria and that lenders are made aware of the nondiscriminatory criteria; (3) collect and analyze detailed data on loans made under the program; and (4) make clear to lenders that the agency will not do business with lenders who discriminate on the basis of race, color, religion, national origin, sex, or marital status.

Agency-by-Agency Analysis

There follows a status report on eight Federal agencies with respect to the general recommendations set forth above, including, where appropriate, more specific recommendations for these agencies.[1] Of the eight agencies, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation (FDIC), the Comptroller of the Currency, and the Board of Governors of the Federal Reserve System are regulatory agencies. The other four, the Veterans Administration (VA), the Federal Housing Administration (FHA), the Federal National Mortgage Association (FNMA), and the Federal Home Loan Mortgage Corporation (FHLMC), fall principally in the second category—agencies that administer their own mortgage loan programs. However, with respect to mortgage bankers, FHA has some of the characteristics of a regulatory agency as well.

Federal Home Loan Bank Board

On April 27, 1972, the Federal Home Loan Bank Board (which regulates the savings and loan industry) published regulations (37 F.R. 8436) adding a new "Part 528-Nondiscrimination Requirements" to the regulations of the Federal Home Loan Bank system. The regulations prohibit lending discrimination because of race, color, religion, or national origin, and include a specific provision prohibiting discrimination based on the racial composition of a neighborhood. Discrimination is also prohibited in connection with application procedures and inquiries. In addition, the regulations (a) prohibit the use of words or other symbols in advertising that imply or suggest a discriminatory policy, (b) require an equal housing lender logo in advertising "other than for savings," (c) require the posting of an equal housing lender poster in the lobby, and (d) prohibit discrimination in employment by member institutions.

Deleted from the regulations was the key section on racial data collection. Such a section was included in the proposed regulations published in January 1972. However, in implementing the regulations in April 1972, the Board stated that it was deferring final consideration of the data collection provision "pending further staff study of comments received and consultation with the other financial regulatory agencies." As of this writing, no action has been forthcoming. Thus, although the Board's regulations have been in effect for more than a year, no mechanism for effective enforcement or for measuring their impact has been established.

The regulation as enacted does not deal with problems of sex discrimination in lending, although the Board has acknowledged its authority to act in this area. Nor does the regulation impose affirmative marketing requirements on

[1] Not all of the agencies with equal opportunity in mortgage lending responsibilities are analyzed in this paper. For example, no analysis is made of the Farmers Home Administration, the National Credit Union Administration, and the Farm Credit Administration.

savings and loans (in fact, even the impact of the equal housing lender logo in sharply limited by the loophole that exempts advertising for savings), require the obtaining of nondiscrimination assurances from builders and developers, nor impose affirmative employment responsibilities on savings and loans. (The Board does have, however, a voluntary program, "Vanguard," designed to recruit minorities for savings and loan employment, and, as noted, all member institutions are prohibited by the Board's regulations from discrimination in employment.)

The regulation as enacted makes no reference to the far-ranging problems of underwriting and other lending policies that are restrictive in nature and that have a discriminatory effect on minorities, women, and the elderly. However, the Board's staff has subsequently drafted "Guidelines Relating to Nondiscrimination in Lending" that deal with the full range of discriminatory lending policies described earlier in this paper. These guidelines were approved by the Board's General Counsel in November and were submitted to the Board for enactment. However, final action has not yet been forthcoming.

If the guidelines are enacted by the Board in their present form, and if the Board's examination program should be revised to include a review of compliance with the guidelines, there is great potential for effectively dealing with the basic discriminatory credit practices.

In addition to implementing an effective racial data collection system, the comprehensive lending policy guidelines, and the other basic recommendations, the Board, by virtue of its regulation over an industry that specializes heavily in home finance, is in a unique position to take steps to help meet the housing needs of the Nation's disadvantaged citizens. For example, the Board should restructure its advances system to provide maximum encouragement for savings and loans to meet their social responsibilities. This can be done through a system of differential advance rates, with savings and loans being rewarded with bargain rates depending on their contribution to meeting the social needs of their community by making certain types of loans or engaging in special projects. Lower advance rates can be financed partly by reducing the dividend paid on Federal Home Loan Bank capital stock.

Federal Deposit Insurance Corporation

Currently, the FDIC (which regulates State banks that are not Federal Reserve members) has issued a statement of policy (37 F.R. 8908) that sets forth advertising provisions (similar to the provision in the Federal Home Loan Bank Board's regulations) and a requirement for an equal lending lobby notice. Because a lobby notice is required anyway by HUD's Part 110—Fair Housing Poster (37 F.R. 3429), the only affirmative provision specifically added by the FDIC is the provision for indicating the bank's policy of nondiscrimination in advertisements for home mortgage loans. This is totally inadequate and does not begin to meet the basic requirements for affirmative enforcement of title VIII.

On September 20, 1972, FDIC published (37 F.R. 19385) proposed regulations dealing with fair housing lending practices. The proposed regulations are similar to the regulations now in effect for the Federal Home Loan Bank Board, except for the critical difference that the FDIC proposal contains the key provision for the collection of racial data with respect to loan applications. (One weakness of the FDIC proposal in comparison to the Bank Board's regulations is the omission, in the FDIC proposal, of a prohibition of employment discrimination by all banks under FDIC supervisory authority.)

With the exception of racial data collection, all of the criticisms of the Bank Board's regulations are applicable to the FDIC proposal. These include the failure to deal with sex discrimination and other discriminatory credit underwriting practices, the loopholes in the advertising requirements and the failure to impose affirmative marketing requirements, the failure to require nondiscrimination assurances from builders and developers, and the failure to require affirmative employment programs.

The FDIC racial data collection provision contains a serious weakness by including language that would have the effect of discouraging full reporting of the requested information. Another weakness is the omission of any minimal requirement for recordkeeping in connection with oral inquiries made in person but which do not result in a written application. Although discrimination in connection with such inquiries is specifically prohibited under the proposed regulations, the lack of any recordkeeping requirement makes such a provision impossible to enforce effectively. A strong point of the FDIC recordkeeping proposal is the proposed requirement for notation of the census tract number in which the property is located. For metropolitan areas, this requirement would make it possible to check for various types of discrimination related to neighborhoods.

In December 1972, FDIC held a hearing on its proposed regulations, and specifically added to the agenda of the hearing were consideration of the authority and desirability of: (1) Prohibiting lending discrimination because of sex; and (2) prohibiting discrimination in any lending practice (not mortgage lending alone).[2]

In the months that have passed, however, no action has been forthcoming to implement either the proposed regulations or the additional provisions suggested.

Comptroller of the Currency

As with FDIC, the only civil rights provision now in effect is a policy statement (37 F.R. 10518) relating to advertising and poster procedures and almost identical to the FDIC policy statement. Unlike FDIC, however, the Comptroller of the Currency (which regulates national banks) has not even published proposed regulations. On December 29, 1971, both FDIC and the Comptroller published notices of intention to consider the advisability of regulations and asked for comments. However, when FDIC published its proposed regulations in September, 1972, the Comptroller did not follow suit.

The basic recommendations of elements necessary for an effective nondiscrimination program apply with equal force to the Comptroller of the Currency.

Board of Governors of the Federal Reserve System

On December 29, 1971, the Board of Governors (which regulates State Chartered Member Banks) published (36 F.R. 25168) a "Civil Rights Nondiscrimination Statement," including advertising and poster requirements. (The poster was revised slightly by a notice on April 28, 1972, 37 F.R. 8571.) The advertising and poster provisions for all four agencies are basically the same.

In its notice in December of 1971, the Board of Governors noted other steps undertaken by the Federal Reserve System including: (1) The use of a civil rights questionnaire in all bank examinations; (2) a special course of study on the requirements of the Civil Rights Act of 1968 in Federal Reserve schools for bank examiners; and (3) bank examiner inquiry into bank compliance with Equal Employment Opportunity requirements of the Civil Rights Act of 1964.

The civil rights questionnaire asks for various estimates, such as the number of applications from minorities and the number of loans made to minorities. But in the absence of racial recordkeeping requirements, the examination procedure is crippled in what should be its basic function of checking compliance with the Civil Rights Act. In addition, the Federal Reserve has taken no action to deal with lending policies that have a discriminatory effect on minorities, women, or the elderly, and has taken no action to implement any of the other basic recommendations applicable to financial regulatory agencies.

Federal Housing Administration (FHA)

Subsidized Housing: Of course, the moratorium on subsidized housing programs has a sharp discriminatory impact on minorities, who often need to rely on subsidies in order to obtain decent housing. Thus, the reinstitution of subsidies is a priority of the highest order, and it must be reinstituted in a manner designed to promote integration and equal opportunity.

Credit Standards: For the most part, FHA's credit underwriting standards are sound and nondiscriminatory. The increased default rate in some FHA programs has been associated with widespread fraud involving significant overappraisals of property value. Studies by George von Furstenberg (*Technical Studies of Mortgage Default Risk: An Analysis of the Experience with FHA and VA Home Loans During the Decade 1957–66,* Center for Urban Development Research, Cornell University, Ithaca, N.Y., 1971) have demonstrated, as a general principle, the sensitivity of default risk to loan-to-value ratio, particularly at very high loan-to-value ratios. In cases where fraud has led to overappraisals so that the ratio of the amount of the loan to the actual value of the house exceeded 100 percent, 120 percent, or more, an abnormally high default rate is to be expected.

FHA's credit underwriting standards themselves are basically good, although there are several areas where revisions should be made to encourage nondiscrimination. For example, the entire paragraph 2–7, *Family Life and Relationship,* on page 2–5 of FHA's Mortgage Credit Analysis Handbook, needs revision. As currently worded, it invites the rejection of loan applicants

[2] For further analysis of the FDIC proposed regulations as well as the other issues raised in conjunction with the hearing, see the comments submitted to FDIC November 1, 1972, by the Center for National Policy Review on behalf of 13 original petitioners and 15 additional organizations; the testimony of William L. Taylor, Director of the Center, at the Hearing; and the testimony at the FDIC hearing by Malcolm E. Peabody, Jr., Acting Assistant Secretary for Equal Opportunity, Department of Housing and Urban Development.

based on an underwriter's subjective concept of "inharmonious domestic relationships," even if the applicant has a satisfactory credit record and income adequate to support the monthly payments. Particularly objectionable is the suggestion of discrimination on the basis of marital status contained in paragraph 2–7(a).

Another paragraph that should be revised is 2–11, *Motive for Continuing Ownership,* on page 2–9. As currently drafted, there is a great possibility for abuse, with underwriters disqualifying an applicant because of lack of conformity to the underwriter's own notion of proper values or lifestyles. An example of this is the testimony of Quinton Wells before the National Commission on Consumer Finance last year in which he indicated that a single man or woman without dependents would be rejected for a loan involving a three-bedroom house even if the applicant had a favorable credit record and adequate stable income.

Particularly subject to abuse is paragraph 2–11(d), which suggests disqualification of mortgagors who apply jointly if they are "unrelated or who, though related, have no particular family responsibility to each other." Since household relationships in minority families often are not "traditional" according to the norm of the white community, such a policy could have a discriminatory impact on minorities.

Data Collection: FHA maintains a fairly comprehensive data system with respect to characteristics of those participating in FHA programs. Racial data is now being collected, but there is a need to integrate racial data with other aspects of the data system. Also, FHA should collect data not only with respect to loans made, but also with respect to loans rejected, for the purpose of comparative analyses.

Counseling: In order to expand opportunities for minorities and others to participate in FHA programs, there is a need for an expanded and thorough counseling program to assist prospective homeowners in preparing for the responsibilities of homeownership and budget planning.

Regulation of Mortgage Bankers: In addition to its function of administering its own program, FHA has undertaken to exercise a certain amount of regulatory control over mortgage bankers in conjunction with certifying mortgage bankers as approved mortgagees under section 203 of the National Housing Act. Because mortgage bankers are not regulated by any other Federal agency, FHA has promulgated some regulations with respect to mortgage bankers (see 24 CFR section 203.4(c) and (d) under the headings "nonsupervised institutions" and "loan correspondent mortgagees"). To retain the status of approved mortgagee, mortgage bankers, under these regulations, are required to file annual audits with the FHA Commissioner and "shall submit at any time to such examination of its books and affairs as the Commissioner may require; and shall comply with any other conditions that the Commissioner may impose" (24 CFR 203.4(c)).

These regulations apply to all activities of mortgage bankers, not simply their participation in FHA programs. Thus, the same basic elements of a nondiscrimination program that should be implemented by the financial regulatory agencies should be made applicable by FHA to mortgage bankers. It is true that, in practice, FHA examination of mortgage bankers has been haphazard. And so the current bureaucratic structure leaves something to be desired as a potential civil rights compliance machinery. (Also, the emergence of the 95 percent conventional mortgage probably means that the potential sanction of withdrawal of approved status is not quite as strong as it once was.) Nevertheless, FHA can require, as part of the normal reporting requirements, the submission of racial data and other information indicating compliance wth nondiscrimination regulations; where such reports raise questions, onsite examinations can be conducted.

Veterans Administration (VA)

Credit Underwriting: The credit standards used by the VA in its home loan program need substantial revision to remove discriminatory features and to increase the opportunity of veterans, particularly minority veterans, to utilize their eligibility. Generally speaking, the standards set forth by VA are much more restrictive than corresponding criteria enunciated by FHA, FHLMC, and FNMA.

In some cases, the VA standards are applied in practice in an even more restrictive manner than is indicated by the written standard. Also, there is a great deal of diversity from among local field stations in the manner in which credit standards are applied. These problems also need to be addressed.

The most serious problem in VA underwriting is discrimination against the income of working wives. Unlike the policies of other agencies, VA standards indicate that a wife's income can be discriminated against on the basis that she is of childbearing age. Also, for even any part of a wife's income to be considered, it must be concluded that her income "will continue in the foreseeable future." By contrast, FHA only requires that her employment "may normally be expected to continue through the early period of mortgage risk," and FHLMC requires that she "will probably work for several years."

Other sections needing revision and clarification in VA credit standards include the provisions concerning overtime pay and part-time jobs, the use of the concept of "balance of income available for family support," the comparison of proposed housing expense with previous housing expense, the section on judging an applicant's credit rating, and the references to the age of the veteran. For a detailed analysis of VA credit standards as contrasted with the policies of other Federal agencies, see the April 1973 memorandum of the Center for National Policy Review entitled *VA's Restrictive Credit Practices —Comparative Analysis with Policies of Other Federal Agencies.* VA has indicated that it intends to make changes in its credit standards, but no details are yet available.

Data Analysis: VA is now collecting racial data on its loan programs and preliminary data are available. However, there is a continuing need to develop a more comprehensive data analysis system, including detailed data on borrower and loan characteristics for accepted and rejected loans, detailed information analyzing the reasons for loan rejections, and data to indicate, on both a national and local basis, how underwriting standards are actually being applied, e.g., how the income of working wives is being treated in the underwriting process. In addition, for loans processed automatically, VA should use a spot check system to assure that lenders are not using discriminatory underwriting standards.

Civil Rights Requirements: VA regulations already make clear that racial discrimination constitutes grounds for suspension of approval of a lender from participation in VA loan programs. Discrimination because of sex or marital status should be added as grounds for suspension.

Federal National Mortgage Association (FNMA)

Underwriting Guidelines: Although FNMA's credit and property underwriting guidelines for its secondary market program for conventional loans are basically free of discriminatory features, in several respects they are vague and should be revised to prevent possible misinterpretations.

Particularly vague is the section dealing with counting income in the case of a joint application of husband and wife where both work. The FNMA guideline states: "The key determination to be made is whether the circumstances reasonably indicate that the income, jointly or severally, will continue in a manner sufficient to liquidate the debt under the terms of the note and mortgage." In a series of meetings with mortgage lenders last year, FNMA generally gave liberal interpretations to this guideline. However, because the practice of arbitrary discounting of all or part of a wife's income has been shown to be so widespread, FNMA's guideline should be revised and made more explicit to indicate that a wife's income should be fully counted if it may normally be expected to continue during the early years of the mortgage, and to make clear that the possibility of pregnancy is not a legitimate basis upon which to discount income.

FNMA should clarify its section on overtime pay, bonuses, and part-time jobs. Currently, such income "may be considered as effective income if it can be determined to be reasonably certain and of a continuing nature." It should be made clear that this means that such income should be counted if it is likely to be stable during the first few years of the mortgage. In addition, FNMA should amend Section 311.03(g), Borrower's Credit Ratings, to include a more positive statement to the effect that a period in the past containing financial difficulty does not make the risk unacceptable if the general pattern of recent credit behavior has been favorable.

FNMA's guidelines state: "FNMA has not and will not designate certain areas as being acceptable or unacceptable to FNMA, e.g., it will not 'redline.' " However, other language in the guidelines could possibly be interpreted as giving lenders an invitation to do their own redlining. Fortunately, in their meetings with mortgage lenders last year, FNMA officials generally indicated that arbitrary redlining was an unacceptable practice and would be considered a violation of FNMA's civil rights requirements. This interpretation should be made explicit in writing.

FNMA's Section 311.04(B)(2) states: "Each property must contain sufficient square footage to be acceptable generally in the area in which it is located." FNMA should make clear that by "area" it means "market area" and not necessarily the specific neighborhood. Otherwise, some lenders might interpret this sentence as encouraging the development of only homogeneous neighborhoods.

Civil Rights Requirements: Section 103 (Equal Opportunity) of the FNMA Conventional Selling Contract Supplement refers to the Federal Fair Housing Law and states:

> A seller shall demonstrate its capability and willingness to assure equal treatment in accordance with this law by the securing and furnishing to FNMA of racial and ethnic data on FNMA Form 1003 for mortgages submitted to FNMA for purchase.
>
> To assure the carrying out of the goals of equal opportunity, FNMA will require sellers to maintain appropriate records for a minimum of one year, whether involving mortgages submitted to FNMA for purchase or not, which records shall be available to FNMA, upon request, in order to determine that the seller's loan production to minorities is consistent with the goal of equal treatment.

While implied, there is no clear statement in section 103 that lenders who discriminate will be barred from doing business with FNMA. An additional civil rights provision is in section 701(p) of the FNMA Conventional Selling Contract Supplement requiring the seller to warrant to FNMA, with request to each mortgage sold, that the mortgagor has not been discriminated against in the fixing of the amount, interest rate, duration, or other terms or conditions of the loan, because of the race, color, creed, religion, sex, age, or national origin of the mortgagor. This provision comes close to saying that FNMA will not do business with lenders who discriminate, although it does not go the full distance because, strictly speaking, it only applies to loans actually made by the lender and purchased by FNMA. This loophole should be closed, and the phrase "marital status" should be added.

Data Analysis: FNMA's provision requiring the furnishing of racial data provides an excellent opportunity for a comprehensive data analysis system analyzing racial data in conjunction with data on income, debt-to-income ratios, sex, age, neighborhoods, loan-to-value ratios, and other variables to determine in detail the kinds of borrowers and terms associated with mortgages benefitting from FNMA purchases. (With the exception of data on census tracts, the basic data needed for a comprehensive data analysis system are readily available from FNMA forms.) The analysis should include data on loans rejected for purchase as well as loans accepted, and should include the collection and analysis of data indicating certain underwriting decisions made by FNMA underwriters (e.g., the treatment of a working wife). In addition, there should be an analysis of loan rejections, with a percentage breakdown of reasons for rejection, including the percentage of mortgages rejected for each reason.

FNMA has not yet committed itself to a comprehensive data analysis system.

Federal Home Loan Mortgage Corporation (FHLMC)

FHLMC's written credit and property underwriting guidelines for its secondary market in conventional loans are basically sound and nondiscriminatory, and contain a number of affirmative provisions. In addition, FHLMC is now in the process of aggregating data on borrower and loan characteristics which should provide some indication of the way in which FHLMC's criteria are being reflected in actual mortgage loans made. This would only be a partially satisfactory data analysis, however, because FHLMC has not as of yet determined to collect data on the race of the borrower and the census tract of the neighborhood. Also, FHLMC needs to collect data on specific underwriting decisions made by its own underwriters.

As far as civil rights requirements are concerned, FHLMC currently states in section 4.2 (Equal Opportunity) of article IV of the Master Selling Agreement Conventional that lenders shall comply with title VIII of the Civil Rights Act of 1968. Presumably, FHLMC would refuse to purchase mortgages from lenders known to be violating the act. FHLMC should add a specific provision to make clear that it will also refuse to purchase mortgages from lenders who discriminate because of sex or marital status.

Finally, although FHLMC's written guidelines are basically nondiscriminatory as far as they go, there are several places where more explicitness or inclusion of a specific positive statement would avoid misinterpretations and encourage nondiscrimination. These would include, for example, a positive statement on making loans to the elderly, a positive statement indicating that the age of the home is no limitation as long as the term of the mortgage is appropriate in relation to the remaining economic life, and a clear statement to the effect that a period of financial difficulty in the applicant's past does not make the risk unacceptable if the general pattern of recent credit behavior has been favorable.

Legislation

The recommendations in this paper can be implemented under existing authority. In fact, most of them are mandated if the agencies are to meet their affirmative responsibilities under title VIII. Thus, the recommendations should be implemented on a priority basis and need not await further legislation.

Nevertheless, legislation would be desirable to explicitly make illegal discrimination on the basis of sex or marital status, and to specifically cover discrimination against the elderly. An additional desirable legislative initiative would be to strengthen the regulation of mortgage bankers by establishing a general regulatory responsibility with FHA or some other agency (so that regulation would not be dependent on a mortgage banker's participation in a Federal program) and providing specific enforcement tools such as authority to issue cease and desist orders.

The full implementation of the recommendations in this paper would result in the elimination of obsolete practices not dictated by business necessity, and could encourage mortgage lenders to meet a high standard of social performance. However, these recommendations cannot be expected to do the full job. The test of "soundness" may not be satisfied by all of the investments that are necessary in order to meet the Nation's urgent housing crisis, such as, in particular, investments in a limited number of neighborhoods that have already experienced a high degree of abandonment and deterioration. Addressing such a situation will require a coordinated effort at revitalization, including direct Federal involvement and possibly a forced pooling of financial institution resources.

Mortgage Money: Who Gets It? A Case Study in Mortgage Lending Discrimination in Hartford, Connecticut

By *U.S. Commission on Civil Rights* *

Chapter 1. Why Study Mortgage Lending

Homeownership is a goal most American families aspire to, but which some find difficult or even impossible to achieve. In 1970, 65 percent of all white families owned their homes but only 42 percent of all black families and 44 percent of all Spanish speaking families. In that year 68 percent of all families headed by men owned their homes contrasted to 48 percent of all families headed by women.[1] Discrimination by real estate brokers and mortgage lenders is largely responsible for this disparity.

In 1968, passage of the Federal Fair Housing Law[2] prohibited discrimination against minorities in obtaining mortgage financing. Yet real estate brokers and mortgage lenders still treat minority homebuyers differently from white purchasers. White, male-dominated lending institutions use imprecise, subjective criteria in granting mortgages; and these criteria, such as motivation and eligibility, are applied differentially.

Although most families have some difficulty in obtaining the financing necessary to purchase a home, minority families and women often encounter insurmountable obstacles when they approach the mortgage lending community. A white family headed by a male whose income is sufficient by itself to carry the cost of home purchase conforms easily to the traditional criteria of the lending community and is readily approved. But minority families, families headed by women, families in which both the wife's and the husband's incomes are necessary, and single persons do not fit as well into the traditional perception of homeowners held by lending institutions. Their applications frequently are handled arbitrarily.

During a period of tight money, as at present, restrictive conditions worsen. As the pool of money available for mortgages decreases, fewer families are able to obtain financing. The access of marginal families to money in this situation, including families headed by minorities or women, is even more restricted.

The purpose of this investigation has not been to uncover individual instances of discrimination by mortgage lenders, but to examine the system of mortgage finance and its effect on homeownership opportunities for minorities and women. The Commission has examined a number of the purportedly neutral criteria that govern mortgage loan decisions to determine the extent to which they afford equal opportunity to minorities and women and assure that decisions will be made on the basis of objective factors, not personal or institutional bias.

Measuring the extent to which the mortgage finance system results in discriminatory treatment of minorities and women is a difficult task because data are unavailable, inadequate, or difficult to obtain. The responsibility for requiring data collection of the Nation's lenders rests squarely with the Federal financial regulatory agencies which have long resisted promulgating such a regulation. Many statements and actions of real estate brokers and mortgage lenders that discourage minorities and women from seeking to finance the purchase of a home never become part of a written record. The fact that loan inquiries and application procedures are informal serves to emphasize that ample opportunity exists for discrimination against minorities and women. Although the practices of mortgage lenders are more often covert than overt, they nevertheless have the effect of denying many qualified families the opportunity of homeownership.

* This study was prepared and originally published in June 1974 by the U.S. Commission on Civil Rights and is available as Commission Clearinghouse Publication No. 48.

[1] Department of Commerce, Bureau of the Census, *1970 Census of Housing: Metropolitan Housing Characteristics—Final Report,* no. HC (2)–1 (Sept. 1972), pp. 9, 18. Department of Commerce, Bureau of the Census, *1970 Census of Housing: Housing Characteristics by Household Composition—Final Report,* no. HC(7)–1 (February 1973), pp. 105, 114. See also, Department of Commerce, Bureau of the Census, *1970 Census of Housing: Structural Characteristics of the Housing Inventory —Subject Report,* no. HC(7)–4 (June 1973), p. 2.

[2] 42 U.S.C. §3601 et seq.

This report reflects the Commission's investigation of mortgage lending policies and practices in a demonstrably typical American city—Hartford, Conn. A sizable minority population is clustered in the central city. Although there are both city and suburban homes priced within the income range of minorities, the incidence of homeownership is lower among blacks and the Spanish speaking than among whites, and the suburbs remain inhabited almost entirely by whites. The central city is declining in population, mainly because of the exodus of white residents to rapidly growing suburbs. In short, the population shifts occurring in Hartford and many of the factors contributing to these changes in choice of residence are characteristic of those found elsewhere. The practices and attitudes of Hartford mortgage lenders also reflect those found in cities throughout the Nation.

The Commission believes that the facts uncovered by this report are sufficiently alarming to alert the community of mortgage lenders—and their regulatory agencies—to the need for a reexamination of the policies and practices under which they operate.

Chapter 2. Population and Housing in Hartford

Hartford, the capital of Connecticut, is a conveniently located commercial center for the State. It is served by Bradley International Airport and three major interstate highways. The insurance industry started in Hartford in the early 19th century, and 39 companies have headquarters there. Like many other metropolitan areas in the country, the city of Hartford is very different from the surrounding towns which make up the rest of the Hartford Standard Metropolitan Statistical Area (SMSA).[3]

Population

During the decade of the 1960's, the population of the Hartford metropolitan area grew substantially, from less than 550,000 to more than 660,000. All of this growth occurred outside of the central city, which declined from more than 162,000 people in 1960 to about 158,000 in 1970.[4]

The racial composition of the central city changed significantly from 1960 to 1970: The black population nearly doubled, from close to 25,000 to a little over 44,000, while the Puerto Rican population almost quadrupled, from about 2,300 to more than 8,500.[5] In 1970, the black and Puerto Rican population combined represented about a third of the inner city population.[6] Over the same 10 years, more than 31,000 whites left the inner city, representing almost 25 percent of the white population.

Although the black population in the suburbs of Hartford increased from nearly 4,000 to 6,400 in the 1960's, blacks still represented barely 1 percent of the suburban population in 1970. Of the more than 9,000 Puerto Ricans residing in the Hartford metropolitan area in 1970, fewer than 700 lived in the suburbs, an increase of just 5 persons over the 1960 figure. (See Table 1, next page.)

The growth of the black and Puerto Rican population in the city of Hartford has not occurred uniformly. Blacks and Puerto Ricans are concentrated largely in the northern section of the city, while the southern and western sections have remained predominantly white.

Housing

Housing in the suburbs of Hartford differs markedly from housing in the central city. It is

[3] An SMSA is a county or group of contiguous counties which contains at least one city of 50,000 or more inhabitants, or "twin cities" with a combined population of at least 500,000. Contiguous counties are included in an SMSA if they meet criteria for socioeconomic integration with the central city. In the New England States, SMSA's consist of towns and cities instead of counties.

[4] Unless specifically noted, population, housing, and income figures are taken from the following Department of Commerce, Bureau of the Census publications: *1970 Census of Housing: Metropolitan Housing Characteristics—Final Report,* no. HC(2)-1 (September 1972). *1970 Census of Housing: Housing Characteristics by Household Composition— Final Report,* no. HC(7)-1 (February 1973). *1970 Census of Housing: Structural Characteristics of the Housing Inventory—Subject Reports,* no. HC(7)-4 (June 1973). *1970 Census of Population and Housing: Census Tracts—Final Report,* no. PHC(1)-87, Hartford, Conn., SMSA (May 1972). *1970 Census of Population: General Social and Economic Characteristics: Final Report,* no. PC(1)-C8, Connecticut (April 1972). *1970 Census of Housing: Metropolitan Housing Characteristics—Final Report,* no. HC(2)-89, Hartford, Conn., SMSA (May 1972). *1970 Census of Population: Puerto Ricans in the United States—Subject Reports,* no. PC(2)-1E (June 1973). *1970 Census of Housing: Detailed Housing Characteristics—Final Report,* no. HC(1)-B1 U.S. Summary (July 1972). *1970 Census of Population: Earnings by Occupation and Education—Final Report,* no. PC(2)-8B (January 1973).

[5] Data on Puerto Ricans are limited in the 1970 census because in some instances this ethnic group is classified together with Cubans and Mexican Americans as persons of "Spanish language" origin. Where possible, data pertaining exclusively to Puerto Ricans have been used.

[6] The 1970 census may have substantially undercounted Spanish speaking persons in Hartford and blacks. Nevertheless, while the undercounting of minorities distorts their actual numbers, the figures at least give indications of trends.

Table 1. Racial and Ethnic Population of Hartford SMSA, 1960–1970

HARTFORD	1970 Number	1970 Percent	1960 Number	1960 Percent	1960–1970 CHANGE Number	1960–1970 CHANGE Percent
SMSA	663,891	100.0[1]	549,249	100.0	114,642	20.9
White	600,805	90.5	516,784	94.1	84,021	16.3
Black	50,518	7.6	28,813	5.2	21,705	75.3
Puerto Rican [2]	9,236	1.4	2,995	0.5	6,241	208.4
CITY	158,017	100.0	162,178	100.0	−4,161	−2.3
White	103,319	65.4	134,720	83.1	−31,401	−23.3
Black	44,091	27.9	24,855	15.3	19,236	77.4
Puerto Rican	8,543	5.4	2,307	1.4	6,236	270.3
SUBURBS [3]	505,874	100.0	387,071	100.0	118,803	30.7
White	496,486	98.1	382,064	98.7	114,422	32.5
Black	6,427	1.3	3,985	1.0	2,469	62.4
Puerto Rican	693	0.1	688	0.2	5	0.7

Source: Department of Commerce, Bureau of the Census, *1970 Census of Population and Housing: Census Tracts,* no. PHC(1)–87 (May 1972), Hartford, Conn. SMSA. pp. 1,14. See also City of Hartford, Conn., Commission on the City Plan, *Analysis of 1970 Census Data* (December 1972) pp. 2–3, table I.

[1] Data for American Indians and Asian minorities are included in each total but are not shown separately. Therefore, combined figures do not equal 100 percent in any category.

[2] Persons of Puerto Rican birth or parentage made up 59 percent of the Spanish speaking population in the Hartford SMSA in 1970 and 72 percent of the Spanish speaking population in the city of Hartford.

[3] Figures for the balance of the Hartford SMSA excluding the city of Hartford.

newer, less likely to be overcrowded, and much more likely to be owned by the occupant. Three of every five suburban housing units have been constructed since 1950, while 80 percent of the housing in the central city was built before 1950. Fewer than 5 percent of the suburban households are overcrowded, compared to more than 10 percent of the city's households.

Of the more than 100,000 owner-occupied units in the Hartford metropolitan area, fewer than 10 percent are in the central city. Eighty-five percent of all black families living in the city of Hartford do not own their own homes; 97 percent of all Puerto Rican families in the city are renters. Of the city's female-headed families, 85 percent do not own their own homes.[7] By contrast, more than 70 percent of the housing in the suburbs is owned by the occupants, including the few blacks and Puerto Ricans who live there.

Earnings are one reason why so few black and Puerto Rican families live in the Hartford suburbs or can be counted among the area's homeowners. Median income for all families in the city as of 1970 was $9,100 a year. But for blacks it was $7,000 and for Spanish speaking families, $5,250. Thirty percent of the minority families in the city of Hartford had incomes below poverty level. By contrast, in the suburbs median income for all families was $13,300 a year. For blacks it was $12,600 and for Spanish speaking families, $12,400.

Economics, however, by no means fully explains the gross underrepresentation of blacks and Puerto Ricans in the suburbs of Hartford or among the area's homeowners. Despite the disparity between the annual income of minority and majority group families, a substantial proportion of Hartford minority families earn enough to enable them to buy housing at market prices. Some 20 percent of the Spanish speaking families in the city and over 30 percent of the black families in the city earn more than $10,000 a year and generally can afford housing costing as much as $25,000. Nearly half of the owner-occupied housing in Hartford's suburbs and fully 75 percent of the owner-occupied units in the city are valued at less than $25,000. (See Table 2.) Nonetheless, few blacks or Spanish speaking families are homeowners.

The more than 18,000 female-headed families, which are almost evenly distributed between the central city and the suburbs, constitute 11 percent of all families in the area. Nineteen percent of these female-headed families are black and 4 percent are Spanish speaking.

In both the city and the suburbs, female-headed families earned substantially less than all families. Within the city of Hartford these families had a mean income of $6,206 compared with $10,011 for all families. Their mean income

[7] Ownership figures are for two or more person female-headed households only.

in the suburbs was $9,562 compared to $14,595 for all families. In addition, the disparity between male and female median earnings in the metropolitan area was equally severe for all races and ethnicities.[8]

Table 2. Owner-Occupied Housing Units by Number and Value, Hartford SMSA, 1970

	Value of Owner-Occupied Units	Number of Units in Area	Percentage of Total Units in Area
Hartford SMSA	less than $10,000	1,006	0.9
	10,000–14,999	4,645	4.4
	15,000–19,999	18,742	17.6
	20,000–24,999	28,380	26.7
	25,000–34,999	32,892	31.0
	35,000 or more	20,580	19.4
	TOTAL *	106,245	100.0
Hartford City	less than $10,000	75	1.2
	10,000–14,999	462	7.6
	15,000–19,999	2,109	34.7
	20,000–24,999	1,973	32.5
	25,000–34,999	1,092	18.0
	35,000 or more	366	6.0
	TOTAL *	6,077	100.0
Hartford Suburbs	less than $10,000	931	0.9
	10,000–14,999	4,183	4.1
	15,000–19,999	16,633	16.6
	20,000–24,999	26,407	26.4
	25,000–34,999	31,800	31.7
	35,000 or more	20,214	20.2
	TOTAL *	100,168	100.0

Source: Department of Commerce, *1970 Census of Population and Housing: Census Tracts,* no. PHC (1)–87 (May 1972), Hartford, Conn., SMSA, table H–1.
* Total may not add to 100 percent due to rounding.

Approximately 5 percent of all male- and female-headed families were living in poverty in 1970 in Hartford. Yet, of the female-headed families alone, 14 percent of the white families, 71 percent of the black families, and nearly 57 percent of the Spanish speaking families were living in poverty. These women are not potential homeowners. Still, a substantial number—about 15 percent—of those women currently renting their homes earn incomes over $10,000 and can afford to purchase inner-city or suburban housing.

Undoubtedly a variety of factors contributes to the gross underrepresentation of minority and female-headed families among Hartford homeowners. What role does mortgage finance play in denying these people homeownership opportunities?

Chapter 3. Minority Rejection in Mortgage Lending

In Hartford, as in other communities, the process by which mortgage loans are made is complex.[9] At each stage opportunities exist for denying mortgage loans to qualified minority families on the basis of nothing more than the personal prejudice of individuals in positions to decide. Few complaints are made by minority families who have been rejected for mortgage loans because there is little objective basis on which they can complain. Usually the rejection is informal, and the minority families rarely know the precise reasons why they are rejected. Indeed, lending institution officials themselves frequently cannot explain these reasons by reference to objective credit factors.

Typically, most American families must successfully run a threestage screening gauntlet before obtaining their first mortgage loan. They are screened initially by a real estate broker, next by a loan officer, and finally by the institution's loan committee. Minority families, however, are much more closely scrutinized than majority families, and each stage is fraught with the possibility of discriminatory rejection. The criteria considered in determining approval or rejection include several factors which are so subjective as to permit decisions on the basis of personal prejudice. Even those criteria which appear to be objective and susceptible to precise measure turn out, on close examination, to be inconsistent and open to differential application.

The Role of Brokers

The real estate broker serves several functions in a real estate transaction. Generally, brokers represent sellers and their principal obligation is to arrange for a sale on the most advantageous terms to their clients. Brokers also have a direct relationship with buyers in that

[8] Data are not available on median family income by race and sex in Hartford. Median earnings of persons by race and sex in the Hartford metropolitan area are: all males, $8,918; all females, $4,225; black males, $6,237; black females, $3,548; Spanish speaking males, $6,131; Spanish speaking females, $3,861. Department of Commerce, Buerau of the Census, *1970 Census of Population: General Social and Economic Characteristics,* no. PC(1) C–8, Connecticut (April 1972), tables 89, 93, and 99.

[9] This report is based on data obtained through interviews of real estate brokers, lenders, home buyers, public interest groups, and Federal and city housing specialists. Interviews were conducted from July 1972 through September 1973. The original written materials are on file and available for review at the U.S. Committee on Civil Rights in Washington, D.C.

buyers usually deal with them when looking for a house.

Studies have documented discriminatory rejection by brokers of minority families who are ready, willing, and able to meet the terms of sale offered by sellers.[10] White brokers have attempted to dissuade minority homeseekers from making an offer on a house they desire; they have gone to great lengths to avoid having to deal at all with minority homeseekers; and they have flatly refused to tender good-faith offers by minority families. These actions—subtle and covert—usually have been consciously discriminatory.

Often, brokers also have a direct relationship with lenders. Through continuing contacts with one or more lenders, they can help arrange for expeditious financing on favorable terms. It behooves brokers to remain in the good graces of lending institutions to assure a friendly reception for those whom they refer for financing.

Although brokers may handle sales everywhere in the Hartford metropolitan area,[11] the minority brokers are located and work primarily in the minority area of the city—Blue Hills and the suburb of Bloomfield. There are many more white firms and they are generally larger, some having branch offices dispersed throughout the city.

The broker's treatment of the home buyer differs somewhat according to the home buyer's race. Both black and white brokers are concerned that the homeseeker is financially able to buy a home. But several acknowledged that they expend more energy ascertaining the purchasing ability of the potential black home buyer, making the assumption that the white family will be creditworthy and the black family unqualified in the eyes of the lender.

A black homeseeker reported that he had contacted a white broker to purchase a house in a white suburb. The broker carefully reviewed his credit report, which reflected current stability but showed a pattern of late payments 3 years previous owing to illness. In apparent response to the report, the broker discouraged the homeseeker from pursuing further his desire to buy in the suburbs and steered him toward a "more suitable" section of town (a minority neighborhood),[12] which the broker felt would be more acceptable to the lender. The black homeseeker subsequently changed brokers, found a suburban house, and obtained a mortgage.

Another crucial variable in the broker-buyer relationship is the race of the broker. Minority brokers serving minority families who are lower middle-income buyers view their role as one of counselor, confidant, and benefactor. They emphasize the importance of developing rapport with homeseekers and offering advice, based on their knowledge of lending institution policies and practices on mortgage qualifications. This advice constitutes a screening of would-be mortgage applicants before the lender is in any way involved.[13] The brokers encourage complete disclosure of social and financial data; then, if they judge the homeseekers "responsible," they make an appointment with a lender, coach the buyers in preparation for the interview, and accompany them to the lender's office.

White brokers, who generally serve more affluent and knowledgeable homeseekers, develop a much different relationship. They may advise the buyer to some degree, but it is the applicants' responsibility to canvas the mortgage market and arrange financing. The most realtors will do is provide buyers with the names of several institutions in the area and give some indication as to the kinds of terms they can expect to be offered.

By contrast, less affluent purchasers, a disproportionate number of whom are minorities, frequently need help in obtaining the necessary financing. This is especially true for first-time purchasers, who tend to be unfamiliar with the complexities of mortgage finance. In seeking this help, they turn to real estate brokers.

If it appears that a minority family is financially able to buy a home, then the broker helps them to obtain a mortgage. A number of the brokers interviewed in Hartford reported that they arrange mortgages for up to 90 percent of their sales. While this practice has been construed as a service to the families, the prequalifying proc-

[10] See Rose Helper, *Racial Policies and Practices of Real Estate Brokers* (Minneapolis: University of Minnesota Press, 1969). Bibliography included.

[11] Commission staff interviewed members of 16 real estate firms from July 1972 through October 1973. Seven of the firms were black owned; one of the persons interviewed was a black woman. This sample is approximately 10 percent of the total number of real estate firms in Hartford and 80 percent of the black owned firms.

[12] The Department of Justice charged seven Hartford real estate companies in May 1974 with promoting resegregation by steering black home buyers into integrated areas and white home buyers away from them. The areas are Blue Hills and the suburb of Bloomfield. All of the firms are white owned and operated.

[13] Although not all were asked, 11 of the Hartford brokers interviewed by Commission staff asserted that mortgage lenders expect them to screen would-be applicants.

ess may be detrimental to homeseekers. The brokers admitted, for example, that they automatically run credit checks on minority families, but not on white families unless special circumstances appear to require it.

If brokers inaccurately assess the financial status of homeseekers, they may use any one of a number of ways to dismiss and discourage them. Homeseekers may be led to believe that they are ineligible when, in fact, they have been victims of deception, discrimination, or both. A case in point is that of a black couple who contacted a white broker in response to an advertisement for a house. The broker asked about the husband's income and employment and then informed them that they did not meet the "income standards of the community." He did not state the asking price of the house or ask how much money the couple had for a downpayment. (They had $5,000.) He simply looked through his listings and told them that he had nothing he "felt was suitable" for them. Only later did the couple think that they might have been discriminated against, but in the process they were prevented from buying the house they wanted.

Families deemed unqualified by a broker for the mortgage they seek are so advised informally and the matter usually ends there. No written record is kept, nor is a lender involved and put in the position of having to reject the applicant. Consequently, acquiring documentation on the extent of discriminatory rejection of minorities by brokers is nearly impossible.

Just as minority home buyers are dependent upon brokers to obtain a mortgage, minority brokers in Hartford have provisional relationships with white lenders. Compared with white firms, minority firms are smaller, with lower sales volume and fewer mortgages to arrange. Thus, they deal with lenders on fewer occasions; and, when they do, they feel they must present only well-qualified families because they do not have the sales volume to use as leverage in favor of marginal applicants.

Black brokers are forced to be more cautious than white brokers in dealing with lenders. If they feel that a lender is discriminating, they are reluctant to make an issue of it for fear of offending the lender. One black broker reported that she applied for a mortgage for herself to a lender with whom she dealt regularly. Her income was $13,000 and she was ready to put $2,000 down on a $20,500 house. Her credit report was favorable. The lender, however, was unusually slow in processing the application and excessively demanding in the documentation required. For example, he stipulated that cash for the closing in addition to the downpayment had to be in the bank prior to approval of the loan. She then applied to another lender and swiftly obtained a mortgage. Although this is not an overt case of discrimination, the broker believes that she was discriminated against because of her race and/or her sex. But she would not press the issue because it might threaten her working relationship with the lender.

Hartford brokers contend that they judge the ability of a potential mortgage applicant on the same basis as the lending institution. They argue that because they arrange mortgages so frequently and are in continuing contact with loan officers, they are thoroughly familiar with the criteria used by the institutions. In fact, it is virtually impossible for brokers to know precisely the policies of lending institutions because lending criteria vary widely among lenders in Hartford and also vary to a large degree among different offices of the same institution.

Lending institutions also differ on whether or not brokers are expected to screen potential applicants. As Table 3 shows, only one of three institutions surveyed by Commission staff has a consistent policy on broker screening. Screening requirements in the other two are determined by individual loan officers. Nonetheless, a number of Hartford brokers act on the assumption that they are expected to conduct screening.

The absence of consistent objective lending criteria, coupled with the brokers' desire to remain in the good graces of lending institutions, tends to make brokers overcautious. They, thus, screen out families whom lenders might well approve. Several brokers conceded that, unless a family fits the traditional characteristics of acceptable mortgage loan applicants, they will discourage the family because they feel that the loan officer will not approve a loan.

In short, if brokers are to err in their evaluation of an applicant's qualifications, they would rather err on the side of conservatism. One lending official reported that, on several occasions when applicants referred by brokers have been rejected, the brokers have felt compelled to apologize for having inadequately screened the applicant. The same official also expressed the view that brokers could be considerably more liberal in their approval.

The process of broker screening also opens up broad possibilities for rejection on discriminatory grounds. Brokers may screen out qualified

Table 3. Lender Policies on Broker Screening of Applicants

Lending Institution	Official Interviewed	Do you expect the brokers to have screened the aplicant?	Location of Office
1 (S&L)	President and vice president	Yes	Main office
	Branch manager	Yes	Nonminority area
2 (S&L)	Vice president	Yes	Main office
	Branch manager	Yes	Minority area
	Branch manager	No	Nonminority area
	Loan officer	No	Main office
3 (Bank)	Vice president	No	Main office
	Branch manager	Yes	Minority area
	Branch manager	No	Minority area

Source: Commission staff interviews.

minority applicants on the basis of their personal bias or their perception, right or wrong, of the lender's discriminatory policies. Rejection at this stage is informal. No specific reason need be given; discrimination is, therefore, difficult to detect.

The Role of Loan Officers

If minority applicants successfully clear the hurdle of broker screening, they still must pass another test before reaching the stage at which their formal application for a mortgage loan is considered and decided upon by the lending institution's loan committee. This is a second screening process, this time by a loan officer. As in the case of broker screening, this stage is informal and based, at least in part, on subjective criteria. The loan officer can reject applicants for any reason, including personal bias, without having to explain why to the applicant.

The basic concern of lenders in determining whether to approve a mortgage loan is security against loss. One consideration is the value of the property on which the mortgage is held. Another is the credit-worthiness of the borrower. For the latter purpose, lenders inquire into such seemingly objective factors as income, occupation, length of employment, age, and credit rating. They also inquire into less tangible factors that clearly call for subjective judgments. For example, one standard text on mortgage credit risks states:

> In judging a borrower's reasons for requesting a loan, the lender should consider the strength of his [her] attachment to the property and his [her] probable future attitudes toward it.[14]

The text goes on to assert:

> A borrower's relationship to his [her] family and friends is a significant element of risk although it is difficult to rate. Evaluators usually consider whether a borrower has an established reputation, a harmonious home life, associates with good reputations, and if he [she] is active in civic affairs or whether he [she] has been dishonest and untruthful in the past, has a troubled family life, and associates of doubtful reputation.[15]

Compounding the problem caused by the subjective nature of the factors considered by the loan officer is the fact that, at this stage of the mortgage application process, decisions are made informally. The same text advises:

> An analysis of the credit risk should include an informal interview between a representative of the lending agency and the borrower and his wife [her husband]. . . . The results [including a verification of employment, bank account, and a check against public records] should enable the lending agency to decide if the borrower should submit a formal application for a loan, or if he [she] should be told that his [her] application would be accepted.[16]

Commission staff investigations in Hartford indicate that lending institutions in that city adhere closely to the above standards and procedures. Savings and loan officers make decisions on the suitability of filing an application on a purely impressionistic basis. In fact, one savings and loan association president reported that only "eligible" persons are allowed to apply for a mortgage. When asked to elaborate concerning what he meant by the term eligible, he said that it was based on his "feeling about the applicant."

A vice president of another Hartford mortgage loan institution told Commission staff that he placed great stock in whether the applicants were "highly motivated" in deciding whether to accept their application. These criteria obviously open up broad possibilities for decisions on the basis of predjudice or other irrational factors. Nonetheless, they are widely used.

The subjective latitude exercised by a loan officer in judging the merits of individual applica-

[14] Department of Housing and Urban Development, *Mortgage Credit Risk Analysis and Servicing of Delinquent Mortgages*, by Anthony D. Grezzo (Washington, D.C.: Government Printing Office, 1972), p. 14.

[15] Ibid. See also Robert H. Pease, ed., *Mortgage Banking* (New York: McGraw-Hill, 1965), p. 216, who states that some lenders visit the applicant's home to determine personal habits that indicate "those important intangibles . . . such as pride of ownership, general housekeeping standard, and reputation within the immediate community."

[16] *Mortgage Credit Risk Anaysis*, p. 9.

tions is reflected in the case of a black couple who were rejected because they had "a lot of debts." The couple's combined income was $18,700, which normally would have qualified them to purchase the $32,000 house of their choice. They had on hand the 20 percent downpayment required. Yet because of a long term debt of $3,000, their application was refused by a white loan officer who argued that the debt was too much for them to handle in addition to the mortgage payments. The same loan officer counsels all minority families to save $15,000 before attempting to purchase a house. The couple subsequently obtained a mortgage at another institution.

Officials at five lending institutions reported that, following informal interviews at which various subjective factors are considered, they are expected to discourage applications from people they consider "ineligible." No reasons need be offered to the rejected applicants, nor is any written record kept to provide a basis for complaint. Applicants are merely informed that they should not make formal application because it will be rejected, revealing another opportunity for discriminatory rejection of minority applicants.

Beyond this, loan officers tend to be overcautious in accepting loan applications and forwarding them to the loan committee. Several loan officials explained that their future careers are determined in part by the default rate on applications they recommend for approval to the loan committee. Thus, they try to avoid accepting applications which they feel might be rejected by the loan committee, since this would reflect adversely on their judgment and might hinder their career advancement.

These policies inevitably result in informal rejection of applicants who might well qualify for a mortgage and never default on it. At one savings and loan institution, two branch managers reported that 80 to 85 percent of the applications they forward to the loan committee are approved. Two branch managers at a savings bank similarly indicated that nearly all of the applications they accept are approved by the loan committee. At both institutions, submission of an application is tantamount to approval. One can only speculate, however, how many applications would have been approved by the loan committee had they not been informally rejected at an earlier stage of the process.

Objective Criteria

Although lending institution officials make substantial use of subjective criteria such as motivation and character in determining an applicant's qualifications for a mortgage loan, they still place heavy reliance on criteria which appear to be objective and susceptible to fairly precise measure. These criteria seemingly would not permit the latitude for decisions based on personal bias.

One such criterion is the income of the applicants in relation to the monthly payments they will be required to pay under the mortgage. The lending institution is legitimately concerned that the applicant's income be sufficient to afford the monthly payments, as to assure against default and possible financial loss to the lender.

The credit-worthiness of the applicant is another legitimate concern of the lending institution. An applicant with an unstable financial past or a history of failing to satisfy debts is a questionable risk and the lender is obliged to be as sure as possible that the applicant, if approved, can be expected to meet the long term substantial payments that the mortgage involves.

Another legitimate concern of the lending institution is the value of the house being mortgaged. It is the lender's obligation to set the amount of the mortgage loan in reasonable proportion to the value of the property, after conducting an appraisal of the property to determine its fair market value, which may differ from the sales price.

Although these three criteria are traditional mortgage credit standards, in Hartford they are applied inconsistently and offer ample opportunities for decisions based on subjective judgments, including personal bias.

Ratio of Monthly Payment to Income: A common formula lenders use is that one week's income should be equal to or greater than the monthly mortgage payment. Hartford lenders, however, use a variety of other formulas as well. (See Table 4, next page.)

Two institutions surveyed by Commission staff have no official policy on the ratio of monthly payment to income and leave the decision on an acceptable ratio to the individual loan officer. Although most loan officers are in a position to judge an acceptable ratio based on experience and training, without official policies or guidelines it is difficult to hold them accountable. At these institutions the apparently objective criterion of the ratio of monthly payment to income can easily be applied subjectively and discriminatorily.

Seven institutions were surveyed that do have official policies on the maximum ratio of monthly payment to income. The two institutions with the most liberal ratios (a bank and a savings and loan association) require that one week's gross income equal the principal, interest, taxes, and insurance (PITI). Three institutions use differing ratios which are based not only on PITI cost but on total housing expenses, including heat, utilities, and maintenance, in relation to gross income. Two other institutions use ratios of net income to housing payments in assessing applicants.

Table 4. Lender Policies on Ratio of Income to Housing Payment

Institution	Official Interview	Policy
(S&L)	President and vice president	PITI [1] = 25% of gross or net income
	Branch manager	PITI = 25% of gross income
(S&L)	Vice president	PITI = 25% of net income
	Branch manager	PITI = 25% of net income
	Branch manager	Housing expenses [2] = 30% of gross income
(Bank)	Vice president	Housing expenses = 35% of net income
	Branch manager	PITI plus fixed debts = 38 to 40% of net income
(S&L)	President	Housing price = twice the gross annual income
(Bank)	Vice president	PITI = 25% of gross or net income
(Bank)	Vice president	Housing expenses = 35% of gross income
(S&L)	Vice president	No policy
(Bank)	Vice president	Housing expenses = 25% of gross income
(Bank)	Vice president	No policy

Source: Commission staff interviews.
[1] PITI is the sum of the Principa and Interest payments on the mortgage, Taxes, and property Insurance costs.
[2] Housing expenses are the sum of PITI, utiities, heat, and maintenance costs.

Thus, there is little consistency among the nine lending institutions on the permissible ratio of monthly payment to monthly income. Moreover, there is also little consistency in this regard among the different offices of the same institution. At one savings and loan association, for example, while the vice president in charge of residential mortgage lending and one branch manager were in accord that the ratio should be 25 percent of net income to equal the PITI cost, another branch manager operated under the formula that 30 percent of gross income should equal total housing expenses.

Even on a day-to-day basis a bank may alter its preferred ratio of housing payment to income, permitting ample opportunity for discrimination. For example, a black couple sought a loan to purchase a condominium in a new development. They went to the lender that had financed a number of the new condominiums and were able to satisfy the institution's standard ratio requirement. The lender turned them down, however, on the grounds that they could not meet a newly imposed higher ratio. Subsequently, they obtained a loan from a different institution and were the first blacks to move into the development.

In addition to inconsistent application of the monthly payment to income ratio among Hartford lenders, there also is inconsistency in the definition of the basic term, income. Generally, income can include salary earned by the primary borrower and secondary borrower, along with commissions, overtime pay, and bonuses. All Hartford lenders agree that the income of the primary borrower should be stable, reliable, and have reasonable prospects for continuation. These same criteria apply to the income of the secondary borrower.[17] The conditions under which overtime pay and income from second jobs are counted, however, are not uniform among the institutions.

Three institutions allow overtime and second job income as effective income, provided that the same criteria as applied to the primary job are met. Two institutions do not necessarily allow such income to be counted even if the criteria are met. Each case is treated individually, and the basic criterion of income becomes less susceptible to objective definition.

The failure of Hartford lenders to accept income from overtime pay and second jobs on a consistent basis necessarily has a discriminatory effect on minority homeseekers, who often rely on these sources of income.[18] The Federal Housing Administration, however, accepts overtime pay as part of income when such pay is characteristic of the job. FHA also accepts in-

[17] Issues relating to the secondary borrower, who is often the wife of the primary borrower, are discussed in Chapter 4.
[18] This argument is supported by guidelines released by the Federal Home Loan Bank Board in December 1973. "Automatically discounting . . . income from bonuses, overtime, or part time employment will cause some applicants to be denied financing . . . Since statistics show that minority group members and low and moderate income families rely more often on such supplemental income, the practice may be racially discriminatory in effect, as well as artificially restrictive of opportunities for home financing." 38 Fed. Reg. 34653 §531.8(c).

come from a second job if the applicant has held it over a substantial period of time and is expected to continue in it during the early period of the mortgage.

Credit Reports: Reports on the credit history of mortgage applicants are necessary information for the lender to have in deciding whether to approve an application. Again, Hartford lenders are not consistent in their use of these reports. Some lenders limit their examination of an applicant's credit history to the previous 2 years, reasoning that this is sufficient to determine the financial responsibility of the applicant. Others, however, extend their examination to the previous 5 or even 7 years. By the same token, while some lenders do not accept at face value adverse reports on a family's credit but look for possible mitigating circumstances or other clarifying information, other lenders assert that any adverse information in the report automatically disqualifies the applicant. No investigation is conducted to determine the circumstances surrounding the adverse report or even to determine whether the adverse information is accurate. The discriminatory effect of this policy of automatic disqualification on minority applicants is apparent, owing to the discriminatory judgments made by credit bureaus in assigning credit ratings.[19]

A 1971 survey of savings and loan associations by the Federal Home Loan Bank Board (FHLBB) revelaed that 57 percent of the associations looked at credit reports for the previous 2 years or less; 34 percent considered the previous 3 to 5 years and 9 percent considered the previous 6 to 7 years.[20] The survey also revealed that 26 percent of the associations sought information on arrest records, and 12 percent automatically disqualified applicants who had ever been arrested, whereas 14 percent disqualified applicants if they had been convicted. Because minority persons are arrested in disproportionate percentages, the disqualification on arrest records alone has a discriminatory effect.[21]

Similarly, 73 percent of the associations require information on previous homeownership, and 23 percent automatically disqualify applicants with "unsatisfactory answer (s)." Because minority persons are overwhelmingly not homeowners in metropolitan areas, this imposes an additional, undue burden on them.[22]

Appraisals: If a mortgage is needed by most families to buy a house, it also is true that the mortage must be large enough. If not, families must either obtain a second mortgage, which can be expensive, or abandon their efforts to purchase the house they desire. The amount of the mortgage a lender will offer to an applicant is based largely on the appraisal, which determines the worth and marketability of the house. One traditional way of discriminating against minority homeseekers is through underappraisal of the houses they wish to purchase.[23]

Commission staff did not attempt to conduct an in-depth investigation of the extent to which discriminatory underappraisal was prevalent in Hartford. Instead, knowledgeable local lenders and borrowers were asked for their expert opinion. As expected, most stated that discriminatory underappraisal was not a common practice, that most homes were appraised at the sales price.

Officials of one lending institution and three brokers, however, reported that appraisal value was lower than the sales price in a substantial number of cases. In their view, this happened most often when the purchaser was a minority group member or when the house was located in an area of minority concentration.[24] Transitional

[19] See S. N. Sesser, "Big Brother Keeps Tabs on Insurance Buyers," *New Republic*, Apr. 27, 1968, pp. 11–12.

[20] Federal Home Loan Bank Board Survey (released March 1972). The FHLBB considered the results of the survey inconclusive, since it included only 74 of the 5,000 federally supervised savings and loan associations.

[21] Figures taken from the Uniform Crime Report published by the Federal Bureau of Investigation in 1973 and interpolated with national population statistics show that the arrest record of blacks was more than three times that of whites in 1972 in proportion to their percentage in the population; Spanish speaking persons are included in the category "white."

[22] Only 34 percent of black families living in central cities and just 14 percent of the Nation's urban Puerto Rican families were homeowners in 1970. Department of Commerce, Bureau of the Census, *1970 Census of Housing: Detailed Housing Characteristics—Final Report*, no. HC(1)–B1, U.S. Summary (July 1972), p. 292. Also, Department of Commerce, Bureau of the Census, *1970 Census of Population: Puerto Ricans in the United States*, no. PC(2)–1E (June 1973), p. 94.

[23] Underappraisal may be discriminatory in effect when it results in a lowered loan amount and a higher downpayment, thus forcing the homeseeker out of the market.

[24] According to the FHLBB survey, only 4 percent of the savings and loans use minority appraisers. Thus, the appraisers are overwhelmingly white and undoubtedly reflect the views of the associations: 30 percent of the associations "disqualify some neighborhoods from lending because they are low income or minority group areas" and 78 percent feel loans in such neighborhoods are "more risky than other loans." Additionally, 11 percent of the associations' appraisers use "different methods or factors" for such neighborhoods. For purchasers in such areas, over a quarter of the associations require higher downpayments; 11 percent levy interest rates 0.5 percent higher, and almost a third give terms 7½ years shorter than loans for homes in other areas.

In May 1972 the Department of Housing and Urban Development (HUD), Office of Equal Opportunity, issued an initial report on a private lending institution's questionnaire. It showed that 18 percent of the associations surveyed refuse to make loans in areas with high minority concentrations.

The new FHLBB guidelines prohibit "redlining," the refusal to lend in a neighborhood solely because of minority concentration. "The racial composition of the neighborhood where the loan is to be made is always an improper underwriting consideration." 38 Fed. Reg. 34653 § 531.8(c).

neighborhoods—those in the process of integrating—very likely fall into this category. They added that often the underappraisal was made without discriminatory intent, but rather on the basis of the traditional appraiser view that property values decline in minority and transitional neighborhoods.[25] They conceded, however, that sometimes the appraisals were the result of nothing more than the personal bias of the appraisers.

Chapter 4. Sex Discrimination in Mortgage Lending

Unequal access to mortgage money for Hartford's minorities occurs largely by virtue of mortgage procedures and criteria which permit and even facilitate decisions based on personal bias and other factors not related to objective lending criteria. Whether because discrimination in mortgage lending is prohibited by both Connecticut and Federal law or for other reasons, lenders in Hartford do not generally admit that they reject applicants on the basis of their race or national origin. In fact, the criteria which govern whether mortgage applicants will be approved or disapproved are, at least on the surface, nondiscriminatory. To the extent discrimination does occur, it is subtle, often unconsciously practiced, and difficult to detect.

Discrimination on the basis of sex is a different matter.[26] Here, the major problem is not that mortgage procedures or criteria permit opportunities for decisions on the basis of discrimination. Rather, traditional mortgage lending criteria followed by Hartford mortgage lenders virtually require sex discrimination.[27] Under these criteria, women are automatically considered suspect risks.

If married and working, women's incomes are discounted for purposes of determining the family's eligibility for a mortgage. No matter how important their income is to the family budget, it is considered "secondary" for mortgage lending purposes, and the family's chances for a mortgage loan are decided largely on the basis of the husband's financial status.

If unmarried, women are viewed with great skepticism under traditional mortgage lending criteria. Regardless of their professional background or work experience, their status as unmarried women renders them suspect credit risks. Female heads of household who are separated or divorced also face unfavorable treatment by lenders. Separated women are in an ambiguious legal status in terms of debt liability, while both separation and divorce bear a traditional social stigma.

This chapter examines the barriers to homeownership only of those women who are economically capable of owning a home. The ability to purchase a house depends directly on household income, and on this point, women who are black, Spanish speaking, or white are at a severe disadvantage compared to men.[28] (See Table 5.) Moreover, the impact of discrimination is felt doubly by black or Spanish speaking women who are penalized because of race and ethnicity as well as sex.

Sex discrimination in mortgage lending is not nearly as difficult to detect as discrimination on the basis of race or national origin. Much of it is based on what lenders consider prudent and objective criteria. In Hartford, as elsewhere, sex discrimination is part and parcel of official bank policy.

This section will detail the various forms that sex discrimination in mortgage lending takes in Hartford. Women of different marital status—married, unmarried, widowed, separated, or divorced—are all viewed somewhat differently by the mortgage lending community. No group of women, however, has equal access to mortgage money.

The Working Wife

Married women are a substantial part of the Nation's labor force. The stereotyped pattern of women giving up their jobs once married to spend full time caring for the house and children clearly is no longer true. As of 1970, in two of every five families with husband and wife both

[25] This traditional appraiser perception is prohibited by the new FHLBB guidelines: "Refusal to lend in a particular area solely because of the age of the homes or the income level in a neighborhood may be discriminatory in effect since minority group persons are more likely to purchase used housing and to live in low-income neighborhoods." 38 Fed. Reg. 34653 § 531.8(c).

[26] Sex discrimination in mortgage lending currently is not prohibited under Federal law. The Federal Home Loan Bank Board, which regulates Federal savings and loan associations, issued guidelines in December 1973 on nondiscriminatory lending practices with respect to age, sex, and marital status (38 Fed. Reg. 34653). The Federal Deposit Insurance Corporation, which supervises most of the Nation's commercial banks, has had under consideration for well over a year, but has not acted on, the issuance of a regulation prohibiting sex discrimination in lending.

[27] In Connecticut, in June 1973, a State law was passed which prohibits discrimination on the basis of sex or marital status in credit transactions including mortgage lending transactions (Conn. Public Act 73–573). Evidence for this chapter was gathered prior to passage of this law; its impact has not been analyzed here.

[28] Median earnings of women in the Hartford SMSA in 1970 were only 47 percent of men's earnings.

Table 5. Women's Earnings as Percentage of Men's Earnings, 1969

	Men *	Women *	Women's Earnings as Percentage of Men's Earnings
White	$8,601	$4,084	47
Black	5,809	3,280	56
Spanish speaking	6,606	3,621	55

Source: Department of Commerce, Bureau of the Census, *1970 Census of Population: Earnings by Occupation and Education—Final Report*, no. PC(2)-8B (January 1973), tables 1, 2, 7, 8.
* Ages 25-64

present, both the wife and the husband worked. Increasingly, the working wife's income is being relied upon as a substantial and continuing part of a family's assets.

Important as a working wife's income is to families generally, it often is essential to minority families. As of 1970, in more than two-thirds of the Nation's black families with husband and wife both present, both worked. Table 6 demonstrates the importance of the wife's income to the economic well-being of black families.[29] Among families in which only the husband worked, black family income was less than two-thirds of that for white families. By contrast, among families in which both husband and wife worked, black family income was nearly 90 percent of the income for whites.

The importance of the working wife's income in achieving the goal of homeownership is shown by data from a sample of mortgage transactions in Hartford, for the years 1971–72.[30] As Table 7 shows, in half of the 72 families in the sample, the wife worked. This was true for 41 percent of the white families and 58 percent of the black families.

These statistics strongly indicate that, to the extent mortgage lenders discount some or all of the working wife's income in determining whether to approve a mortgage loan application, all families necessarily are penalized. For minority families the penalty may be doubly severe because this form of sex discrimination, coupled with discrimination on the basis of race or na-

Table 6. Median Income of Families * With Both Husband and Wife Present, By Work Experience and Race

	1959		1970	
Work Experience	Dollar Amount	Black as Percentage of White	Dollar Amount	Black as Percentage of White
Black, total	3,534	62	8,032	82
Only husband worked	3,025	58	5,965	66
Husband and wife worked	3,845	64	9,267	89
White, total	5,658		9,796	
Only husband worked	5,233		9,065	
Husband and wife worked	6,013		10,396	

Source: Department of Commerce, Bureau of the Census, *The Social and Economic Status of the Black Population in the United States, 1971*, P-23, no. 42 (July 1972) p. 34.
* Heads of households under 35 years of age only.

Table 7. Employment of Wives, by Race

	White		Black		Total	
	No.	Pct.	No.	Pct.	No.	Pct.
Sample	34		38		72	
Total wives employed	14	41	22	58	36	50
Part-time	5	15	4	11	9	12
Full-time	9	26	18	47	27	38

Source: Commission staff interviews with home purchasers, Hartford, Conn., September 1972.

tional origin, effectively places minority women and their families in double jeopardy.

Traditionally, lenders have ignored the working wife's income in assessing a family's financial status. Recently, however, because of their growing recognition of the fact that married women are a substantial part of the labor force and because of pressure from various public interest groups,[31] they have come to count some portion of it. Nonetheless, the policies and practices of mortgage lenders still fall far short of fully accepting the income of working wives.

[29] Work experience and income data on two-earner Spanish speaking families are not available. However, median household income variation among the three groups would suggest that a similar pattern occurs in two-earner Spanish speaking households.

[30] Data gathered through interviews in 1972 with home purchasers. In only one instance was the female the head of the household. She was a nurse whose income was fully considered by the lenders.

[31] For example, a statement in opposition to the Federal National Mortgage Association's proposed guidelines restricting mortgage credit was issued in 1971 by 30 public interest groups including the National Organization for Women, National Association for the Advancement of Colored People, Center for National Policy Review, and Non-profit Housing Center.

Table 8. Lender Policies on Wife's Income

Institution	Official Interviewed	Policy
1 (S&L)	Vice president	100% allowance
2 (S&L)	President and vice president	100% if over 35 and employed 2 or 3 years; if under 35, would take a "hard look"; might require a "baby letter." *
	Branch manager	100% if 29 or older, with no children and in a professional occupation.
	Branch manager	Requires professional occupation; would take a "hard look" at younger than 30.
3 (Bank)	Vice president	100% allowance
	Branch manager	50% allowance unless in a professional occupation, with no children and a "baby letter."
	Branch manager	75% allowance for a professional occupation if under age 30; less allowed for others.
4 (S&L	President	50% allowance
5 (Bank)	Vice president	Depends upon the case
6 (Bank)	Vice president	100% allowance
	Branch manager	Does not count income from nonprofessional occupations.
7 (S&L)	Vice president	Depends upon the case
8 (Bank)	Vice president	Depends upon the case
9 (Bank)	Vice president	100% allowance

Source: Commission staff interviews with banking and savings and loan officials in Hartford, January-February 1973.
* The "baby letter" is a physician's statement attesting to sterility of husband or wife, their use of approved birth control methods, or their willingness to terminate pregnancy.

The 1971 survey by the Federal Home Loan Bank Board on practices of savings and loan associations showed that 25 percent of the respondents would not count any of the income of a wife, age 25, with two school children, who held a full-time secretarial position. More than half of the mortgage lending institutions would limit credit to 50 percent or less of her salary. Only 22 percent would count all of it.

The results of the survey not only show the overly conservative view of mortgage lenders toward a wife's income, but also demonstrate the lack of any uniform policy. This is reflected in Hartford. As Table 8 illustrates, not only are there inconsistencies in policy among the nine Hartford lending institutions surveyed by Commission staff; but, even within the same institution, officers differ markedly in their view of a wife's income.

The refusal to credit the working wife's income is based on the unsupported assumption that to do so would increase the risk of default and subsequent foreclosure. In fact, to date no studies have controlled for this crucial variable. One study found, however, that as the percentage of family income earned by the husband decreased, the chance of a loan's being delinquent actually decreased slightly.[32] Another more recent study, which related borrower characteristics to delinquency and foreclosure rates, found that none of the contributing factors related to the income of the working wife.[33] In short, there is no empirical evidence to support the widely practiced lender policy of discounting the working wife's income.

Policies of Conventional Lenders

Age and Children: A primary consideration in mortgage loan underwriting is the female wage earner's age. This is directly related to the probability of child-bearing. For example, a married woman in her twenties generally would not have more than 50 percent of her income counted, owing to the likelihood that she will bear children and, it is assumed, leave the labor force.[34] By contrast, 75 to 100 percent of the income of a married woman in her late thirties would qualify, according to Hartford lenders.

In addition to the wife's age, the number and ages of children living at home are also considered. Lenders assume that families with

[32] Leon Kendall, *Anatomy of the Residential Mortgage Market* (Washington, D.C.: U.S. Savings and Loan League, 1964).

[33] John Herzog and James Earley, *Home Mortgage Delinquency and Foreclosure* (New York: National Bureau of Economic Research, 1970).

[34] Nationally, 38 percent of all women in the labor force have at least one child under 18 years of age. Forty-three percent of all evermarried women with children under 18 are in the labor force. Department of Labor, Bureau of Labor Statistics, *Marital and Family Characteristics of Workers:* March 1972, (April 1973) p. A-18.

young children will have additional children and discount the working wife's income accordingly. There are, however, exceptions. A married woman, even in her twenties, with no children may have all of her income counted, with certain documentation. This documentation, known in the lending trade as a "baby letter," consists of a physician's statement which attests to her or her husband's sterility, their use of approved birth control methods, or their willingness to terminate pregnancy.

Because of the absence of uniform institutional policy, the requirement of a baby letter depends entirely on the attitudes of individual loan officers. Branch managers in two lending institutions stated to Commission staff that they required the baby letter as a precondition to crediting all the income of a young wife. However, at the central offices of these same institutions opinion differed as to the need for these letters.[35] The lack of consistent policy and resultant confusion is illustrated by the following cases.

A young Hartford couple applied for a 90 percent loan on a $16,000 home. The husband earned approximately $10,000 a year; his wife, $9,500. Their only major long term obligation was a monthly $200 car payment. At first the savings and loan the couple applied to for a mortgage loan was reluctant to approve the mortgage based on the husband's income alone. In order to count the wife's income, the institution asked for a baby letter. The couple refused. Ultimately, the loan was approved, but the couple was never informed what part, if any, of the wife's income was counted.

In another case a married woman was asked by the broker-builder-seller of the property to file a baby letter, which she did. Subsequently, however, the lending institution assured her that no letter was on file. The institution also informed her that her income had not been counted. In this case the broker assumed that the wife's income was necessary and that a baby letter had to be presented. Neither assumption was correct.

Working wives with preschool age children are the least likely of any female subgroup to have their income fully counted towards maximum mortgage allowance. Lenders raise questions and make determinations relying on their own assumptions about the likelihood of more children, the costs of child care, and the length of time spent away from the job after childbirth. A branch manager at one savings and loan told Commission staff that his decisions on crediting a working wife's income are based, in part, on his observation that a woman usually does not return to work until a year after the birth of a child. During that time her income will not be available for mortgage payments. This attitude is common among Hartford lenders. They are reluctant to count more than 50 percent, if that, of a young mother's income, predicting that she will again become pregnant and drop out of the work force for at least a year during the early mortgage period.

The case of one young Hartford couple clearly illustrates the effect this policy has on the ability to purchase a home. The husband, 23 years of age, was a fifth grade teacher who earned an annual salary of $8,574. His wife, 22 years of age, was a secretary earning $5,600. They had two children, a 5 year old and an infant.

The couple first contacted a savings and loan in October 1972 and applied for a $16,150, 8 percent, 30-year mortgage on a house priced at $17,000. The wife was not then employed. Although the application was approved by the Mortgage Guaranty Insurance Corporation (MGIC),[36] it was subsequently rejected by the lender because the husband had cosigned an automobile loan for his brother.[37]

Two months later after the husband had removed his name as cosigner on the auto loan, the couple reapplied to the savings and loan. By this time the wife had assumed a position as a full-time secretary with the University of Hartford. Several weeks later they received a second notice of rejection from the lending institution. This time the reason was that the wife was young, in her childbearing years, and, therefore, likely to become pregnant and drop out of the work force.

This case illustrates the perplexing, sometimes erratic, behavior of mortgage lenders in processing applications from married couples. The fact that the application initially was approved by MGIC, although subsequently rejected by the lender, suggests that the couple was, at

[35] At one lending institution, one vice president would require a baby letter while another would not. In general, executives at the central level in the lending establishments favored full inclusion of the wife's income, unlike more conservative branch managers.

[36] MGIC is one of a number of State-licensed private mortgage insurance companies which insure lending institutions against loss, generally on the top 20 percent of mortgage loans.

[37] The rejection and reason therefore were communicated orally to the applicants by their broker.

worst, a marginal risk for the mortgage they sought, even though the husband was subject to liability as cosigner on an auto loan and the wife was not then working. Two months later, the husband's liability as cosigner had been eliminated and the wife was working. Given these two new sets of conditions, the couple had good reason for optimism and resubmitted their application. Nonetheless, it was rejected. The fact that the wife now held a responsible, full-time position and earned a substantial income apparently counted for little in the lender's judgment.

Occupation: Another consideration which lenders take into account in crediting the working wife's income is the type of job she holds. The income of women categorized as "professional" by lenders is counted more readily than that of women whose jobs are considered "nonprofessional." Although some central office lending officals interviewed by Commission staff insisted that type of occupation is not a determining factor in income allowance, most branch managers interviewed stated that they consistently differentiate according to professional and nonprofessional categories. A woman who is a store clerk or bank teller, for example, would not have as high a percentage of her income counted as a woman who is a business executive, teacher, or nurse. The presumptions are that professional jobs are stable, as are the women who hold them, whereas nonprofessional jobs are short term and unstable.

Type of occupation does not represent an independent factor considered by itself in determining whether and how much to credit the working wife's income. The wife's age and the number and ages of the children also figure in, and the various factors are weighed in an imprecise way that defies objective analysis. One lending institution official said that his rule of thumb in crediting wife's income was that, if the woman is in her child-bearing years, she must hold a professional position, and even then, not more than 50 percent of her income would be credited. He would not under any circumstances, however, count any income of a woman in her childbearing years who held a blue-collar job.

A branch manager of another lending institution stated that he allows 50 percent credit toward the income of a working wife under 35 and 100 percent credit of a working wife over 35, regardless of the type of job she holds, provided that she has been employed for at least 1 year. Another branch manager of the same institution, however, stated that he would never allow 100 percent of the income of a female blue-collar worker. Jobs in that category, he said, are unstable.

The arbitrary character of the application evaluation with regard to wife's income is underscored in the follwing case. A Puerto Rican couple applied for a mortgage with a savings bank. They were both 29, childless, and had been schoolteachers for the previous 5 years, earning a joint income of $20,000 annually. The couple applied for a $16,000 mortgage on a $20,000 home but were told that their income was insufficient. They subsequently obtained a mortgage at a savings and loan where half the wife's income was counted, giving them an adjusted income of $15,500.

This case demonstrates two operational rules of conventional mortgage lending in Hartford. First is the arbitrary nature of lender decisions on counting a working wife's income. At the first institution, rejection on grounds of insufficient income clearly suggests that the income of the wife, who held a well-paying professional job, was totally discounted because, at 29, she was within childbearing age. At the second institution half of the wife's income was counted. Secondly, this case reflects the traditional view of lenders that the income of the working wife, under the best of circumstances, cannot really be relied upon. Even where credit was given to the wife's income, she was treated as half a wage earner rather than as a full wage earner.

Policies of Federal Agencies

Federal Housing Administration (FHA): The FHA's policy on giving credit to the wife's income traditionally differs somewhat from that of conventional lenders. FHA policy is to count either all of the wife's income or none of it. By the mid-1960's, according to FHA records, all of the wife's income was counted in 75 percent of the FHA mortgages made where both husband and wife worked. Today, this figure approaches 90 percent. The significance of these statistics must be qualified by the fact that they apply only to mortgages that were actually made. FHA does not maintain records on unsuccessful mortgage applicants. Thus, there is no way of knowing how many families were unsuccessful in obtaining an FHA mortgage because the wife's income was discounted.

The standard used by FHA in crediting the income of working wives is that "income and motivating interest may normally be expected to continue throughout the early period of mortgage risk." [38] The underwriting manual still addresses somewhat conservatively the risk involved in basing net effective income on two wage earners.

> When the effective income is derived from dual sources of occupational income, as in a case when both husband and wife are expected to be employed during the early period of mortgage risk, risk due to possible reductions in total occupational income frequently will be increased because of the greater probability that one or the other mortgagor may suffer a loss of income. This factor of risk is of particular importance when the dual income is represented by the salaries of young married couples.[39]

On the relationship between the income of the working wife and pregnancy, FHA softens its position.

> The principal element of mortgage risk in allowing the income of working wives as effective income is the possibility of its interruption by maternity leave. Most employers recognize this possibility and provide for maternity leave, with job retention, as an inducement of employment. With strong motives for returning to work any failure to do so after maternity leave would probably be due to causes which would be unpredictable and would represent such a very small percentage of volume that it could be accepted as a calculated risk.[40]

The "strong motive" standard, however, is vague and open to individual interpretation.

FHA policy, although liberal at the national level, is implemented at the local level according to the facts of each case, thereby permitting wide latitude in the exercise of judgment by individual FHA officials. This local autonomy causes some disquiet and misunderstanding within the real estate community. For example, despite the high national percentage of mortgages made in which the income of both husband and wife is counted, two brokers in Hartford believe that FHA will not count the income of a married woman under age 36. The brokers' belief is not groundless because the mortgage table on which many local brokers and lenders rely states, incorrectly, that FHA will not count the income of a wife under 32 years of age.[41]

Veterans Administration (VA): Until very recently, the Veterans Administration treated wives' income more restrictively than the FHA. In February 1973, the *Washington Post* published an article that alleged that a lender required a veteran and his wife, who were applying for a GI loan, to disclose their method of birth control through a physician's statement and to take measures to prohibit conception and/or terminate pregnancy in order to qualify the wife's income.[42] In response to this incident, the Veterans Administration issued a circular to its field stations which attempted to establish guidelines on treatment of wives' income.[43] The circular denied the foregoing allegations:

> . . . it is not now and never has been the policy of the Veterans Administration to request or demand veterans and their spouses to make any such disclosures. . . .

Further on, it qualified this assertion by saying:

> If such a medical statement (supporting evidence that a couple are unable to have children) is voluntarily submitted by the veteran to the lender, it cannot very well be refused upon receipt in VA. However, . . . VA would prefer that any such statements received by builders and lenders be retained by them.

The circular's counsel on the treatment of wives' income was just as ambiguous:

> A proper conclusion that the wife's income may be considered toward the repayment of the loan obligation requires a determination as to whether her employment is a definite characteristic of the family life; i.e., a condition which normally may be expected to continue. Her entire income may be included if it is derived from steady employment and her age, the nature and length of her employment, and the composition of the family indicate it is reasonable to conclude that such income is likely to be reliable in the future. Unless that condition is met, only such portions of the wife's income as is determined to be reasonable may be considered.[44]

On July 18, 1973, however, the Veterans Administration approved a new circular stating that "in consideration of present-day social and economic patterns, the Veterans Administration will hereafter recognize in full both the income and expenses of the veteran and spouse in determining the ability to repay a loan. . . ." [45] All of the VA's regional offices have been instructed that they should no longer discount income on account of sex or marital status in making this determination.

The Federal Home Loan Bank Board (FHLBB): Responding to a 3-year drive by 13 public interest groups, the Federal Home Loan Bank Board issued potentially far-reaching guidelines in December 1973 on nondiscriminatory lending practices. The guidelines caution

[38] Department of Housing and Urban Development, *Mortgage Credit Analysis Handbook for Mortgage Insurance on One to Four-Family Properties* (1972), sec. 1–22. See also Commission on Civil Rights, *Housing, Report for 1961*, vol. 4, ch. 3.

[39] *Mortgage Credit Analysis Handbook,* sec. 2–21.2.

[40] Ibid., sec. 1–22.b.

[41] Mortgage Guides, Inc., *The Mortgage Guide* (Portland, Oreg.: 1962). The table summarizes FHA guidelines in use in 1962.

[42] *Washington Post,* Feb. 24, 1973, p. A–1. See also letter from Carol K. Lewicke to the Federal Trade Commission, Bureau of Consumer Protection, Dec. 20, 1972, available in Commission on Civil Rights files.

[43] Veterans Administration, Department of Veterans Benefits, Information Bulletin no. 26–73–1, Feb. 2, 1973.

[44] Ibid.

[45] Veterans Administration, Department of Veterans Benefits, Circular no. 26–73–24, July 18, 1973.

against practices that may result in discrimination even without actual intent to discriminate. They state that "each loan applicant's credit worthiness should be evaluated on an individual basis without reference to presumed characteristics of a group." [46]

The guidelines describe those underwriting decisions as discriminatory which distinguish credit-worthiness on the basis of age, sex, and/or marital status. The discounting of a working wife's income may result in discrimination against race as well as sex, they argue, because of the greater reliance of the minority family on the wife's income for housing and other necessities.

The Single Woman

The women with the greatest difficulty in gaining access to mortgage finance are single women—unmarried, widowed, separated, or divorced women. Each is treated somewhat differently by mortgage lending institutions, but for all it is their status as women who are not part of a male-headed household that is of greatest significance to mortgage lenders.

Bias against the single individual is evident in the FHA's underwriting manual:

> The mortgagor who is married and has a family generally evidences more stability than a mortgagor who is single because, among other things, he [she] has responsibilities holding him [her[to his [her] obligations.[47]

Thus, unmarried persons—men or women—are at a disadvantage in seeking to obtain a mortgage. This disadvantage, however, is not shared equally by men and women.

A widely held view in the mortgage lending community is that single women must present a stronger paper position than single men. Their credit and income must be more secure than those of men of the same status, and their credit histories must be more closely scrutinized. As a result, the filtering process is applied more rigidly at each stage of the mortgage application procedure, from broker to branch manager to formal application. The myth generating this stringency holds that the female is inherently unstable and incapable of conducting her own affairs. She allegedly needs the protection of a male, usually a husband or father. In the lending industry the myth translates into a reluctance to grant a woman a mortgage loan outright and often, a requirement of an assumption [48] or a male cosigner.

A peculiar consequence of the theory that women need protection is the lenders' disinclination to grant a loan to a woman who wants to purchase a multifamily dwelling, reasoning that she would be unable to perform the necessary maintenance. Normally, "a man would do the repairs himself whereas a woman has to hire someone," one lending official argued. According to this official, VA policy is even stricter than his own. He cited the case of a widow who worked part-time and received social security. She wanted to buy a multifamily property. He approved the loan, but VA rejected the application on the ground of insufficient income. Based on his previous experience with VA, the lender felt that this excuse was used to camouflage the true reason for rejection, which was the repair issue.

The Unmarried Woman: In the case of an unmarried younger woman, the principal reason cited for denying mortgages is the likelihood of marriage and pregnancy, and consequent shift in economic status, which serve as risk factors. One broker told Commission staff that in his experience, of all categories of single women, the young unmarried woman has the most trouble securing a mortgage.

Another broker said that the only way an unmarried woman can get a mortgage is through an assumption. He tried unsuccessfully to secure financing on a home for a professional woman who had worked for 23 years. Such failures not only disappoint the individual; they also influence the real estate community to discourage similar clients. Assumptions, however, are considered a safety device; should the woman default, the institution can hold the principal mortgagor liable.

Policies vary both among and within institutions with regard to unmarried women. Officials of lending institutions at the central level generally stress length of employment; branch managers and brokers emphasize age of applicant and type of job. One branch manager went so far as to assert that an unmarried woman could obtain a loan only if she had a professional career. The marginal case, according to a loan officer, would be that of the older, unmarried woman in a nonprofessional occupation, such as a waitress or store clerk, and with only

[46] 38 Fed. Reg. 34653 § 531.8(b).
[47] *Mortgage Credit Analysis Handbook*, sec. 2–7a.

[48] In an assumption, ultimate responsibility rests with the original mortgagor. The second mortgagor takes on, or assumes, payments of the original loan.

a modest downpayment. Even if she has a reasonably long record of employment, it is unlikely that she would be approved for a home mortgage, he said, because her employment is considered unstable.

The Widow: The widow applying for a home loan generally has a better chance of obtaining it than other single women. She more often can rely on life insurance proceeds, social security payments, or settlement on an estate to provide a healthy downpayment and assure a regular income. One lending official said that although widows represent a variety of ages and economic circumstances, if they have a sufficient downpayment and a guarantee of regular income, their prospects for homeownership often are relatively bright.

The Separated Woman: In Hartford, the separated woman, particularly if informally separated, is in an awkward position in trying to purchase a home. Under Connecticut law, a husband is liable for his "wife's reasonable support while abandoned [by him]." [49] The husband's liability extends even to cases where the wife has an independent income.

One of the primary concerns of lenders in making a mortgage loan is assurance of unambiguous liability. For this reason, the informally separated woman falls into a high risk category. If she were approved for a mortgage loan and then defaulted on payments, lenders could not be certain that the husband would be required to make the payments, even assuming he were financially able to do so. The reason for uncertainty is that the husband's liability exists only if the separation results from his abandoning the wife, not from her abandoning him. Thus, under an informal separation arrangement, the lender could not be entirely sure that the husband was liable.

Under formal separation, the legal rights and liabilities are much clearer. In Connecticut, legal separation carries all the conditions of a divorce except that the parties are not yet free to marry again. Neither party is liable for the debts incurred by the other, and a wife's right to alimony, support of children, and financial allowances are specified by the court. For this reason, one mortgage company requires proof of legal separation as a condition to considering separated women for a mortgage loan.

Other mortgage lenders simply will not deal with separated women at all, whether the separation is formal or informal. The vice president of one savings and loan association flatly stated that, because of ambiguous liability, separated women are not eligible for mortgage loans from his institution.

Despite the fact that FHA policy generally weighs heavily against separated women, in a recent case in Hartford, the local FHA office did approve a separated woman for a loan under the section 235 program.[50] Initially, her application was not processed because she was only separated, not divorced, from her husband. FHA counsel, however, reversed the decision because in his view there was no question of ambiguous liability, arguing that State law permits a wife to own property with clear title in her name even when informally separated from her husband.

Aside from the problems associated with their legal status, another reason why separated women have difficulty obtaining mortgages is that their status allegedly reflects domestic strife. For example, the Federal Housing Administration, traditionally skeptical of discordant marital relationships, states in its underwriting manual:

> It has been demonstrated that inharmonious domestic relationships are an important cause of foreclosure. The determination as to this risk will be dependent upon recognition of items in the credit report and personal history of the mortgagor which give evidence of family discord, pending divorce suits, reconciliation after initiation of divorce suits, and other items which point to unstable family conditions.[51]

This policy underscores the stigma imposed on domestic strife and is especially unfair to women who continue a long and stable informal separation. It is contradicted by a recent study that found no statistically significant relationship between marital status and loan delinquency or foreclosure.[52]

The Divorced Woman: The divorced woman also has considerable difficulty in obtaining a mortgage, both because of the alleged probability of an unstable economic situation and because of her social position. Her financial circumstances are often complex: she may rely on alimony, child support, or an independent income alone, or any combination of these sources.

The divorced woman who has a substantial work history and a separate source of income

[49] 22 Conn. Gen. Stat. Ann. Ch. 809, Sec. 46–10 (1949).

[50] Title I, Section 235, of the Housing and Urban Development Act of 1968 provides subsidies in the form of interest reduction payments to mortgage lenders on behalf of lower income families to enable them to purchase their own homes.

[51] *Mortgage Credit Analysis Handbook*, sec. 2–7.

[52] John P. Herzog and James S. Earley, *Home Mortgage Delinquency and Foreclosure* (New York: National Bureau of Economic Research, 1970).

will be treated as any other single woman. Differential treatment occurs when alimony or child support payments are listed as contributing and fundamental sources of income.

Lenders generally will not rely on support payments which are not court ordered even if there is a long history of reliable payments.[53] One lender stated, however, that the pattern of payments would determine their inclusion in total income. The divorcee whose support is court ordered, and her sole source of income, has a fair chance of negotiating a loan if she can make a reasonable downpayment or obtain private mortgage insurance, and if her total support can sustain the monthly payments.

Credit ratings are a significant factor in mortgage applications, and a divorced woman finds establishing credit particularly difficult if she does not have her own credit rating already. A divorcee shares the taint of any adverse information in her former husband's rating, even if she paid their bills promptly. Thus, any negligence on his part would impair her effort to secure independent credit.

Even when income and credit ratings are sound, divorced women still may be turned down arbitrarily for mortgages as in the following case. A 51-year-old divorcee with no dependents, working as a supervisor at an insurance company in Hartford, sought to purchase a three-bedroom, two-bath house in November 1971. The asking price was $21,500; the sale price was $20,000. At the time, her annual income was $8,600, and she had worked at the insurance company for 15 years. Her credit standing was excellent and she maintained two department store charge accounts. She was willing to put $5,000 down, thus applying for a $15,000 mortgage.

She tried to apply for a mortgage at the main offices of four lending institutions. At one savings and loan she was told not to fill out an application because she was "not qualified" and the loan committee would not approve it. No explanation was offered as to why she was not qualified. At two others she was told that she did not "fit their formula," i.e., 30 percent of income for housing expenses. Having been turned down by three institutions, she went to a fourth, a savings and loan, and obtained a 25-year, 7½ percent mortgage.

[53] This criterion has no basis in fact because support, whether or not court ordered, is infrequently paid. For instance, the Citizens Advisory Council on the Status of Women has reported that in Wisconsin in 1972 only 13 percent of ex-spouses were in full compliance 10 years after the settlement; 70 percent had discontinued support altogether.

Chapter 5. Employment in Hartford Lending Institutions

The policies and practices of Hartford lending institutions discussed earlier operate with a discriminatory effect on minorities and women seeking mortgage loans. Many of these policies and practices are not overtly or consciously discriminatory but are viewed by the lending community as necessary elements of prudent banking. In fact, they can be traced to longstanding bank tradition and are based on certain assumptions concerning the subordinate role of racial minorities and women in society.

Banking traditionally has been a profession dominated by white males. Those in positions to make bank policy have been white males, and the policies they have established have been geared to facilitate credit for white males. Racial minorities and women rarely have been in positions to change or even influence these policies.

Title VII of the Civil Rights Act of 1964 [54] prohibits discrimination in employment, and all lenders in Hartford are covered by this statutory prohibition. The Commission examined the employment records of five Hartford mortgage lending institutions to determine minority and female representation generally and their representation in decisionmaking positions. (See Tables 9 and 10.) [55] The basic findings of this examination are:

- Women are abundantly represented as employees of these institutions but almost entirely in low-level positions which carry no authority to influence the policies of the institutions.
- Applying the discriminatory occupational criteria that these lenders use in weighing a woman's mortgage application, these women would not qualify for a loan from the very institutions that employ them.
- Minorities—men and women—are grossly underrepresented in any positions with these lending institutions but especially in decisionmaking positions.[56]

[54] 42 U.S.C. 2000 e–2.

[55] Data for one institution cover only the main branch for 1971 because there were no comparable data for 1969. The inclusion of this institution does not distort the interpretation because it shows the same patterns as the other institutions. For convenience, the 1971 data are treated as though they were for 1969.

[56] The May 1972 HUD Private Lending Institutions Questionnaire showed that 10 percent of the employees in 50 cities were minority employees, with 4 percent of the decisionmaking positions being filled by minorities and 12 percent of the cashiers and tellers being minority members.

• Of equal importance, the situation has not appreciably improved over the 3-year period between 1969 and 1972.

During this period the number of women employed at these institutions increased by 198, all in office, clerical, and service jobs. The number of female officials, managers, and professionals declined by one, although the total number of such positions increased by 29. The number of minority women working as officials, managers, and professionals increased from one to five. The number of minority men in such positions declined, from five to four.

The number of office, clerical, and service employees increased by more than 260 positions from 1969 to 1972, but the great majority of new employees (75 percent) were white women. The institutions employed an additional 64 white men in this category but added only 3 minority females and 8 minority males.

In 1969, women constituted 58.4 percent of the employees and by 1972 this figure had increased to 59.7 percent.[57] But, whereas in 1969, 6 percent of the female employees were officials, managers, or professionals, by 1972 this figure had declined to less than 5 percent.[58]

The comparative statistics between 1969 and 1972 of minority and female employment by Hartford lenders do not suggest that substantial progress is being made. Until minorities and women are more adequately represented in positions to determine or influence lending policy, it is unlikely that the policies and practices that serve to discriminate against these two groups of homeseekers will be changed.

Table 9. Officials, Managers, and Professionals, by Race and Sex, Five Hartford Mortgage Lenders

	1969	1972	1969–72 Change
Total number	353	382	29
Women	56	55	−1
Minority women	1	5	4
Black	1	3	2
Spanish speaking	0	1	1
Asian American	0	1	1
Men	297	327	30
Minority men	5	4	−1
Black	5	4	−1
Spanish speaking	0	0	0
Asian American	0	0	0

Source: Commission staff review of employment records of five Hartford mortgage institutions, April 1973.

[57] The percentage of female employees who were minority women remained constant at 2 percent both years.

[58] Minority women increased their percentage in this group from just under 2 percent in 1969 to 9 percent in 1972.

Table 10. Office, Clerical, and Service Workers, by Race and Sex, Five Hartford Mortgage Lenders

	1969	1972	1969–72 Change
Total number	1,250	1,513	263
Women	878	1,077	199
Minority women	19	22	3
Black	17	18	1
Spanish speaking	2	3	1
Asian American	0	1	1
Men	372	436	64
Minority men	51	59	8
Black	44	44	0
Spanish speaking	5	11	6
Asian American	2	4	2

Source: Commission staff review of employment records of five Hartford mortgage institutions, April 1973.

Chapter 6. Summary and Conclusion

This report has examined mortgage lending policies and practices in Hartford, Conn., that bear on homeownership opportunities for minorities and women. The Commission's purpose has not been to uncover individual instances of discrimination but to answer this question: If left to operate in accordance with traditional banking processes and standards, will the system of mortgage finance in the city assure fair treatment for minorities and women? The basic finding of this report is that it will not. For minorities and women, the mortgage finance system is a stacked deck—stacked sometimes inadvertently, often unthinkingly, but stacked nonetheless.

As the Commission and other agencies and organizations have documented, mortgage lending traditionally has been a closed community, operated largely by white male decisionmakers, and its standards have been geared to facilitate service to white male customers. Minorities and women have had great difficulty in joining this community, either as decisionmakers or customers.

The principal problem for minorities in the past was overt discrimination. Regardless of their personal or financial worth, minorities, simply because of race or national origin, were considered less desirable risks than whites. Moreover, it was deemed virtually unthinkable to provide them mortgages for houses in nonminority areas. In the past, these discriminatory policies were openly admitted by representatives of the mortgage lending community and stoutly defended as essential elements of prudent banking, even by agencies of the Federal Government charged with responsibility for supervising and regulating mortgage lenders.

Since the enactment of Title VIII of the Civil Rights Act of 1968, mortgage lending discrimination on the basis of race or ethnic origin has been unlawful. Public pronouncements advocating such discrimination are now rarely heard. It is unlikely, however, that the traditional banking attitudes and perceptions about minorities, which developed and hardened over decades, have changed substantially in the 6 short years since Title VIII was enacted. The fact that mortgage lenders no longer openly avow discriminatory practices does not mean they no longer engage in such practices. Rather, it suggests that they have gone underground.

In examining the mortgage lending system as it relates to minorities, the Commission's principal concern was to determine the extent to which safeguards were provided to assure against decisions based on racial or ethnic discrimination rather than on objective credit criteria. It also sought to determine whether the system afforded sufficient opportunity for minorities subjected to discrimination to have their grievances redressed. The Commission found that the mortgage finance system in Hartford not only lacks sufficient safeguards to assure against discriminatory decisions but facilitates discriminatory rejection of minorities. The Commission also found that the system affords little opportunity for such decisions to be reversed.

The process of obtaining a mortgage is arduous for everyone. But running the three-stage gauntlet required to obtain a loan is even more difficult for minorities. Before reaching the final stage of *formal submission* of a mortgage loan application to the loan committee, minorities must first clear two formidable obstacles: the real estate broker and the loan officer. Each of these first two stages carries broad opportunities for discriminatory or other irrational rejection.

Brokers may reject minority applicants on the basis of their own bias. Further, because brokers seek to stay in the good graces of lending institutions, they prefer not to refer questionable applicants who may not qualify or, if approved, may default on the mortgage payment. Thus, brokers may reject minority applicants because they think, rightly or wrongly, that the lending institution frowns on minority applications, or because they misunderstand the criteria used by the lending institution. Moreover, this stage of the transaction is entirely informal. Rejected minority applicants usually are merely told that they do not qualify for a mortgage loan and the matter ends there.

Even if minority applicants clear the hurdle of the broker, they are still one difficult step away from a formal application. The second hurdle is the loan officer, who also handles the transaction on an informal basis. The loan officer's decision to recommend or discourage submission of a final mortgage loan application is based upon a number of factors, including some that are highly subjective, such as motivation, character, and the quality of the applicant's domestic life. Furthermore, loan officers, whose opportunities for career advancement depend in part on the default rate on applications they refer for approval to the loan committee, prefer to err on the side of extreme caution. Indeed, they are reluctant to accept applications which they feel may be rejected by the loan committee, since this reflects adversely on their judgment.

Even criteria that appear objective on the surface often turn out on closer examination to have subjective factors that discriminate against minorities. Criteria such as the maximum permissible ratio of monthly payment to monthly income, the definition of income, credit standards, and appraisals are applied inconsistently by Hartford lenders and have the effect of screening out qualified minority applicants.

Thus, the system of mortgage finance, represented by the screening process and the subjectivity of many of the criteria on which qualifications are measured, affords ample opportunity for discriminatory rejection of minorities. Even though discrimination in mortgage lending may have gone largely underground since enactment of Title VIII, the Commission's assessment of the policies and practices of Hartford lenders offers little assurance that such discrimination has ceased to exist.

While discrimination against minorities by Hartford lenders is subtle, discrimination against women is blatant. Minority women suffer the double effect of both sex and race discrimination.

Women as a class, unlike minorities, are unprotected against discrimination in mortgage lending under Federal law. Connecticut and a number of other States now prohibit sex discrimination in credit transactions, but women, by their very status as women, nevertheless are openly considered questionable risks by mortgage lenders. Their treatment varies, depending upon whether they are married, unmarried, widowed, separated, or divorced, but none receives treatment equal to that received by men.

The income of married women, a substantial percentage of whom are gainfully employed, is considered "secondary" and rarely credited more than 50 percent, if at all, in determining a family's financial status. This policy works considerable hardship on all families for whom the wife's income is essential. However, it compounds the problems of minority families, a substantial percentage of whom rely on the wife's earnings to meet their needs. The policy of discounting some or all of a working wife's income has a doubly discriminating effect on these families, as they are thus penalized because of both race and sex.

The policies of mortgage lending institutions on the discounting of a working wife's income vary widely from institution to institution and frequently within the same institution. Some general standards do exist, however. The most favored working wife is beyond childbearing years, holds a job considered "professional," and demonstrates a consistent pattern of continued employment. She has a good chance of having all or most of her income credited by the mortgage lending institution.

The least favored working wife is the young woman of childbearing years, who may have young children, and who holds a job considered "nonprofessional." This class of working wives is viewed skeptically by the mortgage lending community as "unstable." Certain assumptions are made about her regardless of her real situation. One is that, if she has no children, she is likely to and will leave her job, at least for a time, thereby reducing the family income. Another is that if she already has young children, she is even more likely to have additional children. Again, she allegedly will leave her job, at least for a time. The third assumption is that her "nonprofessional" job is unstable and that somehow makes her unstable. These assumptions add up to a composite picture of a person in whom lending institutions place little reliance. Therefore, her income is automatically discounted, either substantially or entirely. Moreover, whether the family is approved or disapproved, they frequently never learn if, or to what extent, the wife's income was credited.

The single woman has great difficulty in gaining access to mortgage finance. The fact that she is without the protection of a male makes her suspect to the lending community as a credit risk. The image of women as "weaker vessels" also makes lending institutions reluctant to approve mortgage loans, particularly on multifamily dwellings, on grounds that women are unable to perform the necessary maintenance.

The young, unmarried woman has the most trouble securing a mortgage, principally because of the assumption made by lenders that she will marry, have children, and stop working, thereby reducing her economic status.

The widow generally is in a more advantageous position, since she often can rely on life insurance proceeds, social security payments, or the proceeds of her husband's estate to provide a healthy downpayment and assure a steady income.

The separated woman is in an awkward position in seeking to obtain access to mortgage finance. One reason for this is her uncertain legal status for debt liability, particularly if the separation is informal. Another reason is that her status is assumed to reflect domestic strife, an added suspect factor, according to lenders.

The divorced woman also has considerable difficulty obtaining a mortgage, both because of the alleged probability of an unstable economic situation and because of the social stigma attached to divorce. If her support is court ordered, her chances for obtaining a mortgage are enhanced. If not court ordered, they are diminished. Furthermore, unless she has established independent credit, any adverse information in her former husband's credit rating reflects on her and further diminishes her chances to obtain a mortgage.

The Commission also inquired into employment of minorities and women by Hartford mortgage lenders, particularly in decision-making positions. It found that, although women constitute a majority of the employees at the institutions surveyed, few occupy positions in which they can determine or influence lender policy; the vast majority, in fact, are in clerical and service occupations. Blacks and Puerto Ricans—both male and female—are scarce in every level of mortgage finance institutions.

The system of mortgage finance in Hartford, under which minorities and women are inequitably treated, reflects a reluctance by the lending community to alter traditional policies and standards, even though many are unrealistic and others facilitate illegal acts. Discrimination on the basis of race or ethnic origin is prohibited under Federal and State law, but the mortgage lending community adheres to a system under which such discrimination persists, unabated and undetected. Sex discrimination in mortgage finance, although not yet prohibited by Federal law, is prohibited by laws recently passed in several States, including Connecticut, and is totally at odds with the reality of modern-day America in which women are an increasing and substantial part of the labor force. Yet mortgage lending institutions cling to images of women as unstable, unreliable, and in need of male protection.

Reform is clearly needed. One alternative is for mortgage lending institutions, themselves, to reexamine their policies and institute the changes necessary to assure that minorities and women are treated equitably. The Commission, however, recognizes the severe limitations of relying on voluntary reform. The agencies that supervise and regulate most of the mortgage lending institutions in Hartford and throughout the country should, therefore, require that the needed reforms be instituted.

On several occasions in recent years, the Commission, other Federal agencies, and private groups have sought to point the direction for such reforms. These recommendations are still valid. Lending institutions should be required to maintain records of the race or ethnic background and sex of mortgage applicants and persons who make oral inquiries about home loans.[59] Such data is urgently needed as a basis for uncovering and correcting patterns of discrimination. Otherwise, the burden of redress rests entirely on the complaint process, a most inadequate means of remedying discrimination. The regulatory agencies, especially the Federal Deposit Insurance Corporation and the Federal Home Loan Bank Board, which have considered such a requirement, should move with speed to require member institutions to initiate an effective data collection system.

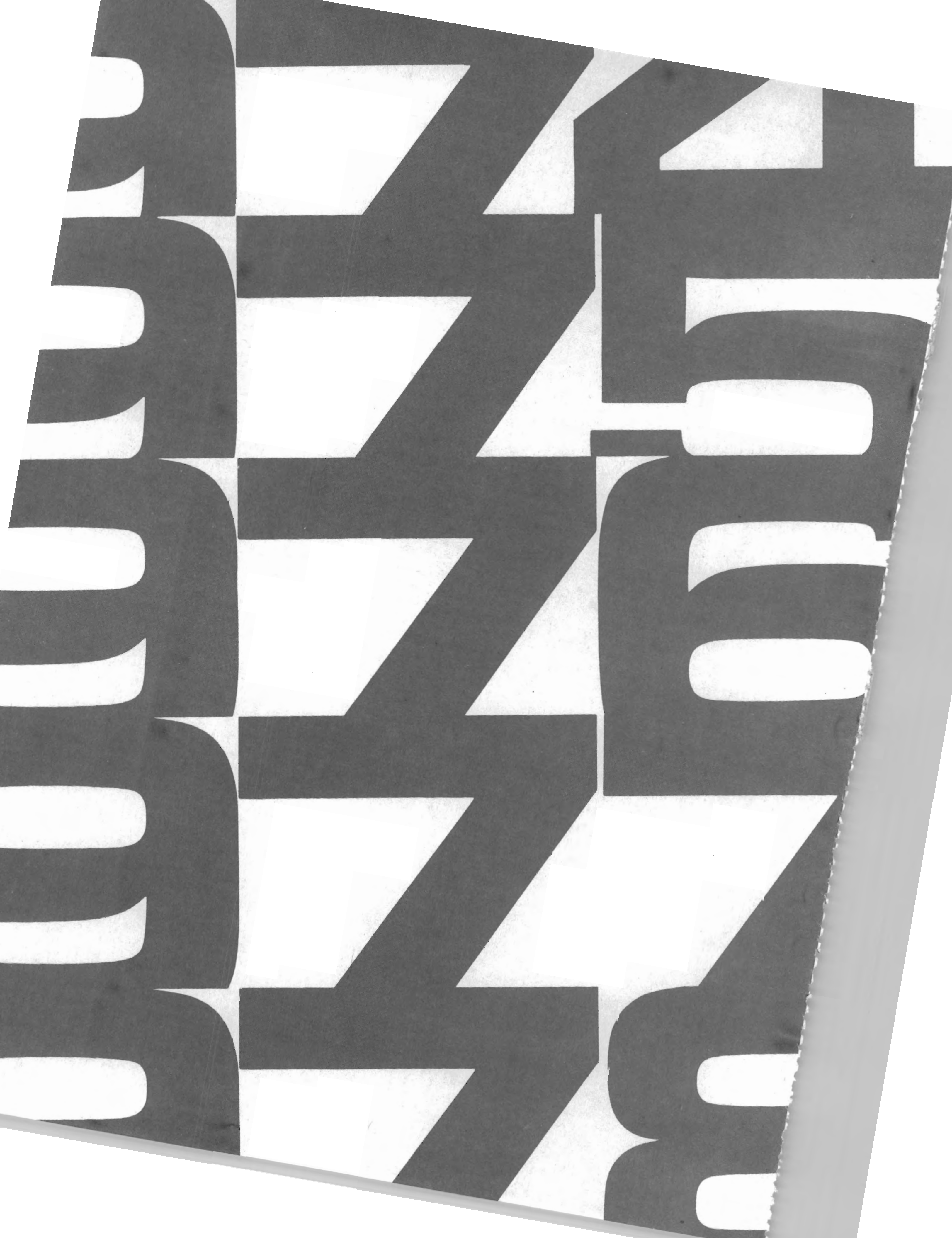
Another way to generate reform is to require lenders to provide homeseekers with written statements of the criteria used in determining their eligibility for a mortgage. Lenders also should be required to notify in writing rejected applicants and persons advised against making application, informing them of the reasons for their rejection. These steps would discourage loan officers from arbitrarily dissuading or rejecting applicants, as such actions would be matters of public record.

Examiners from the financial regulatory agencies should be charged with the responsibility of detecting discrimination by lenders. To this end audits and examinations of lender practices must be expanded. In particular, the Federal Home Loan Bank Board should establish a monitoring system to assure that its newly established guidelines are being followed.

Title VIII of the Civil Rights Act of 1968 (the Federal Fair Housing Law) must be amended to prohibit discrimination based on sex. Single women and working wives could then more easily fight sex discrimination in the courts.

Unless these measures are instituted, equal housing opportunity will remain for most minorities and women a slogan without substance.

[59] The Federal Reserve System, the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the Federal Home Loan Bank Board recently have implemented an experimental program to collect racial and ethnic data over a 6-month period in 18 cities during 1974. The objective is to develop a recordkeeping requirement for racial data on the disposition of mortgage loan applications. The information required under the experiment includes the applicant's age, sex, marital status, and financial situation.



4 Rural Housing

Alternative Low Income Housing Delivery Systems for Rural America

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Summary

Most rural areas are without an adequate low income housing delivery system, mainly because the necessary institutions—including developers, builders, and public agencies—are in short supply. To create all these institutions in rural areas would be a monumental task. However, there is a faster, more effective way to develop a low income housing delivery capability in rural areas through the creation of a public housing delivery system. Public institutions have proved themselves in the forefront of meeting the housing needs of poor people, and the greatest housing need in rural areas is surely that of the poor.

There are few public institutions in rural areas that do or can provide low income housing. Presently, the most active of the alternatives is the rural housing authority, particularly those on the regional or State levels. To some extent, however, other regional agencies are becoming more involved with housing and may offer workable approaches to developing a rural low income housing delivery system. These authorities and agencies can overcome at least some of the institutional gaps existing in rural America and therefore have the capability of combating the problems of small and dispersed populations that plague nonmetropolitan areas. These institutions provide a substantial base on which to build an effective rural delivery system.

Rural Housing Authorities

Most housing authorities in rural areas are small, and the literature on small authorities points to their inefficiencies and the burden they place on Federal housing staff. A poll of all Department of Housing and Urban Development area offices confirmed the problems of small authorities. In an effort to overcome these difficulties and lessen the burden on Federal housing staff, HUD has published over the past decade three management circulars critical of small authorities and praising various efforts at consolidation, including cooperative management agreements and multitown or multicounty arrangements. (HUD has never mentioned State authorities.) The regional or multicounty authorities were considered the most efficient because they require only one annual contributions contract and one board of commissioners. Additional benefits resulting from the regional structure are their greater financial flexibility and their ability to cover a multitude of small towns and unincorporated areas which otherwise could not support housing programs.

Because there are few studies on how these consolidated housing efforts actually operate, the Housing Assistance Council conducted a study of seven rural authorities representing various forms of consolidation. The results were encouraging in terms of the quality of the low income housing programs found in these rural areas, and the potential these authorities exhibited for expanding their responsibilities in housing and the provision of related services. All the authorities, regardless of type, are well respected public institutions in the areas they serve. They provide housing and other services of a decent and often superior quality to families and the elderly living in extremely small towns. Though their costs are comparable to smaller authorities, the service they provide their tenants, according to HUD personnel, is far better. Additionally, these authorities may achieve cost savings in the long run.

Generally, the regional or State housing structures offered the most simplified (only one set of financial records is required, for example) and, yet, the most extensive housing programs of the authorities studied. One of the regional authorities has created its own nonprofit housing developer and has used its bonding authority to support the development of a range of low and moderate income housing. Another authority has placed as few as one to six units in small rural towns throughout an entire State, and has stimulated the rehabilitation of substantial numbers of large older houses. Another provided the Nation with its first demonstration of the Turnkey III homeownership program.

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Although regional and State structures can often best serve rural areas, the size of the regions or the number of units to be managed by one authority depends on the peculiarities of local conditions. The proximity of housing locations or the accessibility of locations to each other may determine whether certain areas should combine their housing efforts. Size of population is also important. In a primarily rural State, where each county's population is small, regional authorities may be less advisable than a single State authority (this analysis extends to other types of housing delivery systems as well). There are no hard and fast rules to determine optimum size of a rural housing program, since local conditions must always be considered.

Other Rural Agencies With Housing Delivery Potential

Economic development districts and other types of regional planning agencies are gradually becoming interested in low income housing development. These organizations have a presence in rural areas, and their comprehensive planning function gives them an attractive advantage over single purpose agencies, such as regional housing authorities. At this time, however, these agencies are generally limited to planning functions and, in many States, legislation prohibits planning and development district organizations from program implementation. In some areas there is a movement toward providing them with the powers to implement certain programs, and nearly a score of such agencies have already become involved in housing development.

In addition to the various types of regional agencies, the State housing agencies created in recent years are also potentially effective rural housing delivery mechanisms. Approximately 31 States have created housing agencies with finance or development powers, or both, and some of these were created specifically to work in rural areas. Most State housing agencies now rely on nonprofit and limited dividend developers to carry out the objectives of the State program. The tendency is therefore towards shallow subsidy programs and higher income consumers. Because of the shortage of such developers in rural areas, the tendency is also towards development in the cities and suburbs. When more State agencies become involved in the direct development of housing, including development under the low rent public housing program, their potential for serving rural housing needs will be better realized.

Conclusions and Recommendations

1. For several reasons, public agencies appear to be the most promising elements for providing basic low income housing delivery in rural areas in a relatively short period of time. At the core of any rural low income housing delivery system should be a strong public housing and community development agency.

2. Although the most common public institution with low income housing capabilities in rural areas is the small local housing authority, it is often an inefficient operation. Regardless of stated HUD "policy," small authorities have proliferated in recent years. HUD should enforce its policy of consolidation of small housing programs.

3. Regional and State public housing authorities are providing housing for families and the elderly living in small towns and rural areas. Their operations have overcome many of the problems faced by small local housing authorities, and their structure provides a realistic approach to serving rural areas. These types of agencies have jurisdictional responsibility for small towns and unincorporated areas that would not otherwise be able to sustain their own housing programs. It should become national policy to encourage regional and State approaches to rural housing community development needs wherever feasible.

4. Rural regional housing authorities are, generally, single purpose agencies, and rarely administer comprehensive community development programs. Further study of these agencies would unveil the full spectrum of their powers and why those powers are not being used. Research is needed into the potentialities and drawbacks inherent in broadening the responsibilities of rural housing authorities, and there should be demonstrations of how these authorities could expand their responsibilities to include other community development roles in rural areas.

5. Economic development districts and regional planning agencies should have overall development plans for the areas they serve that in-

tegrate housing with economic and other types of development. Additionally, some of these agencies have or are seeking program implementation powers. There should be further research into the powers (planning, technical assistance, implementation) of these agencies, and demonstrations of how the full complement of their powers can be used to house low income rural people.

6. State housing agencies have yet to meet the needs of rural areas. State agencies should be encouraged to take immediate steps towards designing and implementing rural low income housing programs, even though this entails additional legislation in many States.

7. All moves toward regional or State housing delivery mechanisms must respond to the arguments for local control. Particularly in the public housing program, the notion of local control has become firmly entrenched. It should be national policy to provide communities with information on the benefits of cooperative efforts, and there should be rewards (housing unit set-asides, etc.) for those communities willing to join in a regional program. State laws should be amended to allow all options for regional and State housing structures.

8. There are many more alternatives to rural low income housing delivery beyond those presented in this report. Although the case studies present various rural housing authority operations and some information was gathered on other types of agencies, much greater detail would be useful. Further research should be conducted into the alternative institutional approaches to rural low income housing delivery and more detailed comparisons should be made of the relative benefits of each.

An Overview of Rural Public Housing Problems

Rural America's critical problems of poverty and bad housing are not mentioned as often as those of the cities, although all available evidence shows that they are as severe. In absolute numbers, poverty level people and inadequate housing units are found about equally in urban and rural areas. Because of the smaller rural population, however, the incidence of poverty and inadequate housing in rural areas is much greater than that in the cities. One metropolitan house in 25 is inadequate, and one person in nine is below the poverty level. In nonmetropolitan areas, one house in seven is inadequate, and one person in five is poor.[1]

Unfortunately, there is a great distance between documentation of this situation and an adequate response to it. Most federally assisted housing programs, as Table 1 illustrates, have focused mainly on the housing needs of moderate income families and the elderly. The exception to this moderate income focus is public housing. With capital grants for construction, and subsequent operating subsidies, this program is specifically designed for poverty level families and the elderly.

Table 1. Percentage Distribution of Families Served by Federally Assisted Housing Programs, by Gross Annual Income

	PROGRAM				
Income	502 [1]	235 [2]	236 [2]	Rent Sups.[2]	Public Housing [2]
Less than $3,000	3.7	0.8	19.0	58.0	61.0
$3,000 to $3,999	7.4	3.8	15.0	20.0	21.0
$4,000 to $4,999	13.4	14.2	20.0 [3]	11.0	11.0
$5,000 to $5,999	15.6	25.2	19.0	5.0	5.0
$6,000 and over	59.0	56.0	27.0	5.0	3.0
Median Income	$6,502	$6,241	$4,831	$2,658	$2,510

[1] Farmers Home Administration, 1972.
[2] HUD, 1971 Statistical Yearbook.
[3] It is doubtful that nearly 50 percent of 236 tenants would have annual incomes less than $5,000 if they were not receiving rent supplements, since the average family income for nonsubsidized families in 236 housing is approximately $6,000.

Although it cannot be said that the public housing program is an accurate measure of the total Federal response to housing needs, it is a

[1] Because figures on dilapidated and deteriorating housing are unavailable, inadequate housing is defined here as housing that is lacking some or all essential plumbing facilities or having more than 1.01 persons per room. The poverty definition used is the same as that established by the Office of Economic Opportunity, an amount that is now approximately $4,200 for a family of four. All figures on poverty and inadequate housing can be obtained from the 1970 Census of Housing (*Detailed Housing Characteristics*) and Census of Population (*Detailed Social and Economic Characteristics*).

Table 2. Percent Distribution of Public Housing ACC's, Population Inadequate Housing, and Poverty Level Persons, by Metropolitan Status and Population Density of Counties, 1971

County Classification	Percent of Population	Percent Of Inadequate Housing[4]	Percent Of Poverty Population	Percent Of ACC's
Metropolitan[1]				
high density[2]	65.1	51.2	51.9	74.6
low density[3]	4.4	4.6	4.7	2.9
Subtotal	69.5	55.8	56.6	77.5
Nonmetropolitan				
high density	7.8	8	7.7	6.4
low density	22.7	36.2	35.7	16.1
Subtotal	30.5	44.2	43.4	22.5
Total	100	100	100	100

[1] Metropolitan counties are those found within a Standard Metropolitan Statistical Area, as designated by the U.S. Bureau of the Census.
[2] A high density county has more than 100 persons per square mile.
[3] A low density county has less than 100 persons per square mile.
[4] Lacking some or all essential plumbing facilities, or more than 1.01 persons per room.
Source: U.S. Bureau of the Census; Department of Housing and Urban Development.

measure of the response to the housing needs of the poor.[2]

In rural areas, the most critical housing needs are those of the poor, and the extent to which public housing is available in these areas measures how well the housing needs of the poor are being met.[3]

The Housing Assistance Council (HAC) and the Rural Housing Alliance have published a study on the distribution of federally assisted public housing units between urban and rural areas. Table 2 is a brief summary of the findings of this study.

Roughly half of the Nation's counties and county equivalents, containing 36 million people, still had no public housing at the end of 1971, even though their need for public housing was as great or greater than in those counties with a program.[4] Clearly, rural areas have not received a share of public housing assistance proportionate to their need.[5]

Reasons for the Inequitable Distribution of Units

There are a number of reasons why rural areas have not received their share of public housing assistance. For one, there are a limited number of units available and the competition among localities for these units is intense. (According to the most recently available HUD data, there were well over 400,000 units in the

[2] The rent supplement program, when attached to subsidized housing units produced under the Federal Housing Administration (FHA) sections 236 and 221(d)(3) programs, also serves poverty level families and the elderly, but, like the other FHA programs, it is largely urban. It is estimated that as of late 1971 only 29 percent of the FHA rent supplement units were outside of metropolitan areas. (See *Low-Income Housing Bulletin*, November 1972, published by the Rural Housing Alliance.) The scale of the rent supplement program should also be considered. In fiscal year 1972, there were more than 100,000 public housing units brought under annual contributions contract (ACC), but only 42,000 rent supplement unit reservations.

[3] The Census Bureau's *Metropolitan Housing Characteristics* shows that fully 60 percent of the housing units in nonmetropolitan areas that lack essential plumbing facilities or are severely overcrowded (more than 1.5 persons per room) are occupied by persons and families with incomes of less than $4,000 per year.

[4] See *Public Housing: Where It Is and Isn't*, by the Housing Assistance Council and the Rural Housing Alliance (available upon request). This study measures the cumulative inequity in the distribution of public housing units since the inception of the program some 30 years ago. In recent years, the distribution of these units between urban and rural areas has been more balanced: from 1959 through 1961 only 25 percent of public housing starts were outside of Standard Metropolitan Statistical Areas; more current figures show the nonmetropolitan share has risen to approximately 42 percent.

[5] It should be pointed out that none of the existing housing programs were intended to meet the need fully. To quote a former Assistant Secretary of HUD for Housing Production and Mortgage Credit, ". . . those who talk about the inequalities and inequities in present programs appear to be lacking in sufficient sophistication, . . . the very inequities are the only things that make them possible." (Interview with Eugene Gulledge, *Housing Affairs Letter*, No. 73–10, March 9, 1973). The point is, of course, that any program designed to meet all low income housing needs would never be created because of the expense. Recognizing this, the complaint made here is not that rural housing needs have not been met—this is not a startling discovery—but rather that those housing resources that do exist have been directed in the past largely to urban areas.

public housing application pipeline as of December 1971.)[6] Because much of the poverty and bad housing in rural areas is invisible to many legislators and program administrators, urban lobbies have taken the lead in the competition for housing units by citing the grave and highly visible concentrations of poverty and bad housing in the cities.[7] (Although purely speculative, it might also be asked whether legislators representing rural districts have been concerned enough with low income housing problems to exert the pressure on the executive branch necessary to see that units are equitably distributed.)

Not all of the disparity in unit distribution can be attributed, however, to the Federal Government's failure to recognize rural housing needs. As mentioned, roughly half of the Nation's counties have no public housing units at all, and this is usually because small rural communities have not taken the initiative necessary to obtain them. For example, ignorance of the program, after 30 years, is still widespread. Although many small rural communities have heard about public housing, they do not know how to form a housing authority or how to apply for units, and HUD does not have an outreach staff to promote the program. (In fact, HUD staff will usually avoid anything resembling promotion, lest they be accused of "forcing" public housing on an unwilling community; HUD relies at all times on "local initiative.")

Some rural communities do not have public housing because of their suspicion of Federal programs or fear of becoming involved with what appears to be a complex undertaking. Others choose to ignore the housing needs of their poor. But although these are real barriers to the development of public housing programs in small rural communities, they are not insurmountable.

If a community does not initiate a public housing program because of suspicion or apathy, the benefits of the program can be explained and put within the context of that community's actual need for low rent housing. Most communities need the housing, and normal civic pride and the desire to prevent further deterioration are usually enough to spur action. If the problem is a lack of local technical expertise, training programs and technical assistance are the solution.

Recognizing that HUD lacks sufficient staff for outreach activities, numerous organizations emerged in recent years to assist small communities in developing low income housing programs, including public housing. They have been successful in many instances. Only in those communities displaying a complete disregard for the housing needs of the poor—and there are still too many of these—can nothing at all be done. However, although an aggressive program of education and technical assistance can result in the creation of low rent public housing programs in many rural areas and small communities, the problem is more complex than this. Housing problems always are.

There are thousands of small rural communities; should each one be encouraged to undertake its own public housing program? The inadequacies of this approach are obvious in terms of time, availability of competent personnel, and overhead costs. In addition, HUD has been aware for some time that small housing authorities have inherent operational deficiencies and, in a number of HUD regions, the agency has been reluctant to allocate units to small rural authorities. According to HUD management specialists, too many small authorities are unable to run their programs economically and efficiently.

Small Authority Problems

The proliferation of small housing authorities, particularly in the South, began in the prewar 1940's and has continued to the present day. During those early years, many small communities were visited by traveling architects intent on increasing interest in their architectural wares (and, undoubtedly, by a few ambitious Congressmen, anxious to bring funds into their district). Once one community was convinced of its need for housing (that is, housing designed by a particular architect), word would spread to neighboring communities. In the spirit of "keeping up with the Joneses," the surrounding communities would invite the architects to draw up plans for each town's own housing authority and project.

Although the traveling architect is a rarity today, small authorities continued to proliferate through 1970. HUD Statistical Yearbooks show that between 1966 and 1970 there were more than 1,200 local housing authorities created in places of 10,000 population or below. As of 1970,

[6] HUD, Report S-10, *Publicly Financed Housing Directory of Applications and Reservations, As of December 31, 1971.*

[7] It is also true that the larger cities have often had first claim on available public housing units because of the relocation needs associated with other Federal programs, e.g., urban renewal, which are rarely used in small towns and rural areas.

housing authorities in places of 2,500 population and below were 49 percent of all housing authorities, as shown in Table 3.

Table 3. Low Rent Public Housing: Number and Percent of Places and Housing Units Represented by Local Housing Authority Programs, by 1960 Population of Place, as of December 31, 1970

Population Size Group	Places with LHA Program[a] Number	Percent	Housing Units[a] Number	Percent
Total	4,399	100	1,270,007	100
1,000,000 and over	5	(b)	191,547	15
500,000 to 999,999	16	(b)	163,223	13
500,000 to 499,999	31	1	173,957	14
100,000 to 249,999	82	2	142,126	11
50,000 to 99,999	164	4	134,769	10
25,000 to 49,999	257	6	112,011	9
10,000 to 24,000	531	12	123,261	10
5,000 to 9,999	516	12	72,715	6
2,500 to 4,999	646	14	60,198	5
Under 2,500	2,151	49	96,200	7

[a] Under program reservation or later stages.
[b] Less than 0.5 percent.
Source: HUD, 1970 Statistical Yearbook

The proliferation of small housing authorities has had considerable effect on the workload of Federal housing staff. Not only have hundreds of applications required processing, but relationships have had to be developed with hundreds of executive directors, mostly part-time, who often do not know the first thing about the public housing program. Too often, once a project was completed, and the impetus for creating the local program dulled or departed (such as the traveling architect of earlier days), a community was left with housing but rarely with the capacity to see that it was efficiently managed.

In the section entitled "Terms and Conditions" (section 101, article 1) of HUD's public housing Annual Contributions Contract (ACC), public housing objectives are clearly stated:

> Each project shall be undertaken in such a manner that it will not be of elaborate or extravagant design or materials, and will be developed and administered to promote *service-ability, efficiency, economy, and stability* and to achieve the economic and social well-being and advancement of the tenants thereof. (Emphasis added)

Two of the key words here are "economy" and "efficiency." Prior to the subsidized housing moratorium, HUD staff was prohibited from allocating units to authorities whose projects could not show "economic feasibility." The term refers to the project's ability to generate more income than required for operating expenses, and to do this without additional HUD operating subsidies. "Efficiency" is closely related to economy and good efficient management practices can keep operating expenses down.

According to HUD regional and area office staff, efficient management is clearly a function of good managers: individuals with experience, initiative, and drive. Such talents generally demand a decent living wage which most small housing authorities are unable to pay. After its fixed costs, utilities, insurance, and payment in lieu of taxes are paid, there is little revenue left for the payment of salaries. For example, if HUD approved the allocation of 25 units to an authority, and allowed use of $10 rental income per unit for administrative salaries and fringe benefits, the authority would have $250 a month to hire administrative staff. Only part-time staff can be obtained with this amount of money. This is how HUD, in its guide, "Low Rent Housing—Consolidation and Cooperative Arrangements for Small Low-Rent Housing Programs," April 1972, states the problem:

> For some small Low-Rent programs, funds available for employment of personnel are not sufficient to employ even one full-time employee. Such programs often operate on the edge of financial feasibility. It may be extremely difficult to find a competent person to accept the responsibility of Executive Director and housing manager for the small compensation which the Local Authorities can afford to offer. As a consequence, many small Local Authorities have been unable to carry out their operating responsibilities in a proper and efficient manner. The deficiencies are usually manifested by poor accounting records and reports, high rent delinquencies, and inadequate maintenance. In summary the operational units may be too small to be efficient.

Earlier this year, the Housing Assistance Council polled the Housing Services and Property Management sections of HUD area offices to determine if there was a minimum number of low rent public housing units considered necessary for an efficient program. Although the responses were not unanimous and were probably related to differing local cost factors, there was considerable agreement. One of the questions asked was as follows:

> Based on low income housing experience in your area, what is the minimum number of units that an authority can operate and still be considered 'efficient'?

No. of Units	No. of Responses
No Minimum	3
40	1
50	3
60	1
75	2
100	12

(Continued on p. 641.)

(Continued from p. 640.)

No. of Units No Minimum	No. of Responses
125	1
150	1
200	1
250	2

Seventeen of the 27 offices responding stated that 100 or more units were minimally adequate. When asked why the number given was considered to be a necessary minimum, 20 of the 27 responses stressed the ability to recruit and retain a competent full-time staff. A number of responses also mentioned the economies of scale available to a larger program, and a few expressed some concern about the financial stability of very small authorities.

In spite of these responses, nearly half of the Nation's housing authorities now have less than 100 units under management, and fully 28 percent have 50 units or less.

Table 4. Percent Distribution of Local Housing Authorities, by Number of Units Under Management, as of December 31, 1972

Number of Units	Number of LHA's	Percent of LHA's
1-49	763	28.1
50-99	574	21.1
100-99	526	19.4
200-299	266	9.8
300-499	227	8.4
500-799	126	4.6
800–1,249	87	3.2
1,250 +	144	5.3
TOTAL	2,713	100

Source: Department of Housing and Urban Development.

Complaints against the use of part-time staff are numerous. For example, HUD's southeastern regional staff has found that part-time employees of small authorities have neither the time nor the skill to complete the extensive financial and tenant data forms that HUD requires. Frequently, a part-time director will leave the program when yearend reports or reexamination of incomes are due, leaving accounts in disorder, allowing rents to become delinquent, and maintenance to decline to a lower level than already existed. The personnel turnover rate is legendary. One small authority in Georgia had nine part-time directors resign in 7 months; another in Alabama saw four directors leave in less than 2 years. Perhaps the greatest stability of some of the small authorities is their low tenant turnover rate.

High turnover in small authority personnel is acutely felt by HUD area office staff. Each time a new housing authority director is hired, HUD has the responsibility for educating that person to HUD requirements because few have had experience in public housing. In recent years, cutbacks in HUD housing management staff and the inexperience of the remaining staff has limited the Agency's ability to respond to the time-consuming needs of small authorities. These authorities require as much attention (and sometimes more) as the larger better staffed authorities. In Georgia, where numerous small authorities operate, the area office recommends a workload of 25 authorities for each HUD "professional" in housing management. The actual workload, however, is 45 authorities.

Deficiencies of small housing authorities have been outlined by HUD in various management circulars, and interviews with HUD area office staff having years of experience with small authorities confirm these deficiencies. Small authorities, as stated before, tend to be poorly staffed and, consequently, over-worked. Frequently, rents are not collected on time, and financial and tenant reports are incomplete and late.

In addition to these administrative deficiencies, there are other aspects of the public housing operation that are given inferior attention. Without a preventive maintenance program, for example, any type of housing will deteriorate; public housing is no exception. But preventive care of housing units is generally not possible without a full-time maintenance staff. Instead, maintenance becomes crisis-oriented and is often more costly in the long run. Most HUD area offices confirm that a full-time maintenance employee is not possible with less than 50 units under management.

For example, one small authority in Georgia was operated by a $50 per month, part-time director. Maintenance was sporadic, and the result was excessive utility bills. When the authority entered into a cooperative management agreement with a larger local authority, the managing authority found that the project's heating system had not worked properly for 2 years. Units were too warm, so tenants kept their doors and windows open, thus using up more heat. Utility bills had consistently put the project in debt, but within 2 months after the new managing authority fixed the heating system, the project broke even.

Table 5. Types of Housing Authorities Permitted Under State Legislation

	State	Regional	Consolidated	County	Municipal	Cooperative Agreement
Ala.		X	X	X	X	X
Alaska	X	(1)				
Ariz.				X	X	X
Ark.		X		X	X	X
Calif.		X		X	X	X
Colo.				X	X	X
Conn.					X	X
Del.	X			(2)	(2)	
Fla.		X		X	(3)	X
Ga.		X	X	X	X	X
Hawaii	X					
Idaho	X			X	X	X
Ill.		(4)		X	X	X
Ind.				X	X	X
Iowa				X	X	(5)
Kans.						X
Ky.		X	(6)	X	X	X
La.		X	X	X	X	X
Maine	X	X			X	X
Md.					X	X
Mass.				(7)	X	X
Mich.				X	X	X
Minn.		X	X	X	(8)	X
Miss.		X	X	X	X	X
Mo.				X	X	X
Mont.				X	X	X
Nebr.				X	X	X
Nev.	X			X	X	X
N. H.					X	X
N. J.			X	(10)	X	
N. Mex.		(9)			X	X
N. Y.					X	X
N. C.		X	X	X	X	X
N. Dak.				X	X	X
Ohio				(11)	(11)	X
Okla.		(12)			X	X
Oreg.					X	X
Pa.					X	(13)
R. I.					X	X
S. C.	X	X	X		X	X
S. Dak.	X		X	X	X	X
Tenn.		X		X	X	X
Tex.		X		X	X	X
Utah				X	X	X
Vt.	X				X	X
Va.		X	X	X	X	X
Wash.				X	X	X
W. Va.	X			X	X	X
Wis.				X	X	(14)
Wyo.		X	X	X	X	X
Total	10	21	12	35	47	46

(1) Regional Native Housing Authorities (Indian).
(2) The Delaware Department of Community Affairs and Economic Development may create a housing authority for a county or any part of a county if the need is demonstrated.
(3) Only in cities of 2,500 population or above.
(4) A maximum of five contiguous counties.
(5) An Iowa attorney general's opinion allows cooperative agreements under the State's Intergovernmental Cooperation Law.
(6) The Kentucky law also includes provisions for a "city-county" authority.
(7) Town and city authorities in Massachusetts may provide housing in the surrounding rural areas.
(8) Subsequent to the creation of a county or multicounty authority, no additional municipal authorities may be created within that area without the permission of the county or multicounty authority and the State housing commission.
(9) Six regional authorities covering the entire State have been created by the State legislature.
(10) A county authority may be created with permission of the director of the State public housing and development authority, and only if no municipal authorities already exist in the county.
(11) The Ohio State Board of Housing may create "metropolitan" housing authorities that comprise two or more political subdivisions, or portions thereof, but that may not comprise an entire county.
(12) Rural electric cooperatives may now serve as regional housing authorities.
(13) Cooperative agreements may be entered into only with the permission of the secretary of the State department of community affairs.
(14) Cities of the first class may not enter into cooperative agreements.

A Better Approach To Rural Public Housing

Many small rural authorities have attempted to overcome their deficiencies by cooperating with other authorities in the development and management of public housing units. The notion of cooperation was first, and perhaps most extensively, promoted more than 20 years ago in the South, where most of the small authorities were located. HUD's staff there (or those of its predecessor, the Public Housing Administration) were exhausted by the burden of working with a multitude of small authorities, and decided that a better approach to rural public housing was required. The result was a patchwork of agreements generally authorizing larger authorities to operate housing units belonging to smaller authorities.

These agreements were legitimized in various HUD management circulars published since 1963. The circulars describe the "deficiencies" of small authorities and urge, but do not require, various forms of consolidation.[8]

State enabling legislation determines the types of housing authority consolidations allowable in each State. Most States fashioned their basic legislation after a model law prepared by Federal attorneys following the passage of the 1937 housing bill, which created the public housing program. Beyond the basic provisions, however, most States exercised their preferences, particularly in the area of authority consolidation. At least 46 States now allow for cooperative agreements between and among housing authorities, 19 States specifically allow for regional authorities, and 12 have provisions for consolidated municipal authorities. (Descriptions of these alternatives follow.)

Types of Housing Authorities

Municipal: A housing authority serving a single municipality (city, town, village, etc.). In many States a municipal housing authority may also provide housing outside the city limits up to a legislatively determined distance. A municipal authority is created by the local governing body with commissioners normally appointed by the mayor.

County: A housing authority serving an entire county, but which may not provide housing in any incorporated locality within the county without the permission of that locality. A county authority is created by the governing body of the county with commissioners appointed by the governing body.

Consolidated: A single housing authority serving several municipalities. It has a single board of commissioners, with one member appointed by the mayor or governing body of each participating municipality. It has a single annual contributions contract for all of its projects. After meeting certain requirements, additional municipalities may become part of the consolidated authority, or existing members may leave the union.

Regional: A single housing authority serving several counties. Like the county authority, it may not provide housing in any incorporated locality within any of the participating counties without the permission of that locality. It has a single board made up of commissioners, appointed by the governing body of each participating county, and a single annual contributions contract for all projects. After meeting certain requirements, additional counties may become part of the regional authority, or existing members may leave the union.

Cooperative Agreements: Most State enabling laws allow any two or more housing authorities to develop and operate housing cooperatively. The types of combinations among authorities are unlimited; for example, two or more city authorities may cooperate, or two or more counties, or even a combination of city and county authorities. Forms of cooperation are numerous, also. These are the most common: (1) Several authorities may decide to use the same administrative staff and prorate costs among themselves, usually according to the number of units each authority controls; (2) several small authorities may contract with a larger authority for specific services, such as accounting or maintenance, and will pay the larger authority a fee for its work. Other forms of cooperation are possible but, in all forms, each authority retains its own board of commissioners and its own annual contributions contract. Although the authorities retain their separate identities, some have chosen to form an executive committee, comprised of one member from each participating

[8] The National Association of Housing and Redevelopment Officials (NAHRO) established in 1965 a "small authorities committee" as part of its housing division. Recognizing the problems of small authorities and witnessing their proliferation, the small authorities committee met several times to develop recommendations for more efficient operations. The committee persuaded HUD to publish a management circular on consolidated housing efforts. The committee documented the problems of small authorities and the manner in which several had attempted to overcome their difficulties.

authority, to act for the individual boards. Some also have established an unlimited revolving fund, pooling their funds each month to pay certain bills.

A variation of the cooperative agreement occurs when a community chooses not to create its own housing authority, but instead authorizes the authority of a neighboring town to develop and manage public housing within its jurisdiction.

State: Some States have enabling legislation creating a State housing authority to develop and manage housing units in areas not already covered by local or regional housing authorities. Like the county and regional housing authorities, State housing authorities must obtain local permission to operate in incorporated areas, or where another authority already has jurisdiction. State authorities have a single board of commissioners, usually selected by the Governor, and a single annual contributions contract for all projects.

The potential advantages of consolidation are numerous, and will be discussed but, in preface, a few words are needed on the relative advantages of each of the various forms of consolidation. Cooperative agreements, although by far the most widespread form of consolidation, are frequently the least desirable, because each cooperating authority retains its own board of commissioners and annual contributions contract (ACC). With separate ACC's, the managing authority's accountant must retain a separate set of books for each authority's account. Also, by retaining separate boards of commissioners, each board (regardless of the number of units it controls) requires individual attention by the managing authority's executive director. In a Public Housing Administration circular, dated November 9, 1965, the "major disadvantage" of this arrangement is explained: ". . . the Executive Director is subject to the control of several Local Authority Boards, and this sometimes detracts from the time, thought, and effective effort given to supervision of routine operations."

The diversion of the executive director's time can be lessened if cooperating authorities form an executive committee of one representative from each board of commissioners. This committee could meet with the executive director on items affecting all the authorities, and the executive director would have to meet with an individual board of commissioners only when there was an issue affecting that particular authority.

A second form of consolidation, the joint municipal or consolidated authority, is preferable in structure to a cooperative agreement because it provides for only one board of commissioners and one annual contributions contact. But this form has one serious disadvantage for rural areas: it can only provide housing within municipal boundaries (incorporated areas) or, in some instances, within 10 miles of the municipal boundaries. There are many unincorporated areas in need of public housing, and these areas would normally not be able to participate in a consolidated (municipal) authority program.

The preferable choice of consolidation for rural areas is the regional housing authority. This type of authority covers all unincorporated areas of the participating counties, and all incorporated areas where permission is given to the regional authority to operate its housing program.[9] Small communities wishing to obtain public housing can participate in the regional program merely by passing a resolution and thereby avoid the process of creating and staffing an authority. In addition, a regional authority has a single board of commissioners and a consolidated annual contributions contract for all projects.

The State housing authority is a variation of the regional authority concept, although it could be more difficult to operate because of the long distances that staff must cover. In States where individual county populations are exceptionally low, however, such as Nevada or Vermont, this type of authority may be the best or only alternative for a reasonably efficient housing program.

Advantages and Disadvantages

Ten years ago, the Public Housing Administration summarized what are considered the "advantages" of regional authorities. The list is not only timely, but it can be extended to consolidated and, to some extent, cooperative agreement authorities as well:

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[9] The county authority, permitted in 38 States, also serves this purpose, but the population of many counties may also be too small to support an adequate sized program. Fully 27.4 percent of the Nation's counties have less than 10,000 population

Percent Distribution of U.S. Counties, by Population Size, 1970

Population	Number	Percent
Below 10,000	839	27.4
10,000–24,999	1,002	32.7
25,000–49,999	567	18.5
50,000–100,000	326	10.6
Over 100,000	331	10.8
TOTAL	3,065	100

Source: U.S. Census Bureau

1. The larger total program permits payments of salaries to attract and retain better qualified administrative staff.

This is self-explanatory and applies to all forms of consolidation, not only regional authorities. With a larger number of units under management, better salaries and full-time employment can be offered, and an authority is more likely to attract experienced staff. HUD has found that competent, well-paid, and full-time employees tend to stay on the job much longer, thus lending stability to an authority's housing program.

2. Operating costs compare favorably with the average cost of operating other single authorities in the nearby area.

Cost comparison is probably the least reliable gauge of the advantages of consolidated housing efforts. In some instances it may appear that regional or similar housing authorities have higher per unit costs than smaller authorities. The difference is usually in service. Smaller authorities may cost less because they give less service. In the long run, inadequate but cheap service will have its effects. The lack of preventive maintenance or a procedure for prompt rent collection will result in higher nonroutine maintenance costs and higher collection losses.

3. Under a consolidated annual contributions contract, operating receipts from all projects are combined and are available to meet emergency and other unforeseen expenditures at any location.

Although cooperative agreement authorities have separate annual contributions contracts, many of them pool their rental income in an unlimited revolving fund for the payment of monthly bills. Each authority is then charged, on a prorata basis, for its share of the expenses. Regional and consolidated authorities have only one account. By sharing funds, one housing project is not made to suffer indebtedness, for whatever reason, while another project is operating in the black. Projects can support each other. This arrangement can make feasible the placement of a modest number of units in a small rural town; another larger project can help support the smaller.

4. Budget, accounting and fiscal reporting functions are performed in a more satisfactory manner.

It stands to reason that a more competent full-time staff produces a better product. In the areas of budgeting, accounting, and fiscal reporting, the regional or consolidated authorities are superior to the cooperative agreement authorities because they have a single annual contributions contract. This means that only one set of books needs to be kept, and one set of reports filed.

The Public Housing Administration list of advantages omits one worth mentioning—adequate and timely maintenance. Larger authorities can afford to hire full-time maintenance staff and, therefore, are able to provide preventive maintenance care. In the long run, the cost of hiring full-time staff is balanced with expenses eliminated by preventing deterioration. Rehabilitation is much costlier than ordinary maintenance.

In addition, larger authorities can conceivably obtain economies of scale in the bulk purchase of materials and equipment. The purchase of heavy equipment is especially important because rental charges are often excessive.

Having briefly described the potential advantages of regional or similar public housing authorities, attention should be given to what HUD has characterized as the "disadvantages." The officially published list is surprisingly short and usually stresses distance and lack of personal service. For example, when several rural authorities combine for management services, the distance between projects may consume a large amount of travel time and can quickly deplete a travel budget. If the combined number of units is large enough, however, and the distances great enough, travel time can be lessened by stationing staff in several locations. Distance does not have to be a barrier to good management.

There is also the notion that local, as opposed to regional, housing authorities always have at least a part-time employee nearby to whom tenants can go with complaints. Even when this is true, it does not assure that tenant complaints will be answered. Admittedly, authorities with units dispersed over a large geographical area cannot afford to place a staff member in each project, but such authorities have found numerous ways to compensate, as the descriptions in the next section illustrate.

Aside from the two disadvantages listed in HUD circulars, some HUD area office staff warn of another potential disadvantage of consolidated housing efforts—political embroilments. With a variety of separate political jurisdictions to contend with, regional and other forms of consolidated authorities must tread carefully to avoid favoring one community at the expense of another. Smaller communities may fear that the larger communities participating in a cooperative management agreement or regional authority might attempt to control the direction of the housing program. Regional authorities confront these political realities daily and have, as the following section will show, taken some precautions to avoid divisive political entanglements.

An appropriate conclusion to this introduction is found in the most recent HUD circular, "Consolidation and Cooperative Arrangements for Small Low-Rent Housing Programs" (April 1972):

> In general, the advantages of consolidation or combination of operations by any of the methods described above far outweigh the disadvantages. . . . It is hoped that the favorable results experienced by many Local Authorities participating in these types of arrangements will serve as an incentive to other small Local Authorities to enter into similar arrangements, thereby contributing to manpower and cost savings and furthering the objectives of the low-rent public housing program.

Studies of Rural Authorities: Regional, State, and Cooperative Agreements

Case studies of some rural housing authorities were developed to provide an overview of how these alternative forms of consolidated housing efforts operate. An examination of the lists of regional, State, and cooperative agreement authorities shows that at least for regional and State authorities, the choices for study were limited. As of December 1972, approximately 30 regional authorities were organized, but few of these had units under management. Only nine States have formed State housing authorities; many are just beginning their programs. In contrast, cooperative agreement authorities are far more abundant.

HUD area and regional offices assisted HAC staff in selecting authorities to visit. Federal housing officials in the southeast, where there has been the most activity in combining public housing programs and where rural regional authorities have operated for decades, were asked to recommend a variety of regional and cooperative agreement authorities. An additional cooperative agreement authority in the Rocky Mountain area was chosen because it was recently formed and offered a fresh outlook on the problems of creating a unified housing program. The choice of a State authority was limited by the small number with units under management, but HAC selected one with an entirely rural program.

These authorities were selected for the study:

- Regional: South Carolina Regional Housing Authority No. I; Mississippi Regional Housing Authority No. VIII; Tennessee Valley Regional Housing Authority, Miss.
- State: Vermont State Housing Authority.
- Cooperative Agreement: Housing Authority of the City of Americus, Ga.; Housing Authority of the City of Nashville, Ga.; San Luis Valley Housing Committee, Colo.

HAC staff visited these authorities, interviewed their employees, and visited some of their housing projects. Personal interviews were also held with HUD management staff in the Mississippi, South Carolina, and Georgia area offices, and the Atlanta and Denver regional offices. These area and regional offices not only provided information on the specific authorities, but also gave overall impressions of regional and similar housing structures in rural areas. These impressions have been incorporated throughout the study. From these interviews, the following descriptions were developed. It should be noted that the descriptions represent the status of these authorities prior to March 1973, and that change may have occurred subsequent to that date.

Case 1. South Carolina Regional Housing Authority No. I

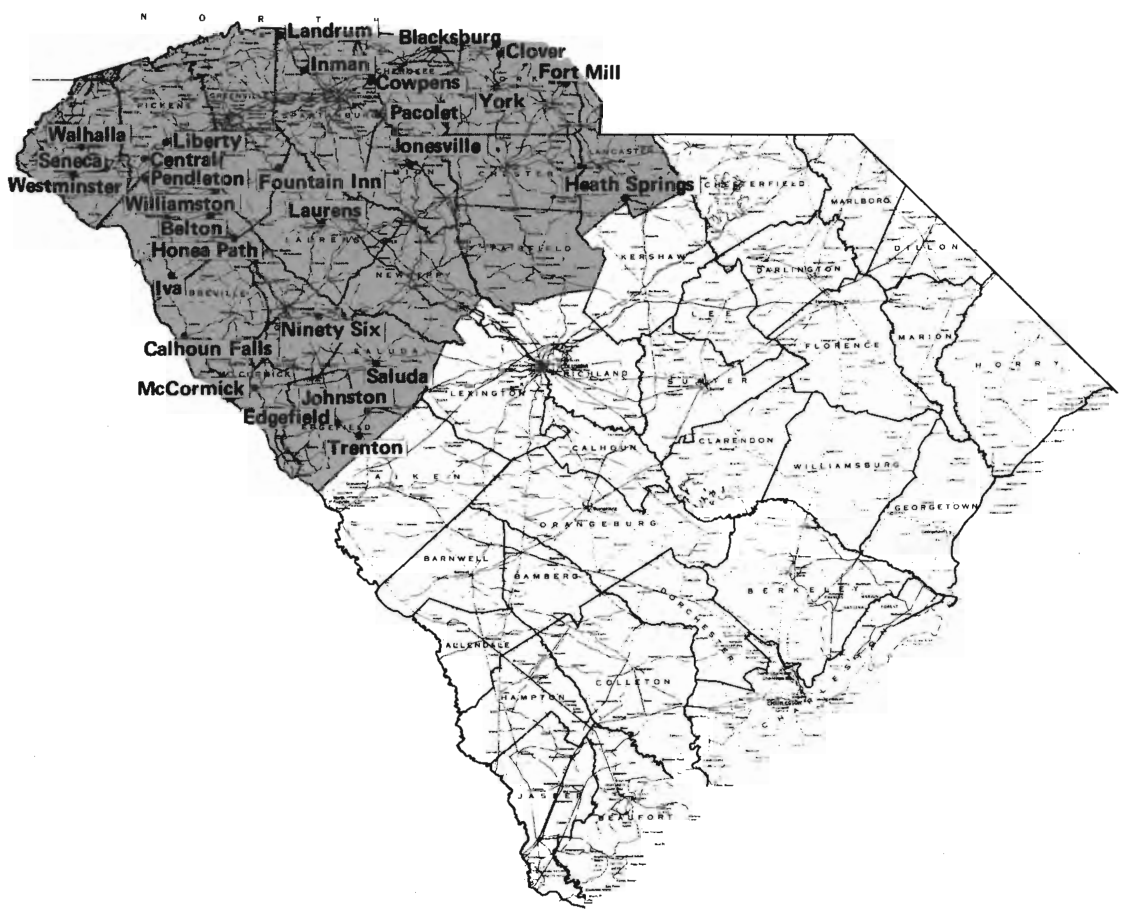
South Carolina Regional Housing Authority No. I, located in Laurens, S.C., was recommended for inclusion in this study by the HUD regional office in Atlanta and by a number of southeastern HUD area offices because of its unique management and maintenance organization and its excellent record for financial solvency. Created under State legislation that favored "regional" authorities, this authority has extended its housing program to nearly 30 small towns. Although the housing projects are widely dispersed, the authority has been able to retain a constant and remarkably high standard of maintenance. In terms of efficiency and economy, Region No. I provides one of the best examples of a regional low rent housing program.

Authority Background: South Carolina Regional Housing Authority No. I was organized under State law in August 1941, although it remained dormant during the war years. By 1948, the authority's first and current executive director was hired, and applications were submitted for units to be constructed in 1950–51. Since that time, 1,110 units have been built despite two lengthy construction lulls. The first lasted from 1952 to 1957 when public housing funds were nonexistent. The second, overlapping the first, lasted until 1968, during the time when Federal housing legislation required that a community have a "workable program" before public housing units could be allocated (most of the region's small towns could not fulfill workable program requirements).

There are 16 States that specifically allow for the formation of regional authorities. South Carolina's original housing law was unique, however, because it gave regional authorities jurisdiction over any portion of their member counties having less than 5,000 population, unless those areas were already served by local housing authorities. The regional authority located its main office at Laurens, a town at the center of Region No. I that had its own authority when the regional authority was organized. When the need for elderly housing in Laurens became substantial, the town requested the regional authority to build and manage units there because the Laurens authority had only 120 units and was not eager for more responsibility. A legal waiver was obtained and the regional authority now owns and operates 80 units of elderly housing within the town's boundaries.

Since the State's enabling legislation was adopted, there have been numerous amendments, and now any size town can form its own authority. A few small towns in Region No. I formed separate LHA's with units under ACC; however, none has entered construction. The regional authority is currently considering proposals for management and maintenance contracts with these small authorities.

The regional boundaries have not changed since they were designated in 1941. At that time, the State was divided into three geographic areas, each with its own authority. Region No. I covers the entire northwest triangle of the State —an 18-county area approximately 160 miles in diameter, as shown on the accompanying map.



Small towns, many with less than 1,000 population, dot the region and are usually near to each other. The regional authority will only build within towns because it has found that county governments are unable to provide water, sewer, and other services necessary for housing projects.

The region provides some striking contrasts in incomes between the northern and southern areas, and the differences are reflected in the authority's slightly higher income limits for applicants in the northern areas of the region. Income differences are attributable to the types of employment available in different parts of the region. In the north, the small towns are mostly industrialized—South Carolina is a "right-to-work" State that attracts numerous small and large manufacturing plants—and wages there average about $4.00 per hour. Employment tends to be steadier in the north than in the south, where it is often seasonal and dominated by the lower paying pulp wood industry and some agriculture.

The proliferation of employment opportunities in the region, particularly in the northern counties, has been matched by a housing boom, primarily for moderate income families but at a cost level low enough to attract from public housing some higher income families. New housing, costing about $15,000 to $16,000, has caused a small exodus of public housing families. Several years ago, the proportion of families to the elderly in the authority's units was 65 to 35; it is now 50 to 50. This reduction has caused a loss of rental income; the elderly pay an average of only $25 per month, while the overall average is $35.

The Authority's Program: There are 57 projects totalling 1,110 units under management in the region. Since the projects are numerous, the total number of units in each town is shown below; all towns have two projects each, except for Seneca, which has three projects, and Ninety Six, which has one.

Location	Population	Units
(Zone 1)		
Westminster	2,521	32
Seneca	6,027	133
Walhalla	3,662	60
		225
(Zone 2)		
Belton	5,257	34
Pendleton	2,615	41
Honea Path	3,707	41
Williamston	3,991	41
Liberty	2,860	26
Central	1,550	24
		207
(Zone 3)		
McCormick	1,864	26
Edgefield	2,750	41
Saluda	2,442	30
Johnston	2,552	36
Calhoun Falls	2,234	24
Trenton	362	10
		167
(Zone 4)		
Landrum	1,859	36
Jonesville	1,447	18
Inman	1,661	26
Cowpens	2,109	54
Pacolet	1,418	25
		159
(Zone 5)		
Heath Springs	955	34
Clover	3,506	46
Blacksburg	1,977	44
York	5,081	52
Fort Mill	4,505	28
		204
(Zone 6)		
Fountain Inn	3,391	22
Laurens	10,298	80
Iva	1,114	22
Ninety Six	2,166	24
		148
	TOTAL	1,110

All these units were built in the conventional method. An additional 165 units were approved in January 1973: 75 units for Clover, and 30 each for Fountain Inn, Ware Shoals and Belton. Half the new units are supposed to be built under Turnkey I, a method that the authority has never used. However, because of the moratorium on federally subsidized housing programs, final approval has been deferred, and construction is now uncertain. Four applications for 300 units in four communities were submitted to HUD between 2 and 4 years ago, but these applications were also returned when the moratorium was announced.

How the Authority is Governed: The regional authority is governed by a 19-member board of commissioners. Eighteen of the members are selected by their respective county's State senator, and the 19th member, a commissioner-at-large, is selected by the other 18 members. All terms are staggered for 5 years each.

Board meetings are held either quarterly, if there is business to discuss, or on a special purpose basis. Commissioners frequently promote additional housing in their particular counties. They act as catalysts, because the authority staff will not go into an area unless it has been invited (to avoid the appearance of imposing housing on an unwilling community, but also because staff does not have the time to do housing promotion).

Housing Administration: South Carolina Regional Housing Authority No. I has a reputation for its economy and good service, due largely to its small but strategically placed staff. The region is divided into six "zones," each with its own resident zone manager, office, and maintenance warehouse. There are approximately 150 to 225 units under management in each zone, depending on the distance between projects. The two zones with the largest number of units both have an additional full-time maintenance employee to assist the zone manager.

A five member staff in Laurens coordinates the entire region's activities. This staff consists of the executive and assistant directors, an accountant, tenant selector, and stenographer. The central office and zone manager staffs total 11 employees, or one administrator for every 100 units under management, the exact ratio recommended by the South Carolina HUD area office. But, because the zone managers divide their time between administration and maintenance, the ratio is actually less favorable.

In addition to the zone managers who do minor maintenance repairs, there are seven other maintenance employees: two aides who are located in two of the zones, a maintenance supervisor, two maintenance mechanics, and two painters located at the authority warehouse in Laurens. If the zone managers are counted as part-time only, the ratio of maintenance employees to units is 1 to 110; a lower ratio than what HUD recommends (1 to 50) but, like the administrative staff, well placed.

The key to the authority's ability to operate in a large area is the zone manager. This person is responsible for all personal contacts with tenants—from taking applications to answering maintenance complaints, supervising move-outs, and reexamining incomes. For most purposes, the zone manager is the tenant's only link with the authority, although some tenants will call the central office if they are not satisfied with his service or he cannot be reached for an emergency repair. Most of the zone managers have long tenure in their jobs.

Applications and Rental of Units: Most applicant referrals are made by public housing tenants. A potential applicant usually obtains the zone manager's home or office telephone number from a tenant, but sometimes the local welfare department will call the zone manager regarding a family in need of housing. Publicity is not used because of few vacancies and a backlog of applications.

Zone managers maintain scheduled work hours in each of their projects every week. Applications are usually taken then and mailed to the central office each Friday. Office hours (in most of the smaller projects, the office is the zone manager's pickup truck) are also used to do maintenance repairs, take maintenance requests, and collect rent.

When an application is sent to the central office, the tenant selector figures the rent and then mails back the application to the zone, where it is filed according to location preference. When a unit becomes vacant, the zone manager selects the new tenant and prepares the lease. The tenant's application and lease are then returned to the central office for permanent filing. Employment and welfare income verifications, as well as income reexaminations, are all completed by the zone manager and sent to the central office for review and approval.

Rent Collection: During the first week of the month, office hours are used for door-to-door rent collection, with late rent pickup during the second week. Tenants who will not be home leave their rent checks with neighbors, or leave permission with the zone manager to enter their homes to pick up the rent checks. When some tenants pay at the zone offices, the zone manager will visit a tenant's home later in the month, primarily to check for repairs—a major purpose of door-to-door rent collection.

Both the zone managers and the authority's accountant keep a close watch on tenant accounts by maintaining records of every transaction and the amounts owed. This attention has apparently paid off, because there are few delinquencies (collection losses totalling only $300 last year) and about five evictions a year. Tenants who have rent paying problems will usually talk with the zone manager and sometimes will contact the executive director to work out an alternative rent-paying arrangement.

Maintenance: Routine maintenance is usually handled by the zone managers. Each has a pickup truck and keeps a variety of supplies at the zone office and warehouse. Most tenants wait until the zone manager is scheduled to be at their project before making maintenance requests. In emergencies, however, tenants can call the zone managers at their homes, the zone offices, central office, or warehouse. The central office has a list of telephone numbers of tenants in each project who can be called to relay messages to the zone managers.

Two zone managers have maintenance aides to assist them. The aides do routine maintenance work and occasionally will clean or paint an apartment, although most interior painting is done by the authority's painters in Laurens. Work that is not routine is handled by maintenance mechanics who work out of the central warehouse. These men do work that requires heavy equipment, including the attachment of sewer lines to new projects, or they clean apartments after families move out. They have a tractor for cutting grass and a truck with a trailer for transporting equipment.

In addition to this maintenance work, the maintenance mechanics are responsible for completing a yearly schedule of maintenance assignments. Each month they check most units for repair or replacement of specific items, as follows:

- January—fix inside doors and cabinets.
- February—prune shrubs and trees.
- March—fertilize all lawns and replace faucet washers.
- April—repair door and window screens.
- May—repair faucet washers, light switches and receptacles.
- June—repair ovens, door springs, bathroom accessories.
- July—repair refrigerators.
- August—(nothing scheduled).
- September—repair space heaters, hot water heaters, ranges.
- October—check windows and doors.
- November—replace faucet washers and packings.
- December—repair switches and receptacles.

An annual inspection of all authority units begins in mid-May. The executive director and his assistant visit each unit and recommend repairs to the maintenance supervisor and the zone managers. The annual inspection also provides tenants the opportunity to express their complaints to authority staff other than the zone managers and keeps the central office more alert to what is happening in the zones.

The maintenance supervisor is responsible for seeing that all maintenance work is done correctly and on schedule. He spends much of his time touring the projects and reporting daily to the central office to coordinate with the assistant executive director maintenance requests from the zone managers.

All supplies are purchased by the assistant director and stored in Laurens until requested by a zone manager. Either the assistant or a maintenance employee from Laurens will deliver supplies so that the zone managers do not have to leave their work areas.

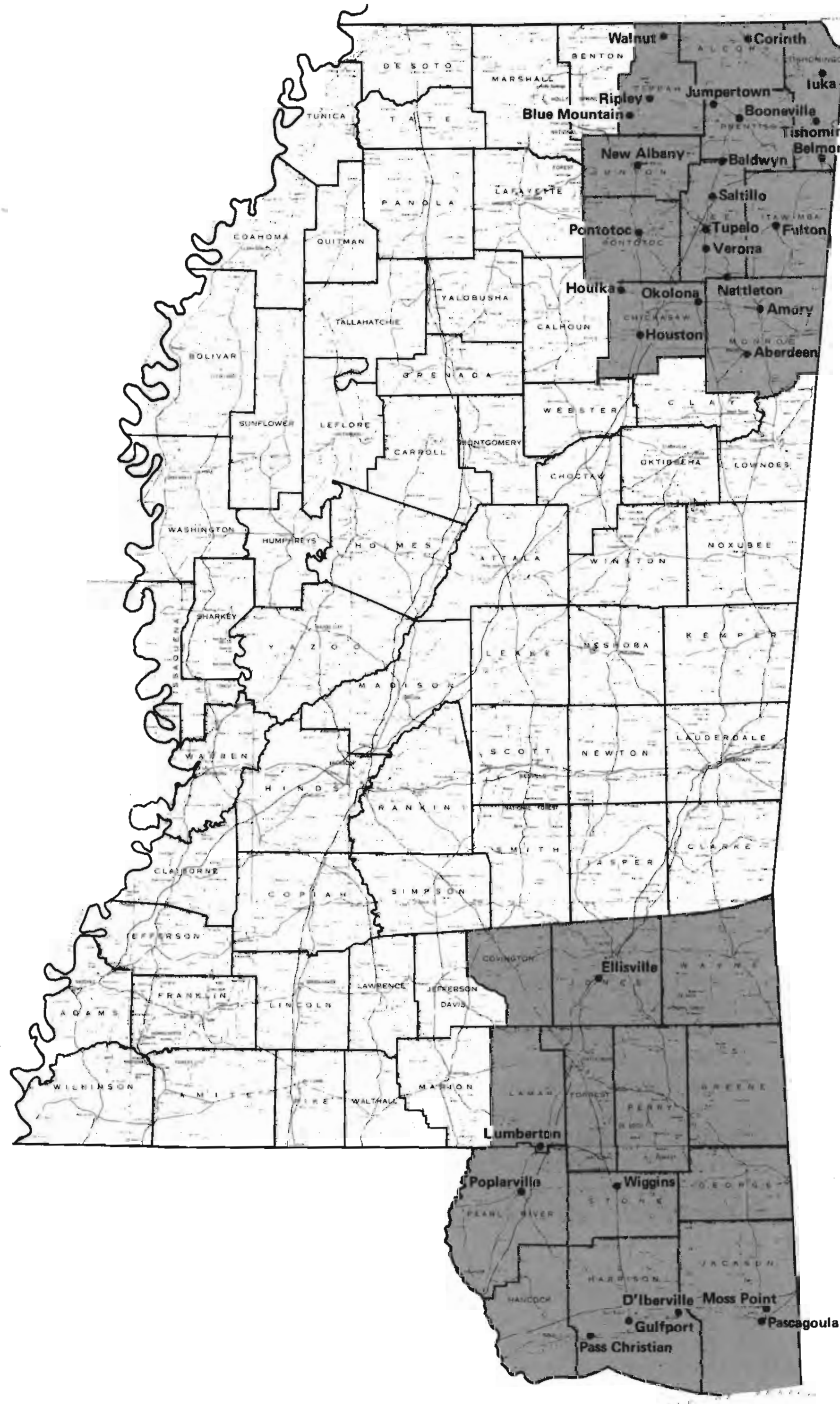
The authority's comprehensive maintenance program is immediately noticeable. Units that are 20 years old look as well kept as those built last year, with no peeling paint, torn screens, dead bushes, or other signs of deterioration. The authority and HUD estimate that there are substantial cost savings in a program of preventive maintenance. And, according to the authority, this also creates good tenant-management relations, with repairs handled promptly before they become irritating to the tenants.

Social Services and Tenant Relations: There is no organized social service program or tenant organization for residents of authority housing, although social service referrals are made by the zone managers who are regularly in contact with the tenants and local social service agencies. Zone managers' monthly visits to tenants serve three purposes: to collect rent; to inspect the unit and receive maintenance requests from the tenants; and to simply talk with the tenant. The third, to "sit and chat" whenever possible, helps to identify social, economic, and health needs of tenants.

Elderly tenants, and particularly those living in the northern part of the region where the Appalachian Regional Commission sponsors elderly programs, are recipients of more formal social services sponsored by agencies other than the authority. The elderly project in Laurens has a recreation room where tenants and other elderly people from the community hold classes, worship services, and social events. Family units in the region are not similarly equipped.

Case 2: Mississippi Regional Housing Authority No. VIII

Mississippi Regional Housing Authority No. VIII, located in Gulfport, Miss., provides a number of contrasts, in terms of management and maintenance operations, to the other regional au-


Walnut
Corinth
Iuka
Ripley
Jumpertown
Blue Mountain
Booneville
Tishomingo
Belmont
New Albany
Baldwyn
Saltillo
Pontotoc
Tupelo
Fulton
Verona
Houlka
Okolona
Nettleton
Amory
Houston
Aberdeen
Ellisville
Lumberton
Poplarville
Wiggins
D'Iberville
Moss Point
Gulfport
Pascagoula
Pass Christian

thorities described in this study. Unlike the South Carolina regional program, for example, most of No. VIII's services are centralized in two offices located in the more urbanized areas of the region where most of the authority's units are found. This centralization helps perpetuate the distinct "urban-rural" character of the authority. Service to the more urbanized areas is handled somewhat differently from service to the rural projects. As one might expect, there is a tendency to focus the most attention on the more accessible and populated areas—one that extends to national housing programs as well.

Authority Background: Established in 1944 under the Mississippi housing law permitting the creation of regional housing authorities, Mississippi Regional Housing Authority No. VIII provides low rent public housing throughout a 13-county jurisdiction in the southeastern portion of the State. Although its early history is obscure, resolutions establishing the authority were obtained from each of the 13 county governments as early as 1944. However, the authority remained dormant for years. The Harrison County Board of Supervisors rekindled interest in low rent housing when it enabled the county's purchasing agent to resurrect the authority. By 1958, a small staff was hired, three projects were completed, and several more were planned. Today, there are 1,302 authority units in a few of the region's larger cities, their rural outskirts, and a number of small rural towns.

The authority retains its original boundaries, outlined on the accompanying map, and, like some other regional housing authorities, its jurisdiction encompasses two fairly distinct geographic and economic areas. There is a relatively densely settled, three-county coastal area along the Gulf of Mexico that includes the cities of Gulfport, Biloxi, and Pascagoula. Employment in this coastal area is primarily in the fishing and tourist industries. Inland, there are sparsely populated areas, with Hattiesburg being the only city of more than 25,000 population in the 10-county rural area. Tree farming, the attendant paper industry, and garment manufacturing are the major sources of employment, and they generally pay lower wages than do the coastal industries.

Recognizing the coastal-rural disparity in incomes, the authority established separate income limits for admission and continued occupancy. A family of four seeking admission to a project in the small town of Wiggins may have a maximum income of $3,900, but a family of the same size applying to a coastal project may have as much as $5,000 income.

Eleven other local authorities in the region provide low rent housing for approximately 2,600 families and elderly persons. At least seven have approximately 100 or less units under management, and three of these are located in towns where the regional authority also has units. The regional authority developed its units in the three towns prior to the creation of the local authorities; their creation was largely a response to the devastation caused by Hurricane Camille. Gulfport, for example, created its own authority in order to operate an urban renewal program. Because No. VIII already had 100 units for the elderly in Gulfport, an agreement was signed allowing the regional authority to continue managing the elderly project but prohibiting it from further development within the city limits. (The regional authority currently operates an additional 560 units in the Gulfport area, but not within the city limits.)

None of the smaller local housing authorities in the region have been incorporated into the regional authority, although one authority has considered requesting this. Like Gulfport, this LHA was created after the regional authority had developed housing in the community where the LHA now has jurisdiction. But, with only 90 of its own units under management, the LHA is experiencing administrative problems and may ask the regional authority to manage the units on a contractual basis. The local authority would retain its own board of commissioners and annual contributions contract. This type of agreement contrasts sharply with the regional authority's current operation by requiring it to keep a separate set of books and to hold separate board meetings. Such arrangements could be burdensome.

The regional authority is indirectly affected by Mississippi's "antihousing" law, prohibiting the development of public housing without a local referendum. Though the authority has managed to avoid this obstacle, an attitude against low income housing does exist in the State. To avoid the appearance of attempting to force low income housing on a community, the authority does not promote its services but waits for a locality to take the initiative and inquire about the program. Thus, many of the small rural communities, desperately in need of housing but apathetic to that need, are unserved. However, the authority seems to protect itself from political conflicts.

The Authority's Program: Regional Authority No. VIII manages 1,302 units dispersed among 24 projects in nine locations. Fully 94 percent of these units are found in three coastal counties, and 78 percent are in or around the two cities of Gulfport and Pascagoula.

Location	Population	Units	Total Units Location
Gulfport	40,791	100	100
Gulfport Area		106	560
		124	
		200	
		80	
		50	
Pascagoula	27,264	152	350
		24	
		24	
		85	
		65	
Moss Point	19,321	60	132
		72	
D'Iberville	7,288	50	50
Poplarville	2,312	18	30
		12	
Pass Christian	2,979	14	28
		14	
Lumberton	2,084	12	20
		8	
Ellisville	4,643	10	16
		6	
Wiggins	2,995	10	16
		6	
TOTAL		1,302	

Two additional projects are nearing construction in small rural towns. Lucedale, with a population of 2,083, will receive its first 72 public housing units, and Poplarville, which already has 30 authority owned units, will receive an additional 40. These projects will spread more of the authority's units into rural areas, with the share in the three coastal counties dropping to approximately 68 percent.

The authority owns 1,202 of its units and leases the remaining 100 units for the elderly in the City of Gulfport. The authority rents all but 200 of its own units under the conventional public housing program; the remaining 200 are part of a single Turnkey III homeownership development—the first in the Nation—just outside of Gulfport.

How the Authority is Governed: A single board of commissioners governs the authority. There are 13 members, one from each county under the authority's jurisdiction. Each commissioner is selected by the board of supervisors in each county for a 5-year term, with all terms coinciding. Most board members are reappointed. A druggist, sheriff, assistant superintendent of education, insurance salesman, and carpenter, among others, are currently represented on the board. No county has appointed a public housing tenant as its representative.

Members of the board have improved communications between the authority and outlying communities by translating apparent needs for low income housing into specific requests for the authority to visit a community and to explain the public housing program.

Housing Administration: The authority has decentralized its administrative and maintenance staffs among two central offices and three suboffices located in the coastal county projects. The largest of the central offices is outside Gulfport, at a 156 unit housing project. The region's basic administrative staff—executive and assistant directors, accountant, tenant selector, and administrative assistant—work here with a staff of 12 maintenance employees serving 820 units. Management is provided for the 156 unit project, the elderly project in Gulfport, and all the rural projects (including D'Iberville, located in a coastal county, but which the authority terms "rural"). Two large projects in the Gulfport area have small management staffs onsite who report directly to the central office.

With no office in the rural counties, distance has been a problem. The projects in these counties are served by a Gulfport management aide who is required to return to the central office daily. Since the furthest outlying project is approximately 100 miles from Gulfport, a round trip can consume up to 4 hours of travel in an 8-hour work day.

A smaller central office is located in Pascagoula, 30 miles east of Gulfport on the coast. From this office, three full-time management specialists, a part-time management aide, and 10 maintenance employees serve 482 units in Pascagoula and Moss Point. Although the longest distance traveled by Pascagoula staff is 8 miles, this will change with the completion of the Lucedale project, 60 miles north of Pascagoula.

Overall, the ratio of full- and part-time administrative staff to units under management is approximately 1 to 100, a ratio acceptable to HUD. The maintenance staff, consisting of 22 employees, provides a ratio of 1 to 59, a slightly lower ratio than HUD prefers. But the overall ratio is somewhat misleading, since 10 of the maintenance employees serve only 482 units, or a ratio of 1 to 48, while another 12 employees serve 820 units, or one employee to every 68 units. This disparity affects the promptness of maintenance service in the areas served by the Gulfport office.

Applications and Rental of Units: All applications are kept in the central Gulfport office but filed according to the community in which the applicant currently lives or wishes to live. No residency requirements exist, but the authority assumes that families, particularly those employed, will not want to move from their communities.

In the coastal areas, applications, like rents, are taken at any of the authority's offices. Although there is a waiting list for most coastal projects, the authority occasionally contacts a local community action or welfare agency when applications are lacking for particular units.

In the rural areas, application taking is informal and normally done on the day scheduled each month for rent collection. A potential applicant may call the Gulfport office to arrange a meeting with the project manager, but, more often, an applicant merely asks rural tenants when the project manager will be in the area. In some small towns the project manager has established contacts with the mayor or welfare agency and will ask them for referrals when necessary. However, most applicants in the rural areas come to the authority through tenant referrals.

There is a maximum economy of staff time here, as the management person assigned to the rural projects performs all necessary functions, such as collecting rent, taking applications, and supervising move-ins, on one scheduled day each month. This serves to cut down on travel days.

Rent Collection: In the coastal areas, tenants will normally pay their rent at the nearest authority office. Rent is due on the first day of the month but can be paid up to the fifth working day. Frequently, if a project manager sees that a tenant has not paid at the beginning of the month, he will call or visit the tenant to determine if there are any problems and to prevent future delinquencies.

Rent collection in the rural areas is the responsibility of the rural project manager who visits tenants door-to-door on a specified day each month. If the tenant does not intend to be home, rent can be left with a neighbor or mailed to the Gulfport office within 5 days of the project manager's visit. Rent collection in the rural projects requires roughly 700 miles of travel, and the rural project manager is required to return to the central office daily. As previously mentioned, to compensate for the distances traveled, the project manager will use rent collection days for a number of purposes, including taking applications and supervising move-ins.

At one time, there were many rent delinquencies in the rural projects. Authority staff attributed the number of delinquencies to the fact that families knew staff could not afford to travel to the rural projects several times a month to seek payment. The authority has instituted a strict rent enforcement policy, and delinquencies have become less of a problem in all areas. Nevertheless, when delinquencies appear at the beginning of the month, the rural project manager has little opportunity to visit or call a rural tenant to determine if there are problems.

Rents are deposited daily in a number of coastal banks. At the end of each week, these banks send statements of all deposits to a computer center in Wisconsin that produces a monthly tenant account report based on the banks' accounts and the daily records sent by the authority's accounting department. The computer service costs approximately $800 per month and substitutes for an additional employee the authority would have to hire. However, the authority is not yet convinced that this is the most efficient way of handling its accounts, because checks and HUD financial statements are still processed in the central office.

Maintenance: Maintenance for all projects is handled through the central offices in Gulfport and Pascagoula, with the Gulfport office having responsibility for all of the rural projects. Each office has a maintenance supervisor, directly responsible to the assistant executive director, and its own maintenance crew. These crews report daily to their respective offices where work assignments are made. All equipment, vehicles, and materials are kept at the two offices. Maintenance materials are purchased by the Gulfport office in large moneysaving quantities or through a HUD-designated consolidated supply contractor.

A tenant with a maintenance complaint can pursue a number of alternative courses, depending upon whether he is located in a coastal or rural area. If he is a coastal tenant, he can either telephone or deliver his complaint personally to any of the authority's offices. If he is a rural tenant, and if the complaint is minor, he can wait until rent collection day to tell the project manager, or he can register his complaint with the tenant in his project whose telephone is partially subsidized by the authority and who, in turn, will relay the complaint to the Gulfport office. In an emergency, the tenant can telephone the central office collect.

Maintenance work assignments depend largely on the number and location of work orders received. For example, if a tenant in Ellisville, 100 miles north of the Gulfport office, needs repairs, he will usually have to wait until there are a sufficient number of other complaints in Ellisville to warrant the 3½ to 4 hours roundtrip. In case of an emergency in one of the rural projects, a local plumber or other skilled craftsman may be called to attend the problem if it will take too long for an authority crew to respond. This is rarely done however.

Obviously, it can take many days for enough complaints to accumulate at rural projects to initiate a visit by a maintenance crew, whereas routine maintenance complaints from coastal tenants are normally answered within a day. The Gulfport maintenance supervisor estimated that two of his men may visit Ellisville about 2 days per month. Ellisville is visited by authority personnel only about 3 days per month, including the rent collection trip.

Although the rural projects appear at a disadvantage in terms of prompt maintenance, they do enjoy more frequent inspections for maintenance problems than do the coastal projects. Yearly maintenance inspections are made of all units, but the rural units are casually inspected by the project manager when he collects rent each month. If he sees a major problem that the tenant has not reported, he will complete a work order. In this way, excessive damages caused by tenants, or other maintenance problems which might not be discovered until the tenants move out, are repaired much sooner.

The authority's 13-county jurisdiction does place some constraints on maintenance practices, particularly since HUD does not take into account the costs of long distance travel when determining maximum per unit per month (PUM) maintenance costs for a particular geographic area. Public housing authorities that cover great distances are allowed about the same maintenance PUM as authorities operating in one town only. Mississippi Regional Authority No. VIII would like to hire eight additional maintenance employees, but finds the PUM allocation prohibitive.

Social Services and Tenant Relations: The authority is not involved in a social service program. A "meals-on-wheels" program serves the elderly project in Gulfport, and Head Start rents the community building in the large Turnkey III project outside of Gulfport, but neither of these programs are authority inspired.

Tenant problems, other than those concerning maintenance, may be telephoned to any of the authority's offices, and the appropriate project manager will speak with and sometimes visit the tenants involved. In rural areas, however, tenant problems are handled by mail unless they can be dealt with on rent collection day. Project managers, especially on rural projects, normally do not make referrals to social service agencies.

Case 3. Tennessee Valley Regional Housing Authority

The Tennessee Valley Regional Housing Authority, located in Corinth, Miss., is unique among rural housing authorities, due mainly to its role as a "mortgage banker," and to the presence of its nonprofit arm, Community Development Inc. (CDI). Also, the leased homeownership program operated by TVRHA is locally designed, though similar to the HUD Turnkey IV program. Although the authority probably serves higher income families than most rural public housing authorities, it is described here because of its potential to serve lower income families and its aggressive use of Federal funds to generate both housing and water and sewer developments for families and the elderly living in rural Mississippi.

Authority Background: Tennessee Valley Regional Housing Authority (TVRHA) was incorporated in September 1942, but remained inactive until February 1969, when residents of Corinth, Miss., reactivated it.[10] In the late 1960's, urban renewal was underway in Corinth and low rent housing units were needed. The Corinth Housing Authority would not apply for the units, leaving the town leaders with the option to find another housing authority. They first attempted to create a county authority, but Mississippi law prohibits the formation of a county authority where a prior county authority has become part of a regional authority. Rather than try to dismantle the regional authority, Corinth town leaders decided instead to reactivate it. An allocation of 1,000 units was received in 1970; another 33 units were obtained soon after a tornado destroyed housing in Corinth's urban renewal area.

[10] Corinth is a large town for northeastern Mississippi, and is the focus of industrial growth for the area.

The type of housing program developed for TVRHA—basically a leased homeownership program, with units developed by the authority's nonprofit spinoff, using funds loaned by the authority—was the result of negotiations with policy-level HUD staff in Washington and the Atlanta regional office. Until recently, HUD operations staff have lacked knowledge of the program.

Community Development Inc. (CDI) was created by TVRHA as a Corinth-based, nonprofit housing development corporation. Its building operation has, however, taken it beyond TVRHA's jurisdiction, which extends to the 10 northeastern counties of Mississippi, as shown on the accompanying map for the previous case. CDI has crossed the northern boundary of the region to build in Tennessee. That building site is probably closer to Corinth than are the projects that TVRHA leases in the southern areas of the region, since a trip from the northern boundary where Corinth is located to the southern boundary of the region is 140 miles. To visit the entire region would probably take two days travel.

Only five towns in the region have more than 5,000 population; most have less than 1,000. Yet, their economies vary greatly, with some relying on factory employment and others on farming. Poverty and bad housing are evident everywhere. In the 10-county region, 29 percent of the population is below the poverty level, and 28 percent of the occupied housing is inadequate.

The response to the region's need for low income housing has been limited. Although nine other housing authorities operate in the region, all having built their units before TVRHA got started, these authorities account for only 650 units of conventional low rent housing. (When the regional authority was reactivated, an agreement was reached with the other authorities that TVRHA would only do leased housing, while the others would continue to produce conventional units.)

When TVRHA's units are added to the other 650, there appears to be a substantial dent in the need for low rent housing. But, as stated earlier, TVRHA is probably serving higher income families than other authorities. In fact, the authority estimates that most of its leased housing tenants could nearly qualify for section 235 homeownership financing.

The Authority's Program: In the original allocation of 1,000 units of leased homeownership units, each of the ten counties was supposed to receive 100 units. Land availability—and actual need—dictate a different distribution. The following chart shows the number of units currently allocated for each project, and the number that the authority is leasing from Community Development Inc.[11]

Town	Population	Units Allocated	Units Leased
Corinth	11,581	232	112
Houston	2,720	8	8
Okolona	3,002	25	25
Houlka	646	42	42
Fulton	2,899	78	49
Verona	1,877	46	0
Tupelo	20,471	10	10
Saltillo	836	81	0
Amory	7,236	14	14
Aberdeen	6,157	75	36
Nettleton	1,591	64	64
Pontotoc	3,453	60	31
Baldwyn	2,366	27	27
Booneville	5,895	20	20
Jumpertown	—	42	30
Blue Mountain	677	30	30
Walnut	458	22	22
Ripley	3,482	72	0
Iuka	2,389	42	42
Tishomingo	410	5	4
Belmont	968	12	12
New Albany	6,426	25	0
TOTAL		1,033	578

Nearly all the housing produced by CDI is either detached or townhouse style for single families, except for a 30-unit apartment complex in Corinth that was built for victims of a tornado. Some development is on scattered lots, but most is in subdivisions where housing for the leased homeownership tenants is mixed with housing financed under other Federal programs. Some also are developed with community facilities, such as a school or recreation area. There are design variations in each subdivision, and the housing is generally attractive and well-spaced.

When CDI began operating, it assembled its own construction crew and "stick-built" the houses. Overhead costs soon mounted, however, and CDI decided it would be more feasible to hire contractors to do the work. CDI is currently purchasing panel style houses that are assembled onsite by private contractors.

[11] Although 578 units were leased by TVRHA as of February 13, 1973, only 270 of those units were rented. The discrepancy is the result of TVRHA leasing units with no water and sewer hookup because the development of these facilities has been delayed.

Because this is not a typical public housing program, the following points may illustrate how TVRHA and CDI produce housing:

- The program is almost entirely leased homeownership (only the 30 apartments in Corinth are operated on a straight rental basis).
- All units are leased from the Community Development Inc. Funds for housing development are loaned to CDI by the authority. TVRHA obtains its money by selling long term notes and loans the money at 8 percent, lower than the interest rate on interim construction loans available on the private market. So far, TVRHA has loaned $11 million, but only $2 million have gone to CDI. The remaining amount was lent to other developers of low and moderate income housing who could not obtain financing on the private market. TVRHA is filling an institutional gap found in most rural areas by acting as a financier.
- TVRHA funds have also been used, on occasion, to pay a community's share of a Federal water and sewer grant. Without this assistance, financing of water and sewer development would have raised land costs to more than CDI could pay or TVRHA could afford to lease.
- TVRHA sells to FNMA the mortgages it receives as collateral from CDI (the Federal National Mortgage Association has committed itself to purchasing all TVRHA mortgages) and repays the long term notes.
- CDI then repays the loan through the rent payments it receives when TVRHA leases CDI units. These payments include the mortgage, taxes, and insurance.
- Until recently, CDI used TVRHA loans mostly to construct housing sold under various Federal programs other than public housing: 235, 236, and 221(d)3.[12] If a unit could not be sold, the agreement with TVRHA required the authority to lease the unit. HUD has recently required the authority to lease all 1033 units as expeditiously as possible.

The agreement between TVRHA and CDI, approved by HUD, has an unusual feature. When a unit is turned over to homeownership, the authority can lease an additional unit from CDI to replace the one lost, as long as the total number of units under lease does not exceed 1033. Obviously, this arrangement perpetuates the authority indefinitely, unlike the operation of a conventional leased homeownership program such as Turnkey IV.

Instead of signing a rental agreement when they are approved for a unit, authority tenants sign a "homeownership opportunity agreement" requiring them to assume the mortgage when their incomes reach a point at which alternate financing is available. Because the authority wants to turn over units in order to lease additional ones, it looks for applicants who seem to have a good chance of assuming homeownership. Therefore, all units are leased to families that have what the authority calls "income growth potential." Most are young, and few, perhaps 10 percent, receive welfare payments. Families with welfare incomes usually have some employment income as well.

The program is too young to reveal whether family incomes will actually rise sufficiently for homeownership. Currently, the average rent on authority leased units is $50 per month, with utility costs deducted from this amount. Houses sold by CDI under the 235 program have mortgages of between $80 and $125 per month, without utilities. The difference in average monthly payments between public housing and 235 would require a substantial income rise.

In addition to the 1,033 units currently allocated, HUD gave preliminary approval for two other projects (approval came before the moratorium, so the future of the projects is in question), 50 units of conventional housing for the elderly in Corinth, and a 100-unit intermediate care leased nursing home.

How the Authority is Governed: The county commissioners for each member county appoint a representative to the board of commissioners, and the 10 commissioners select an 11th member. All terms coincide and last 5 years.

Members of TVRHA's board of commissioners are, as one member described, persons who "understand" financing, well educated businessmen who grasp the authority's role as "mortgage banker." The board has taken an active role in both formulating the authority's housing program and, to some extent, carrying out the authority's daily operation, although this involvement is decreasing as staff gains experience.

CDI's board membership is similar to that of TVRHA; in fact, six of the 10 members on CDI's board are also on the board of TVRHA, although this situation is expected to change. All members are selected by county boards of supervisors.

[12] Farmers Home Administration (FmHA) has also approved 132 units of section 515 rural rental to be developed by CDI at six locations.

Housing Administration: In nearly all aspects of the authority's operation, the roles of TVRHA and CDI intermingle. Although each organization has its own staff, they work together. The authority employs four persons—an executive director, secretary, and two tenant selectors. All accounting work is contracted to CDI, which maintains its own computer service.

CDI's administrative staff is slightly larger, with an executive director, attorney, secretary, salesman, and a director of fiscal management who supervises three bookkeepers and two operators of the IBM computer system. CDI is able to support a computer operation by providing accounting services to many other organizations, including TVRHA, Corinth Urban Renewal Agency, Neighborhood Youth Corps, and some local government departments. Other administrative funds are borrowed from TVRHA but will not be repaid until CDI units are sold to the low income tenants. At that time, CDI will add about $1200 to the price of each house in order to repay the administrative loan.

Because some administrative staff serving the TVRHA leased units work for CDI, it is difficult to establish a ratio of administrative staff to units under management. However, there were only three maintenance employees serving 270 units, as of February 13. This ratio of one employee to every 90 units is much poorer than recommended by HUD.

Applications and Rental of Units: TVRHA employs two tenant selectors who take all applications, verify incomes and employment, decide on applicants, and prepare the homeownership agreement.

The housing program is well publicized through newspaper and radio announcements. Applicants are advised to meet the tenant selectors during their regularly scheduled office hours at each project. The hours are not providing adequate time for all the applicants, since interest in authority housing is high. On the same day applications are taken, the tenant selectors must also supervise move-ins and this, of course, limits the time for interviewing applicants.

When more units are leased, the tenant selectors intend to split the region in half, with one person covering the northern five counties and the other covering the southern five counties. Little time will be spent in the Corinth office, which is located near the northern border of the region near Tennessee. Currently, each tenant selector drives about 100 miles daily, and the authority pays them for mileage on their personal automobiles.

There is a backlog of applications for most units, although many of the applicants will prove ineligible, mostly due to "low incomes." Applications are filed according to the applicant's preferred location and his income growth potential. This latter tenant selection criterion is in accordance with the goals of the homeownership agreement, although it will deny participation in the program to many lower income families and the elderly.

An important feature of the TVRHA housing program is that selected applicants are counseled toward homeownership only. There is no mention of the traditional public housing rental program, although income limits are still approved under HUD and Brooke Amendment guidelines. From the day an applicant takes possession of the unit, he gains fee simple title to that unit with the understanding that eventually it should be his. Homeownership education is another responsibility of the tenant selectors.

Rent Collection: TVRHA and 18 banks in the region have signed agreements requiring the banks to receive tenant rental checks. Each tenant is issued a card identifying the authority's account, which is presented with the rent check to the local bank at the beginning of each month. The banks are expected to send daily statements to the CDI accounting department.

There are problems in this system. Delinquencies are high and the authority is thousands of dollars short on rent collections. With no field staff to encourage timely payments, many tenants fall behind. Bank personnel are not authorized to collect rents door-to-door, and the CDI accounting staff rarely becomes involved in delinquencies beyond writing a letter. CDI does notify the authority's secretary about all accounts paid, and she can transmit this information to the tenant selectors who may talk to the families when visiting the projects. Evictions are the responsibility of the authority, not CDI.

All rent transactions are recorded on an IBM computer system run by CDI. The accounting service costs the authority $1.00 per account per month; eventually, the costs will be $1,033 per month. This is less expensive than what it would cost the authority to hire an accountant and bookkeeper to service over 1,000 accounts.

Maintenance: The homeownership agreement requires tenants to perform their own routine maintenance. Part of the monthly rental is placed in a routine maintenance account and, when the tenant does not perform this maintenance, CDI's costs for labor and materials are subtracted from the account. An additional amount per month goes into a nonroutine maintenance account for major repairs, such as new roofing. According to TVRHA and CDI, most of the families have not done their routine maintenance. Consequently, the three-man maintenance staff employed by CDI is kept busy with numerous complaints called to the Corinth TVRHA office or given to the tenant selectors.

Maintenance employees report daily to the Corinth office for work assignments and often pick up additional work while traveling in their radio-dispatched trucks. But, because of the distances covered in the region and the limited availability of staff, repairs are sometimes delayed as long as 1 week. If a staff maintenance man cannot fix the problem, repairs are further delayed. Costs increase because a local plumber or electrician has to be called. When CDI maintenance men repair something, they use materials that are purchased in quantity at lower costs; in contrast, the local repairman will charge CDI both the full price for all materials and for labor.

Social Services and Tenant Relations: TVRHA is not a social service agency, although some informal referrals are made by the tenant selectors. However, there are no tenant organizations, nor are they encouraged. Tenants are expected to take care of their needs in the same way that an individual homeowner would. For a while, the authority contracted with a local junior college to provide counseling. The program has been discontinued, and the funds have not yet been channeled elsewhere.

Case 4. Vermont State Housing Authority

The Vermont State Housing Authority, located in Montpelier, Vt., was selected for the study because of its almost entirely rural program, and because it has produced a large enough number of units to illustrate the advantages and disadvantages of operating on the State level. Vermont's program is relatively young and limited, particularly when compared to the diverse program of the Hawaii State Housing Authority which operates in both rural and densely populated metropolitan areas. But while the Hawaii program has operated under favorable State legislation and funding, the Vermont program has not been so fortunate.

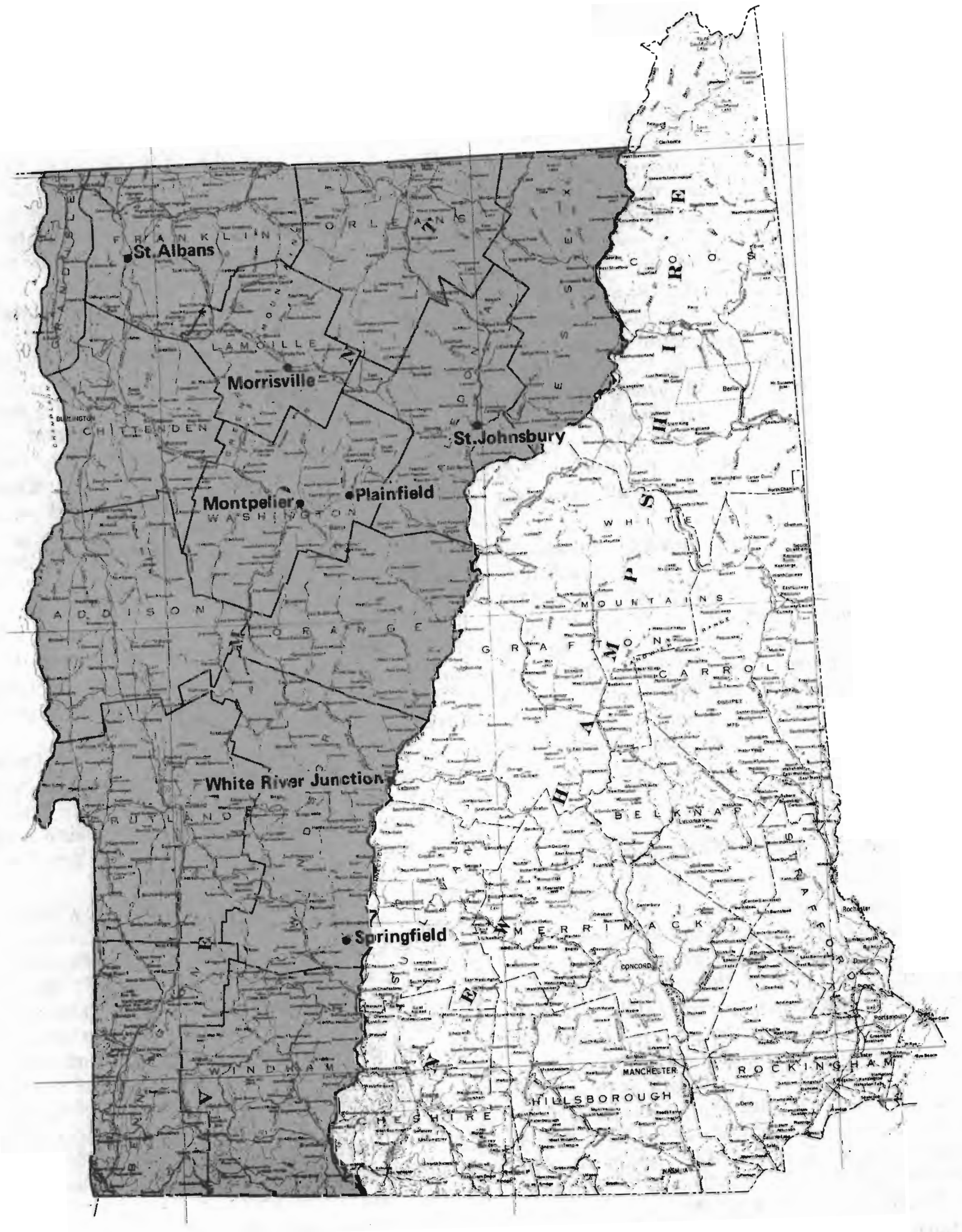
Authority Background: Among the last legislative accomplishments of Vermont's first Democratic Governor in 105 years was the creation, in 1968, of the Vermont State Housing Authority (VSHA). At that time only five housing authorities existed in the State, all in the larger cities and towns. The State authority was created to fill the low income housing gap in rural areas—nearly the entire State. Legislation prevents the authority from receiving funds for other than sections 10 and 23 leased housing units. The prohibition was required by a State legislator who feared the new authority would attempt to compete in towns where other authorities were already operating conventional public housing projects. However, there is speculation that the legislation also protects Vermont communities from what their citizens fear: public housing "projects."

Regardless of the intent of the legislation, there have been some problems. Three small LHA's (two with 60 units each, and one with 125) were established after the State program was created, largely in response to VSHA's inability to produce conventional, low rent elderly housing. According to the HUD area office, none of the small authorities is operating efficiently, and they have requested that VSHA assume management of their units. Some form of management agreement will, in fact, be the only feasible way for VSHA to rescue these authorities, since Vermont law prohibits the State authority from actually leasing additional units in a community once that community has created its own LHA (though VSHA can continue to operate the units it already has under lease in that community).

VSHA is further prohibited by law from receiving any State funds. Though loosely tied to the State's Department of Development and Community Affairs, the authority remains a separate agency solely dependent on the Federal Government for funding.

Given the constraints imposed by the State legislature, VSHA must fight a decidedly uphill battle to serve its constituency. Low income people living in bad housing are found in every village, town, and city in the State (there are no unincorporated areas). As long as a resolution can be obtained from the local government and no other housing authority is operating in the community, VSHA may lease housing there. Since there are only eight other housing authorities in the State providing only 1,500 low rent units, competition in the low income housing market is slim.

Few nonprofit organizations are providing low income housing, although VSHA is leasing some Farmers Home Administration 515 rental units in various locations. Other subsidized housing programs, such as HUD 235, 236, and 221(d)(3), account for only 1,100 committed or



St. Albans
Morrisville
St. Johnsbury
Montpelier
Plainfield
White River Junction
Springfield
FRANKLIN
ORLEANS
LAMOILLE
CHITTENDEN
WASHINGTON
ADDISON
ORANGE
RUTLAND
WINDHAM
WHITE
MOUNTAINS
GRAFTON
CARROL
BELKNAP
MERRIMACK
STRAFFORD
ROCKINGHAM
HILLSBOROUGH
CHESHIRE
CONCORD
MANCHESTER

completed units in the entire State. This production record is poor in relation to the need for low income housing. Twelve percent of the State's housing is inadequate, according to the 1970 Census of Housing, and 12 percent of the population is below the poverty level.

As can be expected, incomes tend to be slightly higher in the larger towns served by VSHA. Yet, regardless of the income differences, the authority has established only one set of income limits, and, with HUD's consent, these correspond with the limits for Burlington, Vermont's largest city.

The Authority's Program: Vermont State Housing Authority has 780 units under lease in 48 villages, towns, and cities in the State. Most locations have only one to six units, although some larger developments do exist, as follows:

	Location	Units
(New Construction)	Montpelier	36
	Morrisville	20
	Plainfield	16
	St. Albans	20
	St. Johnsbury	36
	White River Jct.	36
(Existing-Rehab.)	Springfield	104

Forty more units are being constructed in St. Albans for the elderly, thus completing HUD's allocation of 820 units to the leased rental program.

An additional 150 units of "cooperative" housing have been set aside for the authority as an Operation Breakthrough demonstration, to be financed under the Turnkey IV program and developed by a nonprofit organization. Although the housing will be located on approximately nine scattered sites, management will be centralized, and a mobile maintenance team will be available to all sites. Tenants can build equity in their homes and eventually assume leadership in the cooperative. VSHA would have preferred to obtain the 150 units under the regular leasing program, but only the Operation Breakthrough units were available. The result will be income limits higher than for the regular leasing program.

VSHA's units are dispersed in numerous small communities in the northern part of the State, but in southern Vermont there are more housing clusters. The location of leased units is determined by where families need housing and where housing can be obtained. Even if there is only one eligible applicant for housing in a particular community, the authority will attempt to find housing there, regardless of how rural or isolated the area is, as long as the housing is decent, meets HUD standards, and is economical.

In this way, VSHA has made excellent use of the leased housing program. It has been aided to a large extent by Vermont's supply of large old houses that are still in decent condition. The supply is diminishing, however, and more new construction will be necessary. Recently, many of the older units offered for lease have been structures ready for condemnation.

Although leasing has been a workable program for nonelderly low income families in Vermont (76 percent of VSHA's units are rented by such families), the elderly have not fared as well under this program. HUD will only allow the authority to pay a maximum of $100 per month for a one-bedroom unit. Since Vermont is a high cost State, a decent unit for that price is nearly impossible to find. Consequently, the authority has had limited service to the elderly. In contrast, other housing authorities in the State, all operating under the conventional program, rent two-thirds of their units to the elderly.

Finding Units to Lease: Finding suitable rental units was an enormous task for VSHA when it first began, but publicity helped. Before the authority had administrative funds to hire staff, newspaper articles appeared in many towns explaining the purpose of the program and advertising for suitable rental units. Once administrative funds were obtained, field staff began personally hunting for units. Enough interest has been generated that, now, most owners (or housing developers) come to the authority on their own. The staff does little searching unless there is an acute or emergency need for housing in a particular area; then, they rely on local real estate people and officials who quickly identify potential rental units.

When an emergency situation does not exist, the authority finds units to lease in the following ways:

1. Existing Housing—An owner will contact the central office, either by telephone or letter, offering a unit (or units) for lease. A field representative is sent to inspect the property and, if it looks acceptable or needs some work to bring it up to standard, will tell the landlord to obtain a resolution from the local community giving the authority approval to lease there. This arrangement has worked well. If the owner needs help explaining the resolution, the authority will as-

sist, but, generally, staff time is freed from this activity.

The field representative then completes a "Dwelling Unit Report" describing the unit and what work needs to be done, takes pictures of the unit, contacts the fire marshal, and asks the owner to set a price and the preferred lease tenure, which may be negotiated. If the unit appears in standard condition, has a reasonable price, and is needed in the community—based on applications on hand or on talks with local welfare and other agencies to determine the local low income housing need—the staff will recommend the unit to its board of commissioners. With the board's approval, a lease is drawn up; or, if rehabilitation is needed, the authority will give the owner a conditional commitment to lease the unit when certain work is completed. All units are reinspected before the lease is signed.

2. New Construction—The process leading to the signing of a lease for newly constructed units is similar to the process for existing housing. The developer can approach the authority with plot and floor plans, certified by an architect or engineer, and the projected costs. These are reviewed by the executive director before being recommended to the board. A conditional leasing commitment is issued to developers whose proposals are approved. To monitor the construction, the authority relies on local inspectors, where they are available, and requires periodic inspections by licensed architects or engineers. HUD's inspections have been sporadic, at best.

How the Authority is Governed: The authority is governed by a five member board of commissioners appointed by the Governor for staggered 5-year terms. Though not intentional, the current board represents geographically diverse regions; yet, three of the commissioners come from towns in which the State authority cannot operate because each has its own housing authority.

The board is involved in the approval of every unit that the authority puts under lease. Although approval power is not delegated in the by-laws, the board has developed this control and wants to keep it. Leasing of a needed unit is sometimes held up until the board has its monthly meeting, although units recommended by the staff are rarely rejected. Meetings are cancelled if there is no business because most of the board members drive hundreds of miles to attend the meetings.

Housing Administration: Vermont's statewide housing program is administered from a central office located in the State's capital, Montpelier. There is one small office in the 104-unit project in Springfield where an authority field representative holds office hours, and another field representative operates out of his home in the southwestern part of the State. With 11 administrative employees, VSHA meets the ratio of one staff person to every 90 units under management recommended by the HUD area office.

For administrative purposes, VSHA has designated three geographic areas: the entire northern area of the State is covered by one field representative out of Montpelier; the southern area is divided vertically and covered by two field representatives. A tenant selector trainee in the central office is beginning to assist the northern field representative whose territory now includes over 400 scattered site units and requires about 130 miles of daily travel, at least 4 days a week. An additional field representative position has been requested to divide the northern area, but HUD has refused on budgetary grounds.

The southern areas require far less travel time because the housing tends to be more clustered and the field representatives live closer to the units. Still, all the field representatives are on the road much of the time, using their homes and cars as offices, and reporting daily by telephone to the field supervisor for instructions. Each Monday they all report to Montpelier for a staff meeting. Their responsibilities are extensive. Each representative is a jack-of-all-trades, taking applications, looking for housing units to lease, supervising move-ins and move-outs, handling tenant or landlord complaints, referring tenants to social service agencies, and dealing with all other needs.

Applications and Rental of Units: Vermont State Housing Authority has widely advertised its presence. Consequently, potential applicants call the Montpelier office from all parts of the State or obtain the local field representative's telephone number from a leased housing tenant. If a call is received at the central office, the tenant selector will either mail an application or ask the field representative to interview the applicant. In some instances, a local welfare or Operation Mainstream organization has been asked to interview an applicant. The authority works closely with these agencies and others to find both tenants and suitable housing.

All applications, except those for Springfield, are kept at the central office where they are filed chronologically and according to location. The authority rents units on a first-come first-served basis, unless an emergency exists. Preference is given to current residents of the town in which a vacancy occurs.

Vacancies are low and easily filled, since there is a backlog of applications in most communities. VSHA applied for 400 more leasing units to reduce the backlog but, according to HUD, the application was "lost."

Like most rural authorities, VSHA experiences little vandalism, even when units have been vacated. Unannounced move-outs rarely occur, so landlords can usually plan ahead for any needed rehabilitation on a unit for the next tenant.

Rent Collection: Leased unit owners are responsible for collecting rents the beginning of each month. The authority supplies prenumbered receipt books, and the owner is expected to mail all the receipts to the Montpelier office by the fifth day of the month. Some tenants will mail in their checks, particularly if the owner lives out of State, and tenants of the 104-unit Springfield project pay their rent to the field representative in that area.

The authority's intention in requiring owners to collect rents personally was to ensure monthly inspections for repairs or excessive damage, but problems have developed under this system. Since the authority mails to each owner a full lease payment on the first of the month, some owners become careless about collecting the rents to reimburse the authority for its administrative costs.

One result of this system has been a 20 percent monthly delinquency rate. Some owners simply do not pressure tenants to pay their rent, and the authority's small field staff has little opportunity to visit each delinquent tenant—or irresponsible owner.

Maintenance: Maintenance repairs are the responsibility of the owners. Tenants are supposed to call the owner—or in some of the larger projects, the onsite maintenance employee—when something needs repair, although some tenants prefer to call the authority first. If an owner does not respond to a maintenance request, the authority may order the item repaired and deduct the cost from the owner's lease payment. Excessive damage repairs are billed to tenants, and the authority often gets involved in ordering this nonroutine repair work.

The Springfield units, although privately owned, are managed and maintained by a full-time maintenance employee hired by VSHA. This arrangement has meant a higher standard of maintenance for these units than for the scattered site units. The authority has found that when there are enough units to warrant a full-time maintenance employee, tenant complaints are handled promptly. In addition, preventive maintenance is practiced. This is in contrast to the often erratic maintenance on the scattered site units.

Many of Vermont's small towns have only one skilled plumber or electrician. If an owner calls the town's plumber to fix something at a leased unit, and the plumber is working somewhere else, the tenant's problem either has to wait several days or the owner has to pay the high price of bringing a plumber from 30 miles distant. As a general rule, the tenant waits.

The authority would like to hire its own maintenance team which could be dispatched to any unit at the request of an owner. The team would sell its service to the owner, possibly becoming self-supporting, and would ensure that tenant complaints are answered before the problems become excessive and costly.

Social Services and Tenant Relations: Although the field representatives make some social service referrals, the authority has wanted a social service program since 1970. Budget limitations have prevented the authority from hiring a full-time social services coordinator who would identify tenant problems and develop referral contacts with appropriate agencies throughout the State. Instead, a small social service component may be possible under the HEW/HUD agreement. This arrangement would, however, only allow the authority to focus on "crisis intervention" rather than prevention.

Supplementing VSHA's current and planned social service efforts are three tenant organizations located in Montpelier, Springfield, and St. Johnsbury; all are large towns for Vermont. The authority encouraged the development of these organizations but has found that they lack leadership. Thus far, their major activities have been social, but they are being encouraged to participate more in board of commissioners' meetings.

Unlike the other regional authorities studied—and probably most rural authorities—Vermont State Housing Authority has a detailed grievance procedure. It provides for a grievance panel that includes tenants as well as authority officials. Although the procedure has not yet been used, there is a case developing which should test its effectiveness.

Case 5. Housing Authority of the City of Americus, Georgia

The title, Housing Authority of the City of Americus, Ga., is misleading, because it is the designated authority for four towns in the area and manages units for three other housing authorities. This extensive program is made possible through a "cooperative management agreement," described in the introduction to this study as the tool most widely used to consolidate housing efforts. As an example of a cooperative agreement authority, Americus is among the best known in the southeast, where cooperative housing efforts have often been used in rural areas.

Authority Background: The Housing Authority of the City of Americus was established in 1946 but was inactive for a number of years. A town leader revitalized it, and program reservations were obtained for 150 units. In March 1950, the authority's first and current executive director was hired, and the events that followed have their niche in the history of consolidated housing efforts. Soon after the executive director's appointment, HUD's predecessor agency, the Public Housing Administration, decided that his position should be part-time, considering the authority's small number of units under management. To prevent the loss of full-time administration, the executive director approached leaders in the nearby small towns of Andersonville, Plains, and Leslie about their housing needs. Each of the towns wanted housing but not the responsibility of running a housing authority. Consequently, they were able to reach an agreement with the Americus authority enabling it to act on their behalf in the development and management of low rent housing. These towns do not operate their own LHA's, but have formed a "consolidated," or multimunicipal authority with the town of Americus.

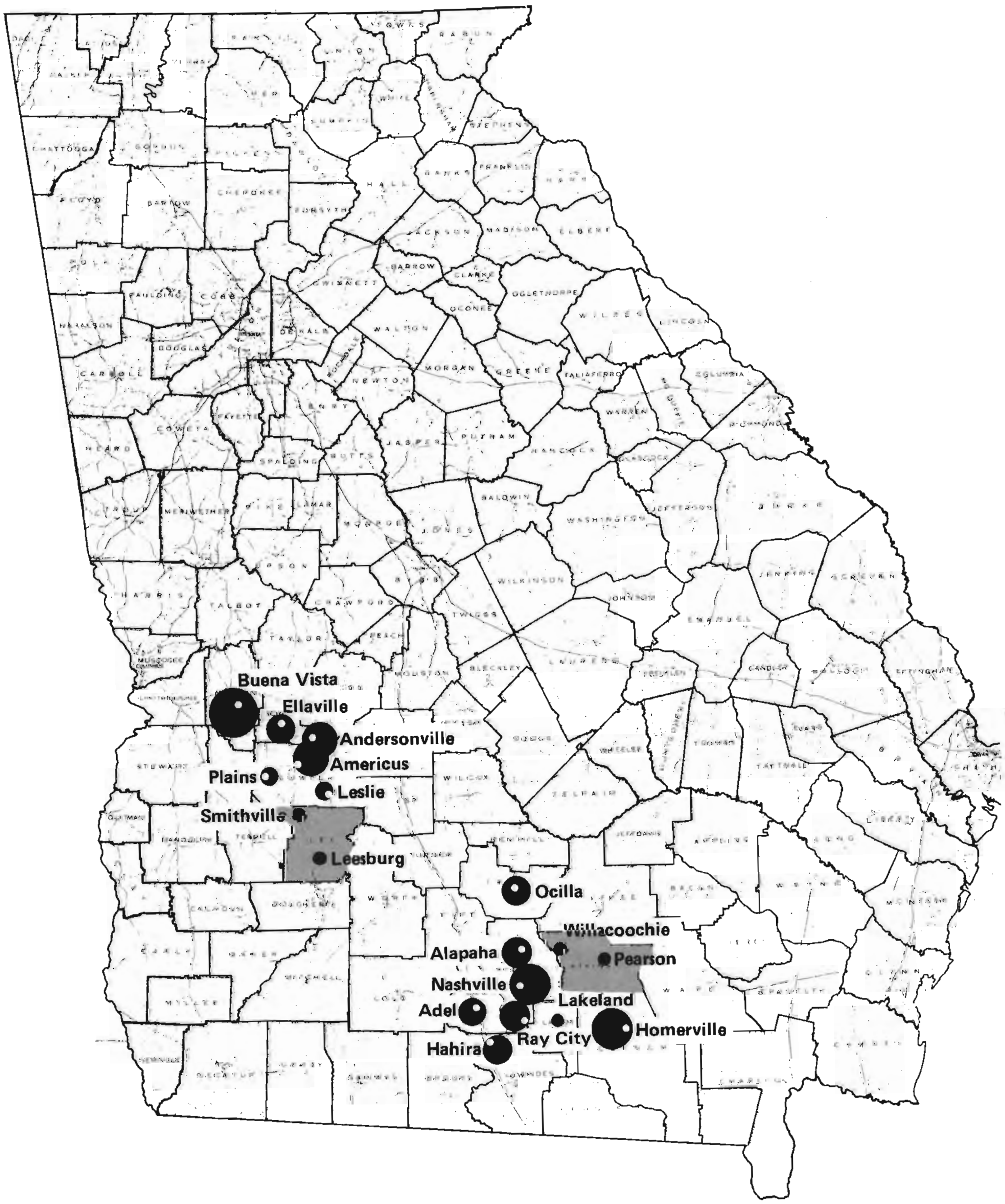
In the late 1950's and early 1960's, the Americus authority director also became executive director of three other housing authorities, Buena Vista (which had not built anything since its formation), Ellaville (which the Americus director helped form), and Lee County (which had projects in two small towns). At the time that Americus assumed management of the Lee County authority, the part-time executive director there was receiving only $50 per month for his services. The books were poorly kept, and maintenance was poor and sporadic. It took an Americus maintenance crew 2 months to bring Lee County units up to decent condition. Once they were, utility bills dropped (defective heaters had not been repaired in 2 years), and the Lee County authority was able to break even.

Buena Vista, Ellaville, and Lee County authorities signed a cooperative agreement with Americus, giving it management and maintenance responsibilities. Each of the authorities does, however, retain its own board of commissioners and annual contributions contract. (This type of arrangement was all that was feasible at the time under Georgia State law, though regional authorities are now possible.)

By joining a cooperative agreement, each of the smaller authorities have remained solvent. According to the Americus accountant, this would not be the case if any of them suddenly had to operate on their own. In contrast, the Americus authority now has enough units, with a total of 390, to be self-sustaining. And, it has an additional function: it is the urban renewal agency for the City of Americus. In this capacity, it has purchased numerous tracts of land, developed land use plans, made land available for recreational facilities and school expansion, and sold lots for the development of 235 and 236 housing and individually developed homes, in addition to building public housing where slums once existed.

The role of the Americus authority as housing manager for numerous small towns was logical. Americus is the largest rural town (with a population of over 16,000) in its southwestern area of Georgia and is central to the four-county region where it now manages units, as shown on the accompanying map. It is also the focal point for the area's industrial growth. As the mobile home capital of the South, it provides employment for people who can no longer find work in the dying agricultural towns surrounding Americus. These small towns, including those served by the authority, are within easy commuting distance of Americus. The furthest distance staff must travel is about 30 miles, although most of the towns the authority serves are within a 12 mile radius.

Employment opportunities have grown in the Americus area, although poverty and bad housing are still prevalent. In the general four-county area served by the Americus authority, 32 percent of the population is below the poverty level, and 51 percent of the occupied housing is inadequate. This level of poverty may account for the


Buena Vista
Ellaville
Andersonville
Americus
Plains
Leslie
Smithville
Leesburg
Ocilla
Willacoochie
Alapaha
Pearson
Nashville
Lakeland
Adel
Homerville
Ray City
Hahira

fact that more than half the families and the elderly living in units managed by the Americus authority are on welfare or social security. Average tenant income is about $3,000.

The Authority's Program: The Americus authority manages 25 projects totaling 610 units in eight locations, as follows:

Location	Population	Units	Total Units at Location
Americus	16,090	50	390
		100	
		50	
		40	
		70	
		30	
		50	
Andersonville	274	5	10
		5	
Plains	683	10	36
		14	
		12	
Leslie	562	10	22
		12	
Buena Vista	1,486	14	74
		18	
		12	
		30	
Ellaville	1,391	10	20
		10	
(Lee County)	(7,044)		
Leesburg	996	16	38
		10	
		12	
Smithville	713	14	20
		6	
	TOTAL	610	610

Of these units, 568 were built by conventional method. Another 50 units of conventional public housing are ready for construction in the Americus urban renewal area, and 32 units of Turnkey I housing are planned for the town of Leesburg. The authority also leases 43 units but has found that the quality is poorer than the conventional units and, consequently, require more repair work.

An additional 150–200 units have been estimated as the minimum need for low rent housing in the Americus area: 100 units for Americus, 50 for Ellaville (a prior application for units was not approved by HUD), and more for Leesburg in Lee County. In these towns, no alternative supply of decent low income housing is available. Units similar to public housing in Americus, for example, rent for $75 per month, or $30 more than the average public housing unit.

Unlike Americus, which has a large number of occupied shacks, the low rent housing needs of Andersonville, Plains, and Leslie have probably been met. With farm mechanization, the populations of these towns have decreased, and the need for low rent housing is minimal.

How the Authority is Governed: Each of the four authorities that cooperate with Americus has its own board of commissioners, with five members on each board appointed by a mayor or, in the case of Lee County, the county commissioners, for 5-year staggered terms. Andersonville, Plains, and Leslie, the three towns that have designated the Americus authority to act in their behalf, do not have their own representatives on the Americus board.

These separate boards apparently satisfy the desire of the smaller communities to retain some degree of local control and, according to the executive director, these boards free the already busy Americus board from having to undertake the low rent housing problems of other towns. Meetings of each board are scheduled annually and for special purposes. Most of the board members are bankers and businessmen who prefer not to meet more often than necessary.

Housing Administration: The authority's housing program is entirely administered from the central office in Americus and a small office serving three projects on the north side of town. One employee in the smaller office collects rent and takes tenant complaints. The remaining eight administrative and 12 maintenance employees work out of the large central office.

With 610 dispersed housing units, the authority maintains a high ratio of administrative staff to units under management, at 1 to 76. The ratio of maintenance staff to units is exactly at the level recommended by HUD, 1 to 50.

All employees are full-time, and their salaries are prorated among the authorities according to the number of units each has under management. Before the prorata formula is applied, the Americus urban renewal program is charged 20 percent of the executive director's salary and 10 percent of the accountant's salary, thereby lowering the administrative cost burden of the housing authorities. The urban renewal program employs its own staff of three; they occupy Americus office space and use Americus supplies. In return, urban renewal pays the authority 15 percent of all its overhead costs.

Applications and Rental of Units: The Americus authority is well known in the area through publicity efforts and word-of-mouth referrals.

Most applicants, including those in the outlying areas, will inquire at the central office, either by telephone or in person. The authority has made it known that applicants can call collect.

If an inquiry is made by someone who does not live nearby, the tenant selector will make an appointment to bring the application to the caller's home or job. Applications are kept in the central office and filed by location preference and time of submission. There are few vacancies, particularly during the winter months, and enough applications are on hand to fill units for many years—an indication of the substantial need for more units in a number of towns.

Rent Collection: On the first working day of each month, the authority sends three maintenance men door-to-door to collect rents at all projects outside Americus. Tenants living in Americus pay their rent either at the office or by mail.

Ellaville, Buena Vista, and Lee County authorities are charged a small fee—the maximum is $6 to the furthest town, Ellaville, and the minimum is $3 to closer towns such as Smithville in Lee County—for the use of the maintenance trucks on rent collection day. They also pay a proration of the maintenance men's salaries according to how much time they spend collecting rent. Because of the fee system, the maintenance men try to use rent collection day to accomplish other duties, such as taking work orders or reading gas meters.

If a tenant is not home on collection day, rent can be left with a neighbor or a money order can be mailed to the central office. After the fifth of the month, chronically delinquent tenants are mailed a letter informing them that eviction proceedings will begin. There are few evictions, however, and tenants with legitimate rent paying problems usually call the central office to discuss their difficulties with the executive director. In the future, the social services director will handle these problems. Delinquencies may run 15 percent to 20 percent per month, but collection losses at the end of the year are minor.

Rents are deposited in local banks on the day the maintenance men collect them. At the end of every month, each authority is charged for its expenses during the prior month. A check is drawn from each authority's bank account and deposited in an unlimited revolving fund to pay the following month's expenses. The fund is reimbursed monthly so Americus is not required to pay all the bills itself and wait to be repaid later. Last year, the authority began experimenting with the use of a computer for handling accounts receivable. Since 1,000 accounts were required to purchase the service, Americus formed a cluster with a number of small LHA's in Georgia. Every month, the other authorities mail their receipts to Americus where they are put in one envelope and sent to Atlanta for processing. It is too early to tell how useful the system will be.

Maintenance: All 12 of the authority's maintenance employees work out of the central office, reporting there daily for assignments. To expedite maintenance service, the authority owns three vans, each fully equipped with materials and tools, two pickup trucks, and a truck-trailer for the movement of heavy equipment. Since all trucks and equipment are stored at the central office warehouse, time is spent daily in transporting the equipment to work sites. The furthest site is less than an hour's drive, however, and maintenance employees going to that site are expected to leave earlier in the morning than the prescribed work hour.

Most requests for maintenance services are telephoned to the central office, where a work order is completed and put in an assignment box for that project. Maintenance requests from Americus tenants are often answered on the same day, since maintenance employees working there can easily be reached for new assignments. But, in the outlying areas, routine calls may take a day or two for service. The length of delay depends on the number of calls that come from a particular area.

The maintenance supervisor knows where every maintenance employee is daily. If an employee needs to be reached, the maintenance supervisor will call a tenant in the project where the employee is working (a list of telephone numbers of tenants who are usually home is kept in the office) and relay a message. The maintenance supervisor considered using two-way radios, but felt they were costly and impractical.

All materials are bought through a consolidated supply contract, except some small items purchased at a local wholesale house.[13]

Agreements with warranty dealers allow the authority to do its own warranty service. All refrigerators and stoves are repaired by the maintenance supervisor, and all repair work on authority equipment, such as trucks, is done by

[13] Public housing authorities may take advantage of HUD's yearly contracts with suppliers to purchase items at low prices.

maintenance employees. Having skilled workmen on the staff lowers the authority's maintenance costs. And, according to the maintenance supervisor, repair and rehabilitation work has been kept to a minimum because of the sound construction of the units.

Routine and emergency maintenance repairs are supplemented by a comprehensive preventive maintenance program. Detailed records on all units have been kept since the current maintenance supervisor was hired about 16 years ago. Each unit is inspected every 6 to 8 months, and the maintenance employee makes repairs during his inspection. If painting is needed, he writes an order for the work. The preventive maintenance checks are performed when routine maintenance assignment boxes are relatively free and after the tenant has been informed of the inspection. Each inspection takes from 1 to 3 hours and helps keep units from becoming run down.

Social Services and Tenant Relations: When the Housing Authority of the City of Americus applied for modernization funds in 1972, one of HUD's requirements was that tenants participate in developing the modernization plans. As a result of this participation, two tenant organizations, each having met three or four times, are ready to write their by-laws and elect officers. The authority has encouraged the growth of these organizations and has invited each to send a representative to the board of commissioners' meetings.

Elderly tenants in Americus have their own social and educational organization. Classes are held weekly in a well equipped recreation room located at one elderly project; all types of crafts are taught by volunteers and by the authority's social services director. Elderly and other tenant organizations do not exist in the other towns managed by the Americus authority.

Another result of the modernization application was the recommendation that a social services director be hired. In January 1973, the new director began visiting every tenant, contacting social services agencies in each county, and working with the elderly group in Americus. The social services director answers tenant complaints, other than maintenance requests, and tries to resolve rent delinquencies.

Thus far, tenants in Americus and the nearby towns have received the most attention, mainly because the small amount of funds the authority could reserve for social services limits the director's ability to travel to the outlying towns. Whereas the director is paid a monthly fee for the use of her car in Americus, Andersonville, Plains, and Leslie, she has to be reimbursed 10 cents per mile for travel to the outlying towns, some 30 miles away.

Case 6. Housing Authority of the City of Nashville, Georgia

Since the operation of the Housing Authority of the City of Nashville is similar to that of the Housing Authority of the City of Americus, Ga., this description will only highlight the operation and point out differences with Americus that *may* be useful to the reader.

Authority Background: The Housing Authority of the City of Nashville, Ga., was organized during the period 1948 to 1951, along with seven other small authorities (one being a county authority) within a 40 mile radius of Nashville. All the authorities were organized by the current executive director but managed and maintained separately, with each authority employing the executive director on a part-time basis. By 1958, the authorities consolidated under one cooperative management and maintenance agreement but retained their own boards of commissioners and annual contributions contracts. Earlier, in 1953, the small towns of Ray City and Alapaha, in the same county as Nashville, signed an agreement with the Nashville authority requiring it to act as their housing authority. In effect, these towns formed a "consolidated" housing authority, with one board of commissioners and one annual contributions contract.

The reason for the eight authorities signing a cooperative agreement typifies the plight of small authorities. Each authority had insufficient units to be solvent on its own. The smallest authority had only 16 units, while the largest, Nashville, had 85. With consolidation, all salaries, materials, and overhead were prorated among the authorities, according to the number of units each owned, thus lessening the burden on any one program.

The Nashville authority operates units in nine towns and one unincorporated area, located in seven counties of south central Georgia, as shown on the accompanying map for the previous case. Nashville is near the center of the area; the furthest site from there is Ocilla, 40 miles and about an hour's drive on narrow county roads. In many of the towns (most with populations between 600 and 3,000, except for Adel, with slightly more than 4,900), the authority feels it has saturated the low income housing market and, in fact, no units have been built in most of them in 17 years, or before the cooperation agreement. These towns have for a long times housed military personnel, but many of these people left as installations closed. There are still some agricultural and forestry employment and a few manufacturing plants, but, for the most part, the area is financially depressed.

Agricultural employment accounts, in part, for the high public housing turnover rate in some towns, usually beginning in the early spring. Many local farmers will supply housing free to agricultural workers during the spring and summer months. Although much of the housing is substandard, many families prefer to move out of public housing for those months to take advantage of the free rent. Some projects experience a 100 percent turnover each year, primarily due to this agricultural exodus.

Elderly persons are gradually becoming the largest percentage of the authority's tenants, and at least 40 percent of all the tenants are on welfare or social security.

The Authority's Program: Nashville manages 438 units in the following 10 locations:

Location	Population	Units
Nashville	4,323	126
Alapaha	633	18
Ray City	617	12
Hahira	1,326	16
Lakeland	2,569	20
Homerville	3,025	80
Pearson	1,700	20
Willacoochie	1,120	20
Ocilla	3,185	70
Adel	4,972	56
	TOTAL	438

Thirty units were leased in Nashville in 1968, but the other units were built in the conventional method. No units are under construction or application, nor were any in the planning stage before the moratorium. During the mid-1960's, the authority also operated an urban renewal program for the City of Nashville.

How the Authority is Governed: Each authority has its own board of commissioners that meets once a year, or for special purposes. The cooperative agreement enables the Nashville authority to act, when necessary, as an executive committee for the other authorities.

Housing Administration: The Nashville administrative staff is composed of three persons: the executive director, accountant, and administrative assistant. The ratio of staff to units, 1 to 146, is far poorer than HUD recommends. There is a better ratio of staff to units in the maintenance department. With eight employees, the authority has one maintenance employee to every 54 units, only slightly greater than the ratio suggested by HUD.

All employees operate out of the central office in Nashville, although the administrative assistant maintains office hours in the other towns, usually for a half day each week. At the small project offices, application forms, leases, and rent receipts are kept. Some applicants will come to the central office from outlying areas, and some tenants will mail in their rent checks. However, the project offices are generally the focal points for these activities.

Applications, Rent Collection and Social Services: The role of the administrative assistant provides an interesting contrast to the way the Americus authority operates its program. Nashville's administrative assistant is a one-man field operation, something that Americus does not have.

During the first week of the month, the administrative assistant collects rent at each of the project offices and, if necessary, will collect rents on a door-to-door basis. Office hours are also used to take applications or to take maintenance work orders that tenants are encouraged to hold except in an emergency. Finally, the administrative assistant uses the office hours to talk with tenants about their problems or complaints; this is the authority's only attempt at social services.

When the administrative assistant returns to Nashville daily, he brings with him all rent receipts and applications for processing. Funds are deposited in a Nashville bank until the assistant's next trip to the project towns, where rent receipts are redeposited in local banks until being transferred at the end of the month to an unlimited revolving account.

Since the authority's clerk typist left, the administrative assistant has relied on the accountant to process all applications (there is a waiting list for most units), prepare leases, and do reexaminations. Another staff member is obviously needed to reduce the workload of both the accountant and the assistant.

Maintenance: Like the Americus authority, Nashville's maintenance staff operates from the central office, dispatched daily on work assignments. Outlying towns are charged a fee for the use of the authority's four trucks and pay a pro rata share of the maintenance men's salaries.

Work orders for each area are usually held until there are enough to warrant sending a truck and work crew. This may take up to a week, although emergencies are answered immediately.

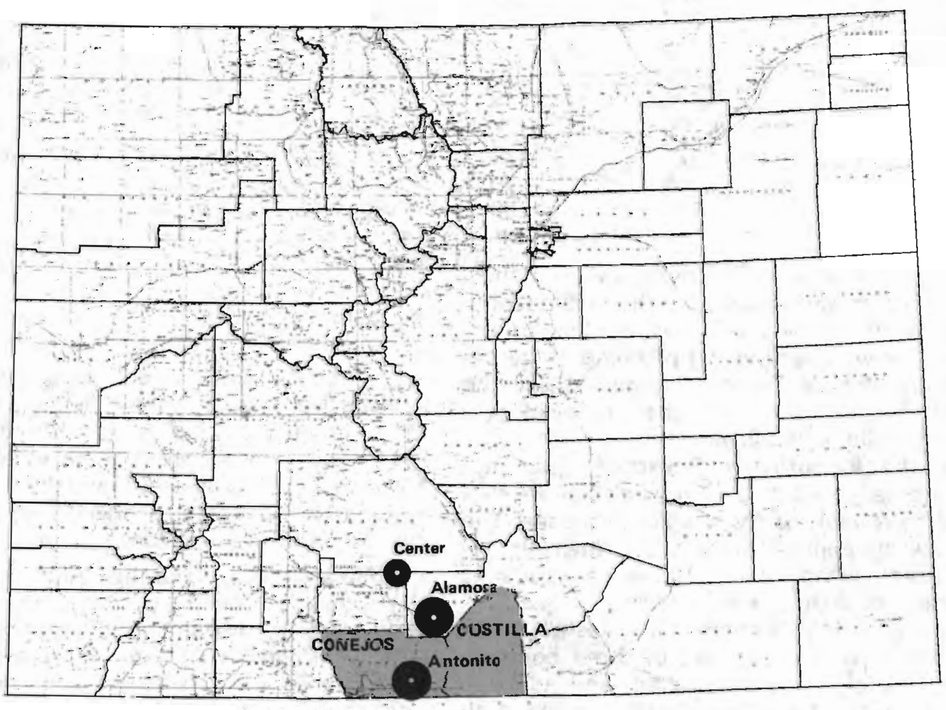
The Nashville maintenance department is divided into work crews: one two-man crew for routine maintenance, and another crew to do painting and yard work, although the latter crew may be divided. The maintenance supervisor tries to make preventive maintenance inspections more than once a year and, when possible, will make repairs himself.

Case 7. San Luis Valley Housing Committee

The San Luis Valley Housing Committee compact was not signed until March 1972. Although no units have been constructed, 200 are under ACC. Bids for their construction were opened in February and March 1973. A management plan was verbally approved by HUD but will not be implemented until units are ready for occupancy. This public housing authority is included as a case study because it illustrates some of the potential political problems in attempting to create a regional structure. Local control is a phenomenon that must be dealt with in any move toward regionalization. San Luis Valley Housing Committee also is included because its development reflects a transition in HUD policy, intimated in management circulars over the past 10 years.

Authority Background: The San Luis Valley Housing Committee, located in Alamosa, Colo., is a unique accomplishment. It brings together for the first time culturally and economically similar towns and counties—the City of Alamosa, the towns of Center and Antonito, and Conejos and Costilla Counties—each passionately protective of its political identity and control. Although the housing compact's development has been stormy at times, it has also resulted in the first major allocation of public housing units to this isolated, poor, and badly housed area of southern Colorado.

To understand the "success" of this housing compact, a look at the physical setting of the San Luis Valley, and at the economic and social forces operating there, is useful. The San Luis "Valley" in actually an 8,000-foot plateau infrequently dotted with sagebrush and cottonwood trees, surrounded on the west by the Rocky Mountains and on the east by the Sangre Cristo Mountains. There are no large towns; Alamosa, the seat of Alamosa County, is the largest with more than 6,000 people. Most of the other towns have less than 1,500 population, and they are distant from each other. The accompanying map shows how sparsely populated the area is.



San Luis Valley's only major industry is agriculture, mainly potatoes and lettuce. Both do well during the mild summer months, attracting migrant workers to the valley to supplement the local workforce. Potato processing provides employment during the long winter months when the valley often records the lowest temperature in the Nation.

Farms tend to be small family-run establishments, although there are some out-of-State operations. Year-round employment is possible on many of the farms because of the processing plants. However, the number of hours vary each day, and employee wages are unpredictable. Most people in the San Luis Valley are poor. Fully 32 percent of the population in the four-county area is below the poverty level, and 28 percent of the housing lacks essential plumbing, is overcrowded, or both.

For a number of years, poverty in the San Luis Valley—and the presence of a large minority population (the overall area has about 40 percent Mexican-American population, although in some towns the percentage is over 90 percent)—attracted poverty workers, regional groups, and State and Federal officials. Many came with promises, but little money, and the local population learned to distrust outsiders. The promises went unfulfilled, the money rarely appeared, and many of the officials went home.

Distrust for outsiders was matched by distrust among local groups, the most acute division being among Chicanos. The presence in the valley of the United Farm Workers no doubt served to heighten the political awareness of Chicanos. The young, particularly, began to challenge the politics of elder residents, who seemed conservative and protective of their status. A division resulted between some older and younger residents, and this division was further complicated by differences among political parties.

In the early 1970's, housing became an issue in the valley. Alamosa had built 40 units of low rent housing in 1964, but the other areas of the valley remained ignorant of the program until outsiders began encouraging the formation of housing authorities in order to build farm labor housing. In 1970, the Colorado legislature passed a housing act that created a division of housing in the State's Department of Local Affairs. Originally, it was designated as a technical assistance and code enforcement agency, but later the division received authorization to give up to 50 percent grants for the development of "modest" housing in rural areas. The emphasis of the grant program was agricultural housing.

Costilla and Conejos counties' housing authorities were organized largely with the assistance of both the division of housing and Uplands Inc., a regional technical assistance organization for low income groups, and the town of Center soon followed with its organizational effort (Alamosa and Antonito already had LHA's). But the housing issue might have died had it not been for Colorado Housing, Inc. (CHI), a nonprofit, statewide, low income housing group funded by the Office of Economic Opportunity.

CHI was asked by the division of housing to go into the San Luis Valley. Once there, CHI's field staff found disillusionment, distrust, and a stack of incomplete organizational forms. For example, the Center authority's organizational transcript had been lost and had to be completely reassembled. CHI decided to stay in the valley to help overcome the chaos created there and to begin preparing applications for low rent housing.

While working with the various communities, CHI approached the HUD office in Denver (this is both a regional and area office) regarding the allocation of units to each authority. HUD responded that it wanted to allocate units to the San Luis Valley, but to allocate a few to one authority and a few more to another was not economically feasible. As an alternative, HUD's general counsel office suggested the formation of a joint management and maintenance organization bound to cooperation by a legal compact. Colorado law allows cooperation between city or county authorities, but does not specifically allow for regional authorities. This type of legal device had been used on two occasions in North Dakota and could be adapted to the San Luis Valley situation. Unless the town and county authorities in the valley agreed to joint management, HUD said it would not be amenable to allocating units to any of them.

CHI had the uncomfortable task of presenting this "alternative"—the only "condition" under which the communities could obtain low rent housing units—to the housing authorities. Staff again remained in the valley, this time for 6 weeks, to accomplish their work. Concern arose over the role of the Alamosa authority. The other authorities feared that Alamosa would dominate the compact because it had housing experience and would have more units than the others. Each community feared loss of political control and, to some extent, had to overcome their fears that CHI might also want to control the authorities.

As final encouragement to the authorities to join the compact as the only means of obtaining desperately needed housing, CHI brought 10 representatives from the valley to Denver to meet with a group from HUD. The meeting was apparently convincing. HUD was adamant in its refusal to fund the authorities separately, but explained that the compact offered each authority sufficient safeguards for local control of housing design and location, and equal representation in making decisions on management and maintenance policies. An important safeguard of the compact was HUD's right to transfer to the housing committee the annual contributions contract payments of any member authority that tried to drop out of the compact after obtaining its units. In other words, the compact could not be used only to obtain units.

The authorities agreed to cooperate, and HUD drew up the compact which was signed on March 27, 1973. Antonito was admitted in February 1973. The signing did not terminate the suspicions each community had of the others; it did, however, provide a forum for cooperative effort. The communities rose above political self-interest in order to bring some decent housing to the San Luis Valley. Although development and management of the housing may prove difficult, the first challenge—that of organization—has been met.

The Authority's Program: Compact members have 200 new units of Turnkey I housing under annual contributions contracts, divided as follows:

Location	Population	Units
Alamosa	6,985	85 (scattered site, 40 may be for elderly)
Center	1,470	30 (scattered site, 10 may be for elderly)
Costilla County	3,091	25 (2 towns, mostly family)
Conejos County	7,846	45 (3 towns, slightly more than 50% for families)
Antonito	1,113	15 (plans not defined)
TOTAL		200

In addition to the 200 new units, 54 units of existing public housing will be managed by the San Luis Valley Housing Committee. These units include 40 owned by the Alamosa Housing Authority and 14 owned by the Antonito Housing Authority.

In their original applications to HUD, each authority requested substantially more units; the response was an original allocation of 200 units, with 200 more to follow during the second year. That was before the federally subsidized housing moratorium.

The housing compact retains the individual authority's power to seek bids and award contracts. Alamosa and Center, however, chose to hold a joint bid opening on February 27, 1973, whereas Conejos and Costilla counties opened their bids separately on March 22 (Antonito will probably accept the builder for Conejos County, since its units were approved after the others). No builder in the San Luis Valley has enough capital to do all the construction, although there are a number of available subcontractors.

How the Authority is Governed: All the authorities joining the housing compact have their own board of commissioners, with five members each, chosen either by the town mayor or the county commissioners. The boards are responsible for all decisions affecting the authorities acting on their own behalf. For example, each board approves housing locations and development proposals for its own community. Lately, these boards have been meeting monthly.

Decisions regarding the joint management-maintenance agreement are made by an executive board composed of the chairman and secretary of each member authority. Although there are 10 members on the executive board, only one representative from each authority may cast a vote. Thus far, representatives to the committee have hesitated to vote without first going to their respective boards for confirmation of their decisions. It is expected that this reluctance to make decisions will lessen once housing development is completed and the management policy is initiated.

Housing Administration: The San Luis Valley Housing Committee is a cooperative management and maintenance effort under the leadership of one executive director. This director was formerly the executive director of the Alamosa Housing Authority, where she had years of experience in managing and maintaining 40 units of low rent housing. The executive director will also serve as accountant, and a secretary will be hired.

A management plan, developed with the assistance of Colorado Housing Inc., was submitted to HUD and received verbal approval. It calls for centralized management from the Alamosa Housing Authority office. Applications and rent collection, as well as most routine maintenance, will probably be the responsibility of part-time, local resident-managers who will either be paid for their work or will perform their services in lieu of rent. The services that the resident-manager will perform would be difficult for central office personnel to handle, since a tour of all the proposed units would require 200 miles of driving.

The resident-manager will be furnished with an authority pickup truck, tools, and supplies to adequately service a multitown area. The use of tenants as managers is an attempt by the new authority to prevent management problems that could result from operating in a widely dispersed region and to keep down management and maintenance costs. This undoubtedly experimental approach to management and maintenance will be closely watched by HUD and others interested in regionally operated low rent housing.

The management plan is also a reflection of each member authority's concern for local control. An individual hired to provide management and maintenance service in a particular jurisdiction will have to be approved by the board member from that jurisdiction.

How Well Do the Authorities Operate?

Public housing authorities in all parts of the Nation demonstrate almost as many different management and maintenance operations as there are authorities. Although many follow similar patterns, variations are always found based on local conditions, personalities, geographic location of projects, and other factors. When the Housing Assistance Council began looking for rural housing authorities to study, the criterion used was not how different an authority was from all others, but how efficiently and economically an authority operated, primarily according to HUD standards. The result was selection of a number of relatively efficient and economical operations (notwithstanding the financial setbacks these authorities suffer due to a lack of operating subsidies), each somewhat different from the other.

These authorities developed their own responses to basic rural deficiencies, such as widely dispersed and small populations, lack of available personnel and other resources, and entrenched notions of local community control. Their responses were varied and, as the descriptions illustrate, there are some imperfections in their approaches. However, when compared to the difficulties of small authorities or of certain large, urban authorities, the problems of the regional or semiregional housing programs appear minor.

Types of Authorities

Each of the rural housing authorities studied was created using the best of existing State legislation to overcome the problems of poor people living in bad housing. In Georgia, where two of the cooperative agreement authorities are located, regional authorities were prohibited until recently, and they are still prohibited in Colorado where San Luis Valley Housing Committee developed. It is unfortunate that the earlier limitation on regional authorities in Georgia has established the idea of local housing authority control there.

In contrast, the regional housing authorities studied are the products of housing laws that promoted regionalism as a way to serve rural areas, particularly farm families. South Carolina's law was the most compelling, for it prohibited the creation of authorities in towns of less than 5,000 population; instead, these towns would have to participate in a regional program if they wanted low rent public housing.

Legislation for the Vermont State Housing Authority created a single housing organization for most of the small towns and rural areas of that State. The legislation also prohibited the formation of county authorities, thus limiting local communities to one other alternative, that of forming their own authorities. But, most of the towns could not support an authority, and it became common knowledge in the HUD area that applications for small authorities would probably not be approved. State legislation could have totally eliminated the need for other authorities had it not limited the State's program to leased housing only; some communities, in apparent desperation, formed their own LHA's merely to build conventional elderly housing.

Administrative Structures

Although the legal structures, or types, of these authorities were limited by State legislation, no such limitations were placed on the design of their administrative structures. HUD provided each authority with guidelines on what needed to be done, but the results were as varied as the number of authorities and, often, unrelated to the type of authority created. Some thorities, including both regional and cooperative agreements, chose to decentralize their management and maintenance functions, while others retained all administrative functions in a central location.

One might expect the physical size of an authority's jurisdiction to influence the location of staff, but it appears to do so only in some cases. For example, South Carolina Regional Authority No. 1 provides housing in small towns throughout nearly a third of the State and, consequently, the staff is decentralized in six geographical zones. Similarly, the San Luis Valley Housing Committee, a cooperative agreement authority that will service widely dispersed communities, will locate resident-managers in each major area. In contrast, the entire State of Vermont is serviced by three field staff, and only two of them live and work in their territories, although they do not maintain full-time offices there. VSHA lacks funds to open field offices, yet one would certainly be useful in the northern part of the State where there are 400 scattered units.

Mississippi No. VIII also covers a large geographical area, but all its suboffices are located along the southern border of the region, while projects 100 miles distant are visited only two or three times a month. But, the bulk of its program is in the Gulfport area, and a competent and well-tenured staff is available there, so the authority is hesitant to move. A more extreme case is Tennessee Valley Regional Housing Authority, whose only office is 140 miles from many of its projects.

The two cooperative agreement authorities in Georgia cover much smaller areas and are able to reach their furthest projects in less than 1 hour of driving time; consequently, they have little use for full-time field offices. Although distance does account for some authorities decentralizing, other considerations seem to prevent decentralization in other places; type of authority does not seem to be the major consideration. More likely, these authorities have made ad hoc responses to local conditions and, to some extent, the constraints of Federal funding (though the role of foresight should not be overlooked).

Whatever the rationale, staff location substantially influences the operation of an authority, as does the type of authority. From the case studies, some generalizations will be made on how these factors—type and location—affect the efficiency and economy of these rural authorities in terms of the following: 1) adequacy of management system; 2) adequacy of maintenance system; 3) level of tenant relations and social service program; 4) extent and diversity of housing program; and 5) program costs. Comparisons will be made between the cooperative agreement authorities and the regional or State housing authorities.

Adequacy of Management System

Several areas of management will be covered. First, there is the efficiency of the accounting system. The regional and State authorities have the most simplified accounting systems because each of them has only one set of books for all their projects. This is not the case with the cooperative agreement authorities; the most extreme example is the Housing Authority of the City of Nashville, Ga., whose accountant maintains eight sets of financial records, one for each authority in the agreement. Americus and San Luis Valley are not far behind with five sets of records each (Americus maintains separate books for its four cooperating authorities and for the city's urban renewal program).

Each authority participating in a cooperation agreement retains its funds in a local bank. When rents are collected, they are deposited in the separate banks, rather than a single depository. At the end of each month, the managing authority's accountant must transfer funds from each account, according to a proration of costs, into a single account for the payment of bills. Later, the accountant figures which bills are charged to a specific authority and then withdraws funds from that authority's account to reimburse the pooled account. Fees are charged to cooperating authorities for the use of the managing authority's staff and vehicles; this system requires separate records of each visit to a particular area so that fees can be applied to the appropriate authority account.

All these transactions are complex and time-consuming. Not surprisingly, the smaller cooperative agreement authorities generally have a higher ratio of accounting staff to number of tenant accounts than do the authorities with one set of books each.

Two regional and one cooperative agreement authority are experimenting with computers to handle at least some tenant accounting.[11] Mississippi No. VIII and Americus are retaining their own accounting staffs, primarily to prepare HUD financial reports and pay bills, so the computer services are not really lowering accounting costs for these authorities. Mississippi No. VIII, though, probably would have hired an additional bookkeeper had it not purchased the computer service.

In contrast to these relatively minimal uses of computer services, the Tennessee Valley Regional Housing Authority contracts all of its accounting work to its nonprofit organization, CDI, which runs its own computer. The arrangement is generally satisfactory because the two organizations are closely aligned.

The second area of management adequacy to be discussed is the efficiency of the rent collection systems. Unlike most other measures of housing authority efficiency, the type of rent collection system has less to do with the type of authority or location of staff than with the type of housing program. Four of the six authorities (San Luis Valley is not counted here because it is not at the management stage yet), including the regional and cooperative agreement authorities, rely primarily on their own personnel to collect rent either on a door-to-door basis, or to hold rent collection hours in each project on specified days. These authorities report low rent delinquencies, and low yearend collection losses.

This is not the case for either the Vermont State Housing Authority or the Tennessee Valley Regional Housing Authority. Both authorities have leased housing programs only (one is rental, and the other is homeownership) and, as a consequence, their tendency is to rely on private enterprise to service tenants. Nonauthority personnel are used to collect rents (in Vermont, owners of leased units are expected to collect rents, and TVRHA relies on tenants to bring their rents to local banks) and the result has been delinquencies and high collection losses.[15]

Because the leased unit owners in Vermont receive their monthly rental check from the authority regardless of the rent they collect, there is little incentive to collect rents promptly and thoroughly. Similarly, in Mississippi, the local banks are not obligated to make tenants pay their rents; the banks act as a depository only and do not receive a fee for their services. The Mississippi program further suffers from the fact that nonauthority personnel process the tenant accounts, but are not responsible for seeking payment.

A third phase of management is the tenant application system. There were only minor differences in the tenant application systems of the authorities studied, regardless of type of authority or location of staff. Most applications were taken either at project locations or somewhere nearby, although appointments for application were most often made through the central offices.

Word-of-mouth communication is the most common form of advertisement for public housing applicants in the rural areas studied. Most of the authorities have used newspaper publicity but found it unnecessary after a while. In rural areas, local information travels quickly and extensively, and the authorities have found that applicants often know about vacant units before the authority is informed of them. Other tenants usually pass the information on to people they know or to people inquiring around the various projects.

It is not known whether this informal system of publicity and referrals discourages some potential applicants. The authorities think not, since even strangers in these small communities will learn where public housing is and will then inquire about applying. All the authorities place housing need above other criteria when selecting tenants, thus lessening the effect of tenant referrals.

Adequacy of Maintenance System

There are three aspects of an adequate maintenance system that will be covered here. The first is prompt service. When emergencies

[11] HUD officials in the Atlanta regional office offer these reasons for promoting computer services: (1) A computer can be more accurate, although this depends on the accuracy of the data fed to the computer; (2) a computer can instantaneously retrieve all types of statistical data; and (3) a computer can save an authority money, because a licensed accountant need not be hired; a bookkeeper will do. The last reason is probably the most important. A small rural authority often is unable to find a competent accountant, nor can many small authorities really afford to pay an accountant a decent wage. The result is poor accounting and financial reporting.

[15] Particularly in the homeownership program, there is the attempt to treat tenants as if they were homeowners and, therefore, totally responsible for their units. This policy needs reevaluation, because numerous tenants are not paying their rent or maintaining their units as required.

arise, prompt service is essential to prevent excessive damage to housing units. Usually, the authority that can respond quickly to an emergency will save itself money and additional work later.

The case studies show that prompt service is less an attribute of the type of authority than of the location of an authority's staff, although type does have an indirect effect on service. For example, the cooperative agreement authorities, Americus and Nashville, have no trouble in offering prompt service to tenants in projects located in those towns, but their service is delayed to outlying projects where fees are charged for each maintenance trip. To limit the multiplication of fees charged each housing authority, maintenance requests are held until there are sufficient numbers to warrant sending a maintenance man. Americus estimates that accumulations of requests take only a few days, but requests to Nashville may take up to a week to accumulate.

Mississippi No. VIII, a regional authority, also services its nearby projects within a day or two, but requests from the rural, outlying projects are serviced more slowly. Because the maintenance staff is located along the coast and must return to the central office daily, maintenance requests from the outlying projects are accumulated. This can take several days or much longer. Unlike the cooperative agreement authorities, however, some of No. VIII's projects are so far from the central office that emergencies are handled by local repairmen, a costly, and sometimes unreliable procedure.

Tennessee Valley Regional Housing Authority tenants are supposed to provide their own ordinary maintenance in accordance with the homeownership agreement, but many of them have abdicated this responsibility to the authority. To provide the necessary maintenance, TVRHA has contracted with CDI, the owner of the housing, which now employs three maintenance men. But, like No. VIII, the staff is poorly located at one end of the region and is slow in responding to requests. Most emergency requests are answered by local repairmen whose costs are higher and whose competency varies. The location of the maintenance staff gives low priority to prompt and, sometimes, adequate maintenance of authority-leased units.

Prompt service also suffers in the operation of the Vermont State Housing Authority, not because the maintenance staff is poorly located, but because there is no maintenance staff. Owners of leased units are responsible for ordinary maintenance in all but one project, and most of the owners depend on local repairmen. When the repairmen are unavailable, repair is delayed. In the few projects where owners have employed onsite maintenance staff, requests are answered promptly and a higher standard of maintenance exists.

South Carolina Regional Housing Authority No. I has overcome the problem of distance in servicing its tenants' maintenance requests by locating staff close to the housing projects. The region is divided into six operational zones, each with its own manager who is also in charge of ordinary maintenance. Some of the larger zones (those with more units) have maintenance aides to ensure that requests are answered promptly and adequately. Zone managers are always prepared to handle emergencies in their areas within short time periods; for instance, the furthest drive from the office in the largest zone is 10 minutes.

The second aspect of an adequate maintenance system is consistent quality. This particular aspect has a similar relationship to the type of authority and location of staff that prompt service has. Housing units within immediate reach of authority maintenance staff appear to have a higher and a more consistent standard of maintenance. In contrast, units serviced by unsupervised nonauthority repairmen show varying maintenance quality; the leased housing units in Vermont are an obvious example.

Preventive maintenance is the third aspect of an adequate maintenance system. In the rural areas in which these regional and similar housing authorities operate, such things as vandalism and excessive tenant damage rarely occur. This is probably true of most rural areas in the Nation. Disrepair and deterioration of units is evidenced, however, and is generally related to how vigorously housing authorities pursue their maintenance responsibilities.

Obviously, prompt responses to maintenance requests will help prevent deterioration, but more is needed. Most of the authorities studied have developed some type of preventive maintenance program, preferring to anticipate problems than respond to crises. The authorities lacking these programs are regional, but the type of authority does not account for their inadequate maintenance services.

Vermont State Housing Authority and Tennessee Valley Regional Housing Authority are both leased housing programs; the latter expects tenants to provide their own preventive maintenance, while the former relies entirely on private owners. Neither is an adequate approach because only some homeowners in Vermont provide this service, while others do not, and many tenants in TVRHA housing do not perform their own maintenance. Furthermore, neither authority is equipped to assume the responsibility of preventive maintenance when the owners or tenants fail to do so.

Level of Tenant Relations and Social Services Program

Although it would be immensely useful to learn about rural public housing from the tenant's point of view, this perspective could not be obtained due to the limited time and financial constraints of this study. However, from interviews with authority staffs, it was possible to gain some understanding of the general authority-tenant relationship. One attitude came through clearly and consistently: Tenants of these housing authorities are respected customers, not a class of people to be contended with. Poverty is not viewed as a defect of applicants or tenants.

In nearly all the authorities studied, tenants know a particular employee whom they can call when they have a maintenance complaint or some problem in paying their rent. This personal contact is, for the most part, the extent of the authorities' social service efforts. Field representatives will respond to tenant problems by referring them to local agencies or, if there is a dispute, by acting as mediator.

In rural areas, the plethora of social and health service agencies and social workers available to urban dwellers is lacking. Instead, rural public housing tenants must turn to their friends, families, and the public housing representative for advice and assistance. The broad social service programs that HUD recommends for housing authorities are really not possible in most rural areas; the alternative is, generally, personal concern, and most of the authorities reviewed exhibit a high level of personal concern for their tenants.

It appears that the rare existence of a formalized social services program in rural areas has little to do with the type of authority, location of staff, or even the type of housing program. The availability of resources may be the key factor in whether a rural authority provides a social service program; for example, Americus had modernization funds to support its one social service coordinator. Tenant organizations are still a phenomenon of urban areas. In fact, based on this study, the only towns in which tenant organizations have developed, such as Springfield, Vt., and Americus, Ga., have large populations for rural communities and concentrations of public housing units.

Extent and Diversity of Housing Program

The type of authority probably has its greatest impact on the extent of an authority's program, in terms of geographic area and number of people served. The three regional and one State authorities studied cover much larger geographic areas than do the cooperative agreement authorities. And, with the opportunity to develop housing both inside and outside of incorporated areas, these authorities are able to take advantage of a much greater selection of housing sites.

VSHA has leased housing in at least 48 towns, South Carolina has units in 29 towns, and TVRHA is developing units in 22 towns. This dispersion of units gives these authorities not only a presence throughout their regions, but credibility for future roles in providing a diversity of services to small rural communities. The only regional authority that has not built in a large number of towns is Mississippi No. VIII; its reasons for not doing so are mixed. The authority has largely responded to the housing needs of people living in the more urbanized areas of the region, and has made an important contribution to solving their needs. But, since the authority relies on local initiative to generate a public housing project in a particular area, rural areas needs have received much less attention. Apparently, the rural communities in this region are either apathetic to the housing needs of their residents, or are uninformed of the authority's program; for whatever reasons, there is little public housing there.

Program diversity hardly describes any of the authorities in the study, although TVRHA is an outstanding exception. Yet, it is not surprising that these authorities have not branched into other types of housing programs or water and sewer development (although the two cooperative agreement authorities have been, or are, urban renewal agencies). Few public housing authorities, including those in urban areas, do anything but public housing. They have not been encouraged to do so, and, in some instances, legal restraints have been placed on their participation.

Table 6. Comparison of Operating Costs in Regional or Consolidated Housing Authorities and Local Housing Authorities [1]

Authority	No. of units	Total Routine Expenses	Total Administrative Expenses	Administrative Expenses Other Than Salaries	Total Ordinary Maintenance and Operating Expenses	Total Nonroutine Expenses [2]	Residual Receipts/ (deficit)
Americus Consolidated Housing Authority							
GA–129	58	43.82	9.21	2.36	17.46	2.91	(1.05)
GA–62 [3]	446	43.98	7.84	1.20	17.07	5.55	.24
GA–179	44	49.73	9.48	2.78	19.32	3.12	(7.67)
GA–213 [3]	20	40.29	9.74	3.04	15.29	5.35	(1.20)
Total/Average	568	44.46	9.07	2.35	17.29	4.23	(2.42)
Nashville Consolidated Housing Authority							
GA–172	80	30.73	7.76	1.02	13.88	5.44	.64
GA–136 [3]	16	31.82	7.97	1.20	14.37	6.83	(4.01)
GA–92	141	33.00	7.71	.97	15.05	5.40	(2.18)
GA–88	56	33.76	7.31	1.18	11.19	7.16	(8.04)
GA–138	20	36.00	7.75	1.29	11.17	5.78	(13.76)
GA–165	20	28.87	7.67	1.50	13.13	9.56	(28.58)
GA–168	70	31.91	7.32	1.19	11.81	1.05	.72
Total/Average	403	32.30	7.64	1.19	12.94	5.89	(7.89)
Other Georgia Authorities							
GA–229 [3]	20	34.04	8.04	2.00	10.38	5.25	(6.80)
GA–236	54	37.98	7.00	2.00	8.92	0	5.26
GA–117	38	33.11	7.45	1.13	10.97	3.82	.25
GA–28	406	27.62	6.54	1.35	13.00	4.10	(4.43)
GA–173	20	36.46	7.66	1.66	13.79	6.02	(6.95)
GA–6	12,896	64.94	14.06	2.69	21.65	6.44	(41.02)
GA–23	736	26.87	7.61	1.25	13.24	4.75	(9.52)
GA–4	1,962	41.42	10.67	2.26	13.36	10.87	(11.21)
GA–208	30	27.55	7.47	1.47	14.22	12.16	(6.10)
GA–156	120	34.69	6.66	1.12	13.53	5.05	(4.07)
South Carolina Regional Authority No. I							
	1,110	30.15	6.51	.95	9.53	3.83	2.22
Other South Carolina Authorities							
SC–11	120	31.97	7.48	1.65	11.64	2.01	4.24
SC–4	890	36.02	7.86	.77	12.10	2.09	1.36
SC–3	1,240	39.15	7.34	.90	11.10	2.22	—
SC–17	156	33.22	7.94	1.40	9.85	7.36	5.06
SC–2	1,603	46.25	8.02	.82	14.91	6.58	(13.27)
Mississippi Regional Authority No. VIII							
	1,002	35.36	7.40	1.60	13.63	3.70	(5.71)
Other Mississippi Authorities							
Miss–67	20	26.00	7.33	2.83	6.04	6.50	(3.79)
Miss–76	380	26.53	6.65	1.21	9.32	5.87	.56
Miss–68	50	24.98	7.92	2.64	10.82	3.82	(1.48)
Miss–68 [3]	101	36.05	9.44	3.94	10.44	.15	(4.17)
Miss–5	727	42.64	8.46	1.40	13.19	9.46	(4.78)
Miss–83	112	26.23	7.52	1.62	9.82	4.32	(3.90)
Miss–80 [3]	22	30.51	7.12	3.26	11.69	1.42	(3.62)
Miss–75	26	33.14	7.15	2.15	9.62	2.96	(3.00)
Miss–71	163	26.37	7.91	1.43	11.44	2.88	(6.76)
Miss-65	160	33.48	7.27	1.70	11.49	1.15	5.92
Miss–58	24	29.26	9.54	3.28	9.79	1.55	2.74

[1] Does not include leased housing budgets, and all figures are for the 1973 fiscal year, unless otherwise noted.
[2] Total Nonroutine Expenses is an average over the past three years, unless otherwise noted.
[3] Budgets not available for the 1973 fiscal year.

Program Costs

A brief comparison of actual operating costs between regional and consolidated housing authorities, and between larger and smaller authorities located in nearby areas, does not reveal major differences. However, as Table 6 shows, smaller housing authorities usually have lower costs than larger authorities. This sample is limited, but similar data compiled by HUD on all housing authorities and interviews with HUD personnel in area and regional offices confirm that smaller housing authorities generally have lower costs.

This superficial comparison of costs tells us little. Interviews with HUD personnel prior to the compilation of this budget data offered little reason to expect cost savings, except those associated with the bulk purchase of equipment and materials, and with spreading overhead costs among more units. It was generally thought that a more sophisticated cost-benefit analysis was required. HUD personnel were convinced that there are cost savings attributable to consolidated and regional housing operations that cannot be measured in the short run.

A cost-benefit analysis would measure the level of services an authority provides for the dollars it spends. For example, a high quality maintenance program can save an authority money in the long run by providing service to prevent major deterioration, thus keeping non-routine maintenance costs low. The quality of maintenance is probably directly related to major rehabilitation expenditures, as well as to the useful life of the housing unit. Comparisons should be made of the preventive maintenance services of small housing authorities, many of which operate with only part-time personnel, and of the larger consolidated or regional authorities. The smaller authorities may have lower costs because they provide lower quality services, which will eventually result in higher costs.

The overall quality of management services should also be measured and compared. For example, it has been said that small authorities, again because of inadequate staffing, keep poor accounts and provide HUD with incomplete records. It may be possible to measure in terms of costs the extra work required of HUD staff to monitor these small LHA operations. Also, the stability of small authority personnel has been questioned, because high turnover rates are evident. LHA staff turnovers require extra effort on the part of HUD staff to educate and train new directors, because most of them have had no prior experience with the public housing program. This extra HUD effort may also be measurable in cost terms.

It should be noted that small authorities that want to consolidate, or communities wishing to form larger regional authorities, do not risk HUD disapproval because of the potentially higher operating costs of larger authorities. In every interview of HUD personnel, it was stated that the slightly higher costs were compensated by better service to tenants, and by less burden on HUD staff; some form of consolidation was generally preferable to HUD than the multitude of small local housing authorities.

Other Related Issues

Beyond the question of how well existing regional and, in the case of Vermont, statewide housing authorities are operating, there are several other issues to be considered. One of these is the question of optimum size. A recent study, for example, has suggested that all public housing authorities should operate a minimum of 2,000 units to achieve reasonable economies of scale and efficiency of operation. Another issue to be considered is the proper scope of powers that a rural regional housing agency should have, and what functions it could perform in the absence of viable alternatives. Finally, there is the possibility of using all available agencies and institutions to deliver low income housing. The analysis in this report has concentrated solely on public housing authorities as rural housing delivery mechanisms. There may be several other types of agencies that could perform the same function.

Optimum Program Size

In the preceding pages, various regional and similar housing authorities operating in rural areas have been described in terms of efficiency and economy. These authorities ranged in size from 200 units under annual contributions contract to over 1,300 units under management, and covered areas as large as an entire State or as small as several towns and a county. If one were to rank these authorities in order of their efficiency and economy in serving the low income housing needs of rural families and the elderly, South Carolina Regional Housing Authority No. 1, one of the larger regional authorities with 1,110 units under management throughout nearly a third of the State, would probably rank above the others. Does this mean that larger authorities in rural areas are necessarily more desirable? Is 1,100 units an optimum size for a rural regional authority? Is there an optimum size?

In the survey that the Housing Assistance Council made of HUD area offices, the most frequent response to the query regarding the minimum number of units required for an authority to operate efficiently was 100 units. This number would provide sufficient income to hire one full-time administrative employee and, possibly, two maintenance employees. Most HUD housing management staff consider full-time employees essential to the efficient operation of a housing authority. Yet, it is doubtful that HUD staff would consider 100 units an optimum size for an LHA. In fact, one housing program's management director stated that 100 units will only provide "sufficient operating monies for a scarcely efficient operation."

In spite of the cost comparisons shown in the previous section, many HUD staff still believe that there are certain economies of scale in a larger operation. As another HUD management specialist from a west coast area office replied in the survey: ". . . all LHA's regardless of size must perform the same functions. Obviously, the larger the LHA, the more easily these required functions can be distributed." At some point, however, economies of scale will probably diminish or, as in the larger cities, disappear. In terms of actual numbers of units, very little is known about the optimum size of a housing program, even though educated guesses abound. In the larger cities, the question of optimum size is not raised; the primary concern is providing enough housing to meet the existing need. The question, then, is a particularly rural one, because there is little possibility of breaking down large urban authorities, but some hope of creating larger rural programs.

Although the question of optimum size cannot be clearly answered in terms of units either for urban or rural areas without a great deal more investigation, the question in rural areas can be approached in terms of geography rather than units.

For purposes of illustration, let us take four small rural towns each needing 25 units of low rent housing. Knowing that HUD recommends a minimum of 100 units for the sake of economy and efficiency, these towns decide to consolidate their management and maintenance programs under one administrative staff. On the surface, this seems like a practical solution to the problems of smallness. But, in fact, the towns are in a sparsely settled State, such as Montana, Idaho, or Nevada, and are 40 to 100 miles distant from each other. Since this consolidated authority could support only one full-time administrative person and, perhaps, two maintenance employees, where should they be placed to avoid an inordinate amount of travel costs and wasted travel time between projects? Unless this authority can devise some sort of zone system for maintenance and management of units, which would probably require using part-time personnel, the costs of travel would be prohibitive. If the authority were to expand even more to encompass many more towns and units, it might be able to support a system of full-time zone or area managers and maintenance personnel, and design a system to keep travel costs and time to an acceptable minimum.

The South Carolina Regional Housing Authority No. I uses a zone management and maintenance system to operate 1,110 units in 29 locations throughout one-third of the State. Because the small rural towns in this northern part of the State are in close proximity to each other, the authority's program could continue to grow considerably within its current boundaries without incurring greatly increased costs in travel and time. However, if the authority were to expand to include other contiguous areas where towns are more sparsely distributed, these costs would definitely increase, along with the costs associated with a lower level of services for outlying projects.

Both of these illustrations point to local conditions that make any formula approach to the optimum program size unlikely. The proximity of towns, or actual and potential project locations, largely determines the type of management system needed and many of the costs associated with management. When designing a rural program, possible jurisdictions must be laid out, the best management programs for these designed, and costs estimated. Once this is done, decisions can be made more effectively.

Although the dispersion of towns and project locations is the most apparent consideration found in this study, there are many lesser ones not yet clearly identified. For example, there might be some danger in combining small rural towns with larger, more urbanized areas in a single program. Mississippi Regional Housing Authority No. VIII sheds some light on this problem. This authority is now servicing towns with populations of 40,000 and 27,000, and several towns of slightly more than 2,000 people. The case study shows that the larger towns receive most of the authority's attention. Tenants in the larger towns receive more prompt and regular service, since staff is located nearby, than those in the smaller, more distant towns. It might be a better arrangement, at least in this instance, to incorporate the 660 units in and around the City of Gulfport into a city housing program and form a similar program for the 350 units in the City of Pascagoula. This would leave a combination of the smaller rural towns in the 10-county area served, and, though revenues would decrease, the more specific rural orientation might improve services. There is also the possibility that many more small towns in the region would consider joining an authority that did not appear to be dominated by two larger cities.

In addition to the dispersion of project locations, accessibility to each other is also a factor to consider. Rural areas often have considerable transportation problems because of poor or indirect roads and extreme weather conditions. In southern Colorado, for example, it would be difficult for the San Luis Valley Housing Committee to expand its jurisdiction beyond the plateau it now serves because roads from this area often become snowbound and are dangerous to drive during many months of the year. In large portions of Appalachia, where the need for low rent housing is acute, there are relatively few paved roads, and the steep, mountainous dirt roads frequently become flooded or snowbound.

These local conditions affecting the size of a rural housing program all lead to the conclusion that an optimum number of units does not exist. Whereas many more than 1,000 units are feasible in an 18-county area of South Carolina, less than 500 may be feasible for southern Colorado. While some States may find a single statewide agency feasible, others will find a system of regional agencies more suited to local needs. Local factors must be considered in each case.

State Housing Programs

Although regional agencies have been emphasized here, the proliferation of State-level housing agencies points in another possible direction. To date, most State housing agencies have not been active outside of metropolitan areas, and only a small portion of their units has gone to low income people. There are several explanations for this situation. Most State housing agencies now rely on existing private housing delivery mechanisms, such as nonprofit or limited dividend corporations, to sponsor housing. They are generally unable to provide housing in areas where no other impetus to housing development exists. Consequently, because of the severe shortage of all types of housing sponsors in rural areas, these agencies have limited their activities to the cities and suburbs. Many State agencies are actively encouraging the creation of local housing delivery agencies where none exist. Nevertheless, rather than initiating, developing, owning, and managing housing projects, most State agencies remain dependent upon other local agents. While many do have the powers to own and develop land and housing, only a few have used these powers.

Another reason why the performance of State agencies in rural areas has been unimpressive is that they almost invariably use the section 236 program, which is geared towards the larger cities and towns. Only a handful of State agencies have initiated the single-family loan programs that are appropriate to rural areas and small towns. Finally, there is the problem of subsidies. Except for the occasional unit leased to a local housing authority, and the rent supplements attached to a portion of the section 236 projects, State programs generally provide only interest subsidies which do not serve low income people.

Despite their current performance, State housing agencies may have the potential to meet the low income housing needs of rural areas, at least under certain conditions. Many rural States have recently created housing agencies with broad housing finance and development powers. Perhaps the most useful are the combination housing finance agencies/housing authorities.[16] These are able to function as housing finance agencies, providing the existing housing delivery system with seed-money loans, technical assistance, mortgage and construction lending, or units for public housing leasing. Like other HFA's, they can also try to create local housing delivery mechanisms. But their public housing powers enable them to take the initiative and develop and manage low income housing where no other local delivery capability exists. Although they may rely on other local agencies to deliver housing, they do not need to do so. Also, use of the public housing programs allow State agencies to serve lower income people.

[16] These are: Maine, South Carolina, West Virginia, South Dakota, Hawaii, Idaho, and Delaware.

The problem with statewide housing delivery mechanisms, as with the regional mechanisms previously discussed, is to devise effective plans for developing and managing low income housing over great distances in rural areas. Because the problems of statewide agencies must be confronted and because so little experience exists to draw upon, a considerable amount of additional research and demonstration is needed. For the moment, it might be helpful to identify some of the factors bearing on the feasibility of a State-level housing delivery mechanism.

Like the problem of defining an optimum size for a rural regional housing program, the feasibility of creating a statewide low income housing delivery mechanism is dependent upon local conditions. The most obvious of these is the size of the State. In several small States with proportionately large rural populations, a regional housing delivery mechanism might be an unnecessary level of administration. Rhode Island and Delaware, for example, are hardly as large in areas as many of the regional housing authorities found in larger States, and their total populations are comparable as well. Hawaii, Connecticut, and Massachusetts could fall in this category. Vermont and New Hampshire are of comparable size, but, as seen in the case study of the Vermont State Housing Authority, a great deal of travel is required to administer centrally even a leasing program.

Use of the section 23 leasing program by a State agency is especially feasible where there are large supplies of unoccupied housing that is sound or in need of minor repair. Unfortunately, this is the situation in many rural States where outmigration of the young has left many good houses empty. This housing program theoretically does not require the same amount of local administration as a development and management program. However, as seen in Vermont, private owners have not been very reliable with maintenance and rent collection, and hence the agency is considering the creation of its own maintenance force. Another problem with the leasing program is that the supply of available adequate units is limited, and the units that are available do not necessarily meet local needs. For example, the local housing need may be for elderly units, as is quite usual in rural areas, but the supply of housing for leasing consists of the large old homes, inappropriate for the elderly.

Another situation where a statewide delivery mechanism for rural low income housing might be feasible is in the Great Plains and Rocky Mountain States, where there are concentrations of population and clusters of small towns in one part of the State, and the remainder is virtually empty. A look at a map of Idaho, Utah, Colorado, or South Dakota illustrates this situation. In such cases, the jurisdictions of regional housing agencies would have to be so large to obtain suitable population aggregates that there would be little sense in setting up the administrative machinery necessary. Instead, limited regional or local offices of the State agency would suffice for management purposes, and major functions could be centralized at the State level, e.g., accounting, records, planning, finance, etc. The extra amount of travel costs required in such a system might be made up in the centralization of these other functions.

Any State could operate a statewide low income housing delivery system merely by creating a system of sub-State offices. The actual cost considerations would have to be worked out by the individual States. The question to be asked, however, is when does a State level mechanism become more desirable than an agency closer to the local level. This entails more than costs. The politics of a housing program administered from other than the local level are very complex. A State-level housing agency may appear to many localities as an interloper, and something over which they have no control. There are also the management problems that arise when decision-making power is centralized at a distance from local conditions. When these and all other relevant factors are considered, the regional agency may often emerge as the most practical for rural areas.

At any rate, the State housing agency appears to be here to stay and will be assuming a much larger role in the coming years. It is essential that some thought be given to how they can overcome the barriers that have prevented them from serving rural areas.

Other Possible Regional Housing Agencies

There have been several other types of regional institutions developed in rural areas in recent years. The most prevalent of these are the Economic Development Districts (EDD). Although encouraged, funded, and officially recognized under the Public Works and Economic Development Act of 1965, EDD's are actually created under a variety of State laws.

Many of these agencies have become actively involved with low income housing, sometimes going beyond the planning they normally do. There is a clear overlap of the concerns of Economic Development Districts and low income housing organizations. In fact, the function of housing authorities can be easily thought of as only one part of the more comprehensive programs now being developed by other types of agencies.

The basic mission of an EDD is to stimulate the economic development of a multicounty area by identifying needs and assets, and assisting the implementation of projects through planning and technical assistance. Their concerns range from the physical infrastructure necessary for economic development (e.g., water and sewer, access roads, vocational schools) to the development of specific enterprises, such as tourism or manufacturing. EDD's usually claim to be strictly planning and technical assistance agencies, but the line between planning and actual program implementation often becomes nebulous.

The funding pattern for EDD's illustrates the scope of their activities. The Economic Development Administration (EDA) is still the largest single source of funds for EDD's, but a considerable amount of funding comes from other Federal agencies for specific planning purposes, and also from State and local governments.[17] In many States, EDD's have been designated under State law as multipurpose regional planning agencies or A-95 review agencies.[18]

EDD's are comprised mostly of elected local leaders, with a professional staff. The initiative for creating an EDD must be local. Local leaders request through the Governor that the Secretary of Commerce designate their area as an EDD. In order to be designated, the proposed area must encompass at least two "redevelopment areas," and at least one "growth center," as defined by the Economic Development Administration.[19] It is also necessary to meet flexible criteria of sufficient size, population, and resources to foster economic growth on an areawide basis. However, every State is entitled to at least one EDD, regardless of whether or not it meets the established criteria.

Before an area is officially designated an EDD, it must prepare an Overall Economic Development Plan, which is a combination of a comprehensive plan and a work program.

The stated policy of the Economic Development Administration is that EDD's incorporate as nonprofit bodies under the laws of the State or States in which they are located. The actual creation of EDD's has not been this simple. Many are now created under State laws specifically enabling the creation of economic development agencies for regional planning agencies. Still others are created under interlocal cooperation laws found in a majority of the States that allow local governments to cooperate in the joint exercise of their powers. The law under which an EDD is created is a matter of some importance, as it could limit the types of services it may provide. For example, many State enabling laws for regional planning agencies prohibit them from undertaking operational programs. If an Economic Development District organization were created under such a law, it would be unable to serve as a regional housing agency.

It is important to point out that most Economic Development Districts are found in rural areas. As of December 31, 1971, there were 146 EDD's authorized and 111 actually designated. Of the 111 designated organizations, 102 were funded by the Economic Development Administration, eight by the Appalachian Regional Commission, and one funded locally. Forty States had at least one designated district, and 905 counties were covered.

A second type of regional agency in rural areas is the regional planning agency or council of governments, supported largely by HUD section 701 funds.

As of June 30, 1972, 39 State governments had taken official steps, either through executive order or legislative action, to delineate a system of planning and development districts at the sub-State regional level. This included 451 districts, 290 of which had policy boards and technical staff. As of the above date, 432 such agencies had been designated as regional clearinghouses (A-95), and 49 percent of these were in rural areas.[20] There is some overlap be-

[17] For example, EDD's are now receiving funds from the Departments of HUD, HEW, USDA, and Transportation, as well as from OEO and the Law Enforcement Assistance Administration.

[18] As of the end of 1971, 60 EDD's had been designated as regional A-95 review agencies. (See Sub-State District Systems, Council of State Governments, 1971.)

[19] A growth center is usually an urban center integrally related to the overall economic development of the district, intended to serve as a stable center of development and as a source of employment. Growth centers may not be more than 250,000 in population. They are eligible for all EDA programs.

A redevelopment area is usually a multicounty area designated by the Secretary of Commerce because of: (1) Substantial and persistent unemployment for an extended period of time; (2) loss of population due to the lack of employment opportunities; (3) a median family income only 50 percent of the national median family income; or (4) a threatened rise in unemployment due to the closing or curtailment of a major source of employment.

[20] *Rural Development: Financial and Technical Assistance Provided by the Department of Agriculture and the Department of Housing and Urban Development for Non-Metropolitan Planning Districts in Fiscal Year 1972*, U.S. Department of Agriculture, Washington, D.C., 1972.

tween these agencies and economic development districts.

Those regional planning agencies that are not also economic development districts are usually considerably less "activist" than those performing EDD functions, insofar as they are less likely to become involved in program implementation. In the area of housing, the typical regional planning agency fulfills its basic function by including a housing element in its regional plan. This includes estimating housing needs, formulating regional housing goals, and, in more urban areas, creating "fair share" distribution plans. These planning agencies have also assisted local housing developers, including public housing authorities, with market information for the packaging of applications and development plans. They have also been very helpful in promoting awareness of low income housing needs and have frequently provided technical assistance to public and private housing sponsors.

There are several potential benefits to be obtained by giving the responsibility for the delivery of low income housing in rural areas to economic development districts and other planning organizations.

First, they exist. EDD's, and to a lesser extent regional planning agencies, are established institutions in rural areas. This is a major benefit because it is often easier to begin with an established institution and expand its responsibilities than it is to conceptualize and create a new agency. Both startup time and initial operating costs could be reduced in this way.

Second, the existing agencies often have trained staffs. Because they are established institutions, many EDD's and planning agencies have recruited trained staffs already familiar with the process of housing development. There is little difference between the basic process of economic development and housing development. Both are largely dependent on land development, provision of basic facilities, mortgage finance, public finance, etc. It would not be difficult to direct their resources to housing programs.

Third, they usually understand the area in which they are working. EDD's and planning agencies have a basic familiarity with the social and economic problems of the area and have a developed plan for meeting these problems. Also, those receiving HUD 701 funds have included housing among their planning concerns.

Fourth, EDD's and other planning agencies normally have a broader view of rural development needs than do single-purpose housing agencies. It must be asked whether rural areas can afford a proliferation of single-purpose development agencies, (e.g., renewal, economic development, housing, public works, etc.), or whether it would be more efficient to work through multipurpose community development agencies.

There are also several reasons why economic development districts and other planning agencies are not likely housing delivery mechanisms. There may be limitations on EDD and planning agency functions in existing legislation. Many, because they are created under State laws prohibiting them from undertaking operational programs, could not become involved with the delivery of low income housing except through planning and technical assistance. Also, many see the combination of planning and program implementation as bordering on conflict of interest. This is especially true if the agency holds A-95 review power.

The Multipurpose Agency

If it is difficult to find experienced and capable agencies in rural areas to deliver low income housing, it is even more difficult to find the other types of agencies that now carry out the related community development functions of renewal, codes, water and sewer, and social services. Indeed, there is some question whether the proliferation of such agencies is desirable. In urban areas, complaints are often heard about the functional fragmentation of agencies and responsibilities in the fields of housing and community development. If the idea of using all available agencies in rural areas to deliver low income housing is a useful one, it can perhaps be extended to include the concept of a multipurpose rural housing and community development agency able to perform a wide range of functions.

At this time, State enabling legislation for public housing authorities is the broadest available, giving local authorities a wide and flexible array of powers. Because most State public housing laws were based upon a model provided by the Federal Government, they are all basically the same. However, for several reasons, local housing authorities have never been encouraged to investigate and utilize the full scope of their powers. Urban areas have other agencies to meet needs ancillary to housing production, but in rural areas few housing authorities had the inclination or expertise to go beyond the development and management of housing units. Today, most rural housing authorities would resist the suggestion that they become involved with water and sewer development, for example, even though this is a desperate need.

The concept of multipurpose housing and community development agencies for rural areas is one worth investigation regardless of the type of agency it is built upon.

First on the list of powers for such agencies would be the ability to develop, own, and manage housing for low and moderate income people under any Federal or State program, either existing or proposed. Frequently mentioned throughout this report is the fact that rural areas lack the local agencies necessary to use all existing housing programs. For example, one town has a housing authority, but no interested sponsor or developer for HUD or Farmers Home Administration interest subsidy programs; another town has an active nonprofit housing sponsor but no public housing authority. In either case, there is only one-half of an adequate housing program.

To overcome this situation, rural housing agencies should be created, thereby making the whole range of housing subsidy programs available. At this time, Federal legislation prevents public agencies from utilizing several housing programs, most notably the interest subsidy multifamily programs of HUD and the Farmers Home Administration. This should be corrected, and if new programs are created the same mistake should not be repeated.

Additionally, a multipurpose rural housing and community development agency could become involved in:

- The management of privately-owned, subsidized housing. This could bring about a higher quality of management services for such housing in many areas and also standardize the quality of services throughout an area.
- Coordination of a comprehensive social services program for residents of all subsidized housing.
- Development of water and sewer facilities, which are now provided, if at all, by a variety of public agencies, special districts, and private entrepreneurs.
- Development of other necessary community facilities, such as community centers, clinics, and recreation facilities.
- General renewal and land development for housing and other community development purposes.
- The design and enforcement of housing codes, which are now practically nonexistent in rural areas.

The reasons for combining several housing and community development functions in one rural agency are generally the same as those covered earlier in this report for combining the operations of several small housing authorities. Such an approach would make more effective use of the talent available to administer programs in rural areas and possibly achieve some economies of scale as well. Also, there are the added benefits of increased coordination among related functions. As the division between housing, physical development, and related social programs breaks down, and the broader concepts of "community development" and "rural development" are refined, it is likely that multipurpose agencies, such as described here, will be created and tested in rural areas.

Recommendations for Action

The types of regional and multijurisdictional rural housing agencies described in this report are not prevalent. Most rural areas of the country are not served by any type of low income housing agency. Where agencies do exist, they are usually small local housing authorities, even though Federal housing professionals have been aware of their shortcomings for years. This situation has persisted not because alternatives do not exist; several of the authorities in this report have operated for more than 10 years. It has persisted largely because there has never been a concerted effort of Federal, State, and local governments to see that rural America is served by a system of effective and efficient low income housing agencies. The situation continues, in effect, by default.

Several steps—both short and long term—may be taken to encourage a system of effective rural housing agencies.

Research

Much more extensive research must be done on the current state of rural housing delivery and how it can be made more responsive to the needs of low income people. The time and financial constraints of this report only allowed for some reasoned generalizations; more specific knowledge is required to design an adequate delivery system. There are problems that need further identification and explication, particularly in the area of housing management.

HUD currently is spending $20 million on 13 demonstrations of public housing "management innovations" throughout the country but, with the possible exception of Hawaii, the demonstrations are entirely urban. Obviously, the management recommendations will be addressed primarily to the dynamics of operating an urban housing program. The development of a housing program for rural areas must first recognize that rural management needs—and the ways to meet them—are somewhat different than those of urban areas.

For example, rural areas do not suffer the vandalism and the crime more common to urban areas, so security service is not a major management concern or expense. On the other hand, rural housing is often on scattered sites, with units under the same management often 40 miles from each other, making distance a major concern and expense. There are numerous management problems that are specific to rural areas, such as how to provide needed social services when there are no available resources. Other management problems shared with urban areas might not be solved by urban solutions. These problems must be identified much more thoroughly than in the Housing Assistance Council case studies before a full panoply of solutions can be offered.

Furthermore, although the Housing Assistance Council has attempted a superficial comparison of costs between regional housing programs and small local authorities, there is substantial need for a thorough cost-benefit analysis of various approaches to providing rural low income housing. The cost differences between larger and smaller authorities are minor, but possible cost benefits of larger authorities resulting from preventive maintenance and timely rent collection, among other things, are still uncharted. The extent of these benefits must be uncovered before establishing new housing policy.

One of the most difficult obstacles will undoubtedly be the reluctance of many small communities to join in multijurisdictional agencies out of fear that they would lose their autonomy in housing matters. Local control has long been a volatile issue in low income housing programs, particularly public housing. It would be vitally important to first gage local attitudes toward local cooperation in housing before dealing with them through either incentives or appropriate educational efforts.

More extensive research into existing housing legislation at the State and Federal levels will also be needed. This legislation, which largely has determined the structure of the existing low income housing delivery system, should be analyzed carefully for changes necessary to encourage a more flexible and responsive system. A thorough analysis of the laws pertaining specifically to the creation of public agencies is particularly necessary. For example, the public housing enabling laws in practically every State, based on a model law created in the late 1930's, may need reexamination.

What is needed is a legislative overview of the laws creating existing and potential low income housing delivery institutions, and an analysis of how they related to each other and to the Federal legislation creating the subsidy programs. Questions that remain unanswered include:

- What changes in State laws would be needed if Economic Development Districts or Regional Planning Agencies were used as low income housing delivery mechanisms?
- What is the full scope of powers of a housing authority, and what kinds of programs can an authority legally undertake?
- If it is decided that regional agencies are more desirable than cooperative agreement compacts, it should be taken into account that most State laws that allow regional authorities prohibit an existing housing authority from becoming part of a regional agency unless it has permission of all of its bondholders. Is this provision necessary, or may it be repealed without the permission of bondholders?

These are only among the more obvious questions to be answered. They do illustrate the types of questions that must be asked and emphasize that a delivery system consists of institutions as well as subsidy programs.

Demonstration

Demonstrations similar to HUD's $20 million management innovation program are needed in rural areas to identify and test innovations in low income housing, particularly in sparsely populated areas.

The purpose of most demonstration programs is not only to prove something's value in a particular situation, but also to test its applicability to somewhat different situations. Demonstrations reveal unexpected problems and ways to deal with them.

This study has proposed the creation of multipurpose rural housing organizations at the regional level that could, through a multiplicity of powers and responsibilities, overcome the current deficiencies of rural areas that prevent the development of low income housing and related services. Such organizations do not now exist in rural areas (nor in urban areas, although they have all the institutions to provide housing and other services). Consequently, this concept will require extensive testing before becoming a full-scale operation.

Technical Assistance and Training

This report stated that half of the Nation's counties, most of them rural, have no public housing units. In rural areas that do have public housing, small authorities abound. These small rural authorities probably do not know the potential benefits of consolidated housing efforts, and part-time housing authority staffs may not be expected to organize their own full-scale regional housing programs. There are still communities in this country that do not know much about the public housing program, let alone the relative benefits of various management options. And, many communities with small housing authorities would never consider, without encouragement, sharing programs with a neighboring community. The need for an aggressive program of technical assistance and training is apparent.

In southern Colorado, the recently appointed executive director of the new San Luis Valley Housing Committee asked HAC how other rural authorities handle the problems of management and maintenance over widely dispersed geographical areas. Although she was a former director of a one-town authority, she was unprepared for the unique problems of multitown and multicounty jurisdictions. Similarly, the Tennessee Valley Regional Housing Authority in Mississippi was uninformed of potential approaches to overcoming the problems of distance and now has some serious management problems. These and most other rural authorities were created and continue to operate in a vacuum of information. As a consequence, they might unknowingly repeat each other's mistakes. Planning for a technical assistance and training program should include consideration of the following questions:

Types of Assistance Needed: Existing rural authorities and communities needing low income housing may require assistance in several areas, including:

- Assessment of low income housing needs;
- Assessment of the best housing programs to meet housing needs (communities first must know what programs exist);
- Coordination with other communities on the development of a suitable housing delivery program, including legal assistance;
- Design of an adequate management and maintenance program;
- Training of staff in development procedures, accounting and record keeping, housing management, etc.;
- Development of social service resources and liaison with related governmental entities, and public and private organizations.

Technical assistance and training should be a continuing task. It should begin with the actual "selling" of a rural housing delivery system to communities, regions, or States, proceed through the formation of a program and the development of staff, and continue during the lifetime of the program providing information on new ideas and resources.

How Can Assistance Be Provided: The three obvious resources for technical assistance and training are private housing organizations, States, and the Federal housing bureaucracies.

The only HUD technical assistance effort with purported rural concern was the so-called 106(a) program, which gave financial assistance to private and public organizations so that they could provide assistance to sponsors of low and moderate income housing. The original intent of the program was to encourage more and better use of HUD programs in small communities. However, a review of the grantees shows that most were urban-oriented, and few are connected with the public housing program. In addition, the program was meagerly funded at $1 million for 1 year.

The 106(a) program has been abandoned in the fiscal 1974 budget on the grounds that many other groups are now providing the technical assistance the program was intended to encourage. However, the "other groups" noted in the budget generally are those funded by the dying Office of Economic Opportunity, and these groups are disappearing every day.

If private organizations are to provide technical assistance to localities for the development of effective housing delivery mechanisms, some program similar to 106(a), funded adequately, will be necessary.

A national organization, adequately funded and experienced in dealing exclusively with rural housing problems, would be a valuable technical assistance resource. The Housing Assistance Council, since its inception in fall 1971, has provided such services.

State-level housing agencies and departments of community affairs are another source of technical assistance to localities. In many States these agencies are already involved (particularly DCA's) in creating more effective local institutions. However, not all States, and especially not all rural States, have agencies with highly developed outreach capabilities. The creation or expansion of these capabilities would be encouraged by a Federal financial assistance program similar to 106(a) or an increased flexibility in State 701 funds. Another possibility would be setting aside community development block grant funds, if such a program is enacted, to improve State technical assistance functions in housing.

The most obvious resource is the Department of Housing and Urban Development, or a comparable agency for rural areas. HUD has a good deal of technical knowledge, although the concept of a rural delivery system will require substantial in-house training. Unfortunately, some HUD personnel believe that public housing should not be "sold." Many communities know little about the program, however, and their low income, badly housed families and elderly should not have to suffer from this ignorance.

A HUD technical assistance outreach program would require substantially more staff than currently employed. However, the Farmers Home Administration system of county offices could also serve as an available outreach staff for technical assistance. This also would require much retraining of FmHA staff, who have limited experience with the concept of public delivery systems. They are, however, more familiar with rural problems than HUD staff, although both agencies might be too severely understaffed at this time to initiate a technical assistance outreach function on a broad scale. In any event, the Farmers Home Administration should be included in any effort to design and create rural housing delivery mechanisms.

Changes in State and Federal Law

A comprehensive review is needed of State laws, largely responsible for the specific characteristics of publicly created housing related agencies. The review must examine whether existing State laws, such as public housing enabling laws, can serve as the basis for an effective rural housing delivery system, or whether new laws should be created. Prior to such a study, it is only possible to suggest the types of actions to be considered.

The most direct action is the creation of regional housing authorities through State legislation. The New Mexico legislature created and designated boundaries for six regional housing authorities (NMSA Ch. 196, Section 4–30–1), empowering the Governor to appoint boards of commissioners for them. Other possible approaches would be to establish the jurisdictions of the regional housing agencies along the same lines as designated regional planning districts, or to designate the jurisdictions after consultations with local officials and a series of public hearings.

State legislation could create the agencies and mandate that local officials designate board members within a given period of time, or automatically give a seat on the agency board to each locally elected executive of general purpose government. This legislative initiative would be greatly enhanced if the State legislatures would also appropriate funds for initial operating expenses.

If the States do not legislatively define and create a specific type of regional housing and community development agency, all options should be available for the creation of such agencies. One option is to allow regional bodies created under State planning laws to provide services under contract to localities within the region. This would require amending laws in many States.

States may also prohibit the creation of new public housing agencies in towns that are below a legislatively determined population level. This has already been tried or proposed in several States. For example, the original South Carolina legislation allowing for the creation of regional housing authorities also provided that the regional authorities would serve all towns of below 5,000 population. (This limit eventually was reduced to where any community could have its own agency.)

In Minnesota, Section 462.426(3) of the 1971 act allowing for the creation of multicounty housing and redevelopment authorities provides:

> In order not to foster the development and proliferation of minor political subdivision housing and redevelopment authorities, a county or multi-county authority once established shall preclude the formation of additional municipal

housing and redevelopment authorities within the area of said county or multi-county authority without the explicit concurrence of the county or multi-county housing and redevelopment authority and the state housing commission.

Clearly, limiting the ability of small towns to create housing delivery agencies is not unheard of, and other similar examples exist. Such limitations are potentially effective means of encouraging the creation of alternative delivery mechanisms.

It is difficult, if not futile, to anticipate the changes in housing programs resulting from the current turmoil in Federal policies. Although a lengthy analysis of Federal housing legislation could be made in terms of how well it encourages the effective delivery of low income housing in rural areas, a wait-and-see attitude is perhaps more appropriate at this time. However, several suggestions follow.

In existing Federal law, public bodies are prohibited from developing housing under several programs that, although not always serving low income people, should be part of a comprehensive housing program. Because of the overall absence of housing sponsors of all types in rural areas, this prohibition should be relaxed to allow any available agency to sponsor and develop housing under all programs. The alternative would be half of a housing program in many rural areas.

For example, public authorities cannot sponsor section 236 multifamily housing. (This is opposed by the Treasury Department on the grounds that its sponsorship by public authorities would expand the use of tax exempt bond financing for housing.) A public housing agency with bond-issuing powers also cannot sponsor a Farmers Home Administration multifamily project (section 515), because its ability to raise funds through bonds amounts to the availability of "credit elsewhere," violating Federal law. (This opinion was supplied to the Housing Assistance Council by the FmHA General Counsel.) Provisions in the proposed Senate omnibus housing bill (S. 2182) would allow the sponsorship of the 236 and 515 programs, although their final approval is uncertain.

To overcome these limitations, many housing authorities have "spun-off" nonprofit corporations to do the work the authorities cannot. This complicated and unnecessary procedure could be avoided if Federal law were changed. The idea of housing authorities managing housing produced under other programs has gained much acceptance recently. The power to develop under other programs should also be considered at this time.

Establishing a regional or cooperative agreement housing and community development agency also is long and difficult under existing Federal law. Because these types of agencies are only options, it often requires a delicate process of community organization and education to induce several counties or cities to participate in a joint housing and community development effort. With no immediate incentives, this is a very difficult "selling" job. A great help to this work—a necessity, in fact—would be a grant-in-aid program to cover the startup costs of these types of regional agencies.

In the past year and a half, the Housing Assistance Council has assisted in the creation of several multicounty housing and community development agencies. One of the essential elements in this assistance has been loan money to provide the initial staffing and overhead necessary to form the agency, obtain approval of organizational transcripts, and submit development plans and applications to HUD. Under the public housing program, other Federal funds do not become available until all of the above tasks have been completed. Depending upon the size of the area and the initial program, the staffing and other necessary starting costs range from $35,000 to $60,000. There is now little of this badly needed money available to interested localities.

These funds could be provided by broadening the uses of 701 funds to include the design and implementation of new housing and community development administrative structures. A grant-in-aid program could be designed specifically to encourage such agencies, or newly created housing authorities could be made immediately eligible for preliminary HUD loans.

Perhaps the best model for this purpose is the 701 program, which has been successful in encouraging regional and metropolitan planning and a high level of organizational competence. If other incentives, such as unit set-asides, are also available, it might be possible to obtain local contributions to create regional housing agencies.

The problem here is that much of the essential work must be done just to create the agency. Unless regional agencies of this sort are automatically created by State law, it will be necessary to identify the types of organizations eligible to receive grants to do the preliminary work to create them. This is now done by economic development districts, regional planning agencies, community action agencies, and nonprofit housing development corporations. These types of organizations, as well as units of general purpose local government and existing local housing and community development authorities, should be eligible for such grants.

A final suggestion anticipates a proposed program not yet enacted: block grants for community development. All current proposals would give automatic formula entitlements to metropolitan cities and counties only. The so-called Sparkman proposal would set aside 25 percent of available community development funds for nonmetropolitan communities, although each would have to apply to HUD for funding. The Administration's "Better Communities Act" would make no automatic set-aside for nonmetropolitan communities but would leave the funding of these communities entirely to State discretion.

None of these approaches takes advantage of an excellent opportunity to induce the creation of regional housing and community development agencies in rural areas. This opportunity consists of making rural regional agencies that meet certain criteria of competence and operational feasibility eligible for automatic formula entitlement, just as metropolitan areas are eligible for such entitlements. It makes little sense to award an automatic entitlement to a city of 50,000 but not to a multicounty rural agency serving as large a population. If the basic idea behind the creation of rural regional housing and community development agencies is to provide rural areas with the same technical competence and sophistication available now in larger cities, then such sophistication should be rewarded when achieved.

Incentives

The concept of consolidated rural housing efforts has been praised, urged, and, in some instances, even required by HUD personnel. Still, each year larger numbers of small rural authorities are formed (at least until the federally subsidized housing freeze). Although HUD management circulars may state that it is the agency's policy to encourage various forms of consolidation, it is rarely enforced, and an overall approach to consolidation has never been proposed. Obviously, the legal structure of an LHA is determined by State enabling legislation, but nearly every State allows for various forms of cooperation—either through management agreements, consolidation of municipal authorities, regional, or State authorities. The necessary tools—but not always the incentives—are available in most States.

It may be time for HUD to reevaluate its policy of distributing scarce public housing resources to any locality, regardless of whether the local housing agency is fully capable of handling these resources. More stringent organizational requirements clearly exist in the interest subsidy programs. A thorough evaluation of this policy will hopefully result in the establishment of some minimal organizational qualifications, such as full-time staff or a social service component, for eligibility for low income housing assistance.

To declare a national policy of consolidation without a national policy of rewards or sanctions is self-defeating. Some form of encouragement must be offered to induce the consolidation of existing small authorities and the creation of new authorities with regional scope and responsibilities. The most productive of several approaches that may be needed to effect national policy would probably be housing unit set-asides.

Most small rural communities now must wait years to receive a commitment of new public housing units. If HUD were to set aside a portion of new public housing units to encourage the consolidation of small authorities or the creation of new regional authorities, the prospect of having the lengthy application period reduced or eliminated would be enough to induce action in many areas.

This "carrot"—housing unit set-asides—could also be the stimulus for improved housing legislation in numerous States that now prevent such cooperative housing programs. But, housing unit set-asides, on their own, are not the panacea for small inefficient housing authorities nor for the absence of authorities in areas where they are needed. A program of incentives goes hand in hand with an adequate outreach program that will both convince some communities of the benefits of cooperation, and others of the benefits of providing, for the first time, decent low income housing. On their own, housing unit set-asides cannot overcome distrust of the public housing program, nor apathy towards the housing needs of the poor.

The Laws of Seven Southeastern States Viewed from the Perspective of Rural Housing Needs

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Introduction

Current national policy favors greater responsibility at the State and local level in the solving of urgent social problems. Programs such as revenue-sharing contemplate the exercise of greater initiative on the part of the States. Some expectations of achievement, however, may not be fulfilled unless important statutory and administrative changes are made by State and local governments. Accordingly, in considering the provision of adequate housing in rural areas, it is important to examine the existing legal structure and determine possible needs for new legislation at the State level.

Like the research project of which it is a component, this report centers on seven southeastern States—Alabama, Arkansas, Kentucky, Mississippi, Tennessee, Virginia, and West Virginia. Occasionally, however, the report also discusses Federal programs and laws which bear on rural housing.

The first seven sections of this report consist of studies of the relevant laws of the seven States. These studies, prepared by Duke University law students, were the first major step in the research upon which this report is based. Next came comparative studies of the seven States in relation to various relevant topics; and these comparative studies also constitute sections of this report. Finally, on the basis of the research incorporated in the various sections, the report itself was prepared.

Obviously, certain topics have more importance for rural housing than for urban residential development. For example, mobile homes, which in some urban areas have been almost completely excluded by zoning ordinances,[1] may have special importance in rural areas, where such restrictive land use controls often do not exist. Conversely, housing and occupancy codes, which loom large in many cities and towns,[2] are not often found in rural areas—at least not in the seven States with which this report is concerned. Requirements that are present in typical housing codes might prove unworkable in many rural ares. Water supply and waste disposal in a heavily populated urban area present different issues than in some rural areas, where wells and septic tanks must be relied on. On the other hand, rural areas may be especially concerned with any legal restraints on banks and savings and loan associations which tend to reduce the number of financial institutions from which a rural homebuilder may hope to obtain needed funds.[3]

State Assistance for Housing

Of the seven States studied, at least three have given legislative approval for State efforts to improve the housing supply. So far as the laws are concerned, the State assistance would be available for rural as well as urban areas.

The Kentucky Housing Corporation, created in 1972,[4] is probably the most ambitious of the State efforts in the housing field. Its purpose is to create "decent, safe, and sanitary" residential housing in rural and urban areas which have deteriorated in recent years through the spread of slum conditions.[5] The corporation is governed by 13 directors, of whom five are designated State officials and the remaining eight are private individuals appointed by the Governor for 4-year staggered terms. Among the corporation's powers are: The making of federally insured or guaranteed construction or mortgage loans to sponsors of residential housing when the loans

[1] *Vickers* v. *Gloucester Township,* 37 N.J. 232, 181 A.2d 129 (1962), *cert. denied,* 371 U.S. 233 (1962); *People* v. *Clute,* 18 N.Y.2d 999, 224 N.E.2d 734 (1966). However, the legality of such exclusionary zoning has become increasingly suspect. See e.g., *Town of Conover* v. *Jolly,* 277 N.C. 439, 177 S.E.2d 879 (1970); *State of Washington* v. *Work,* 75 Wash. 2d 208, 449 P.2d 806 (1969).

[2] In many instances, a chief inducement for adoption of substandard housing ordinances was meeting "workable program" requirements for certain federal funds.

[3] Thus limitations on branch banking or the radius within which a financial institution may make loans may be very important in determining the availability of credit for the rural homebuilder.

[4] Ky. Rev. Stat. § 198A.010 et seq. (Supp. 1972).

[5] "Decent, safe and sanitary" housing is a phrase that appears in federal housing legislation.

are not available from private lenders; purchase of federally insured mortgage loans made to persons of lower income for residential housing when the funds are not available from private lenders; acquiring, establishing, and operating residential housing for persons and families of lower income, and entry into agreements with any Federal, State, or local governmental agency to provide adequate living quarters for such persons and families in cities and counties where a need has been found for such housing and no local housing authority exists to fill such need; providing technical and advisory services to sponsors, builders, and developers of residential housing and residents thereof; promotion of research and development concerning construction of low-cost residential housing; and encouraging community organizations to participate in residential housing development.

Interestingly, the statute requires that lower income persons and concerns in the area of the assisted housing be given a preference as to work to be performed. Rental housing assisted by the Kentucky Housing Corporation must provide for "maximum feasible tenant participation." Also, the corporation is to establish standards of performance for materials, methods, and designs; and these standards are to meet minimum requirements of the Federal Housing Administration or the Farmers Home Administration.

The corporation also administers a housing development fund, which is distinct from any other funds that are administered by the Corporation. The purpose of the fund is to make temporary loans to (a) defray "development costs" of sponsors, builders, and developers of residential housing; [6] (b) provide to lower income persons applying for mortgages the amounts necessary to make downpayments and pay closing costs; and (c) make construction loans which are not federally insured, when such loans are not available from private lenders. The corporation is empowered to issue up to $200,000,000 of revenue bonds; and also it may issue bond anticipation notes, interim receipts, or temporary bonds. The Kentucky statute applies various restrictions to any assisted sponsor, builder, or developer—among them a limit on the return that may be received by any investor in an assisted limited dividend corporation or association. Tax-exempt status is conferred on the Kentucky Housing Corporation's property and obligations; but the corporation is authorized to make payments to local governments in lieu of the local taxes and assessments, from which its real estate has been granted exemption.

West Virginia has passed a Housing Development Act [7] which establishes a development fund to finance and provide assistance to public and private builders constructing residences for low and moderate income families. One of the legislative findings which support the act states that the shortage of housing for persons of low and moderate income "is severe in certain urban areas of the State, is especially critical in the rural areas of West Virginia." [8] The fund is governed by a board of directors consisting of four officials as public directors and seven private directors, appointed by the Governor for staggered 4-year terms with the advice and consent of the State Senate. The powers of the fund in West Virginia are similar to those granted by Kentucky to its housing corporation. Revenue bond financing is contemplated; and the fund is subject to a loan limitation of $130,000,000.

In 1972, Virginia enacted the Housing Development Authority Act,[9] which is very akin in nature and purpose to the Kentucky and West Virginia legislation. In Virginia, the governing board consists of seven commissioners, of whom two are public officials and the remainder are appointed by the Governor, subject to confirmation of the General Assembly, for staggered 4-year terms. Among the powers expressly conferred upon the Housing Development Authority—and apparently not granted specifically in West Virginia and Kentucky—is the power to "insure mortgage payments of any mortgage loan made for the purpose of constructing, rehabilitating, purchasing, leasing, or refinancing housing developments for persons and families of low and moderate income upon such terms and conditions as HDA may prescribe." [10] In addition, the Authority is empowered to make mortgage loans to housing sponsors and to persons and families of low or moderate income who may purchase residential housing. The Authority is directed to

[6] "Development costs" are defined as "the costs approved by the corporation as appropriate expenditures which may be incurred by sponsors, builders and developers of residential housing, prior to commitment and initial advance of the proceeds of a construction loan or of a mortgage, including but not limited to . . . legal and organizational expenses, expenses for tenant surveys and market analyses, and necessary application and other fees." Ky. Rev. Stat. § 198A.010(4) (Supp. 1972).

[7] W. Va. Code §§ 31-18-1 et seq. (1972).

[8] Id. at § 31-18-2.

[9] Va. Code §§ 36-55.24 et seq. (Supp. 1973). Virginia has also recently created an Office of Housing, id. at § 36-55.7 et seq., and a State Board of Housing, id. at §36-55.15 et seq.

[10] Id. at §36-55.30(15) (Supp. 1973).

supervise housing sponsors, including limited-profit housing sponsors, involving the rent schedules and tenant selection. The act also specifies certain terms and conditions in loans by the Authority. Similarly, the terms and conditions of mortgage insurance issued by the Authority are provided for; and the mortgage insurance premium is limited to .5 percent of the principal balance outstanding at the beginning of the mortgage year.[11] The Authority is granted an exemption from taxation with respect to its notes and bonds and its real estate. It is financed largely by the proceeds of revenue bonds, and apparently there is no dollar limit on the amount which it may borrow.

The State-established housing organizations in Kentucky, West Virginia, and Virginia are all too recent to provide much experience concerning their advantages and problems. In West Virginia, a constitutional attack on the housing development fund has been successfully resisted, and the creation of the fund has been found by the courts to have a "public purpose." [12] Since revenue bond financing is utilized for the most part, State constitutional limitations on indebtedness would not be applicable.

To the extent that funds for homebuilding are less available in rural areas than urban, the existence of a State-established housing development fund may be especially important as a means to fill the credit gap. To obtain best utilization of the development fund, it would seem desirable to have explicit legislative permission for the administrators of the fund to use not only direct loans but also loan guarantees and mortgage insurance.

In conjunction with the extension of credit, the administrators of the housing development funds have an opportunity to impose conditions that will help assure the good quality of the housing that is developed. The imposition of such conditions may be especially important in rural areas where such traditional governmental controls as zoning ordinances and building codes may not be applicable.

Housing Authorities

All of the seven States long ago enacted legislation permitting the establishment of local housing authorities—generally on the basis of a determination that unsafe and unsanitary housing conditions exist. All seven States authorize two or more counties with similar housing problems to combine in creating a regional housing authority with the same powers as the predecessor county authorities, which then cease to exist. None of the States expressly authorizes a statewide housing authority. However, the Kentucky Housing Corporation, authorized in 1972, apparently is empowered to operate public housing in cities and counties where a need exists therefor and where no local housing authorities exist.[13]

In all seven States, the powers granted to the county and regional authorities are broad. All may build, operate, maintain, and lease housing projects, acquire real estate, issue bonds, borrow money, contract with the Federal Government, insure their property, and perform other functions necessary to construct and operate housing projects. The projects must comply with local building codes, zoning, sanitary and safety ordinances, and are run on a nonprofit basis. The States studied require special procedures for tenant selection and for determining rental rates, although they do not prescribe absolute schedules for rent. Some of the States do limit net aggregate income of a renter to 5 times the rental rate.

All seven of the States have similar provisions—five in identical language—under which an owner of a farm that is operated or worked upon by low income farmers in need of safe and sanitary housing may file an application for the appropriate housing authority to provide dwellings for such persons. Such an application is considered by the authority in formulating projects to provide housing for farmers of low income. Under the various statutes, the housing authorities have broad power to provide rural public housing for low income farmers—if they choose to exercise that power.

Building Codes

Of the seven States, only Virginia has provided for a Uniform Statewide Building Code,[14] which is to be promulgated by the recently created State Board of Housing.[15] In prescribing standards to be complied with in constructing buildings, the board is to consult the standards of the Southern Building Code Congress, the Building Officials Conference of America, and the National Fire Protection Association. "Where practical, the Code provisions shall be stated in terms of required level of performance, so as to

[11] Id. at § 36–55.36(3) (Supp. 1973).
[12] State ex rel. *West Virginia Housing Development Fund* v. *Copenhaver*, 153 W. Va. 636, 171 S.E.2d 545 (1969).
[13] Ky. Rev. Stat. § 198A.040(10).
[14] Va. Code §§ 36–97 et seq. (Supp. 1973).
[15] Id. at §§ 36–55.7 et seq. (Supp. 1973).

facilitate the prompt acceptance of new building materials and methods. When generally recognized standards of performance are not available, such provisions shall provide for acceptance of materials and methods whose performance has been found by the State Board, on the basis of reliable test and evaluation data, presented by the proponent, to be substantially equal in safety to those specified." [16]

Enforcement of the Statewide Building Code is the responsibility of the local building department; but if a county or municipality has no building department, then the local governing body is to enter into an agreement with some other agency for enforcement. A Board of State Building Code Review is also provided, which is to hear all appeals from decisions and convictions arising under application of the building code.

Virginia also has a statewide building code for mobile homes and modular housing. Its statute, the Virginia Industrialized Building Unit and Mobile Home Safety Law, was enacted in 1972.[17] Just as with the Statewide Building Code, the legislature has directed that the administering agency—in this instance, the State Corporation Commission—have due regard for generally accepted standards promulgated by nationally recognized organizations and that, where practical, the rules and regulations "be stated in terms of required levels of performance, so as to facilitate the prompt acceptance of new building materials and methods." [18]

In 1945, Alabama authorized the promulgation of a statewide building code applicable to State building and construction, schoolhouses, hotels, and moving picture theaters.[19] In addition, municipalities and counties were authorized to adopt this code and apply it to other private buildings.[20] Mississippi has provided: [21]

> The construction codes published by a nationally recognized code group which sets minimum standards and having the proper provisions to maintain up-to-date amendments are hereby adopted as minimum standard guides for building, plumbing, electrical, gas, sanitary and other related codes in Mississippi. Any county within the State of Mississippi, in the discretion of the board of supervisors, may adopt building codes, plumbing codes, electrical codes, sanitary codes or other related codes dealing with general public health, safety or welfare, or a combination of the same *within, but not to exceed, the provisions of the construction codes published by nationally recognized code groups*, by order or resolution in the manner herein prescribed. Said codes so adopted shall apply only to the unincorporated areas of the county; provided, however, such codes shall not apply to erection, maintenance, repair or extension of farm buildings or farm structures; . . ." (Emphasis supplied)

Apparently, the Mississippi legislature, while not requiring that counties adopt a building code, wished to prevent the adoption of building codes that imposed arbitrary requirements not found in nationally recognized construction codes. Otherwise the local codes might become a means of precluding the use of new components and materials which could reduce housing cost. Somewhat in the same vein is a West Virginia statute which prohibits a local building code from excluding materials and components that have been certified as acceptable by the Federal Department of Housing and Urban Development.[22] West Virginia also has specified, by statute, requirements for sliding glass doors and safety glazing materials.[23]

In establishing a Statewide Building Code, utilizing performance standards for this Code to the greatest extent possible, and providing statewide safety standards for mobile homes and industrialized housing, Virginia stands out as a model for the other six States that were studied. Indeed, the greater economy and efficiency that promises to result from Virginia's action should aid in reducing the cost of rural housing there. At the very least, it seems important to assure, as Mississippi and West Virginia have attempted to do, that local building codes will not become a barrier to the use of more economical materials and methods in construction.

Land Use Controls

Although the seven States are not identical in their methods of land use control, their laws generally provide for some type of planning commission and for zoning ordinances, the final responsibility for which usually lies with local governments. Thus, the State has primarily an advisory and coordinating role. In some instances, provision is made for extraterritorial zoning and subdivision control.

For present purposes, perhaps the most important point to note is that in three of the States—Kentucky, Mississippi, and Tennessee—land used for agricultural purposes is to some extent exempt from zoning restrictions; [24] and in

[16] Id. at § 36–99 (Supp. 1973).
[17] Id. at §§ 36–70 et seq. (Supp. 1973).
[18] Id. at § 36–73 (Supp. 1973).
[19] Ala. Code, Title 55, § 367(1),(7)–(9) (1960).
[20] Id. § 367(11) (1960).
[21] Miss. Code Ann. §2890.7 (Supp. 1972).

[22] W. Va. Code § 8–24–50a (1972).
[23] Id. at § 47–5–1 (Supp. 1972). Tennessee has a similar provision. Tenn. Code Ann. § 53–2549 (Supp. 1972).
[24] Id. at § 13–414 (1955) (regulation not authorized for buildings on lands devoted to agricultural uses); Ky. Rev. Stat. § 100.203(4) (1969) (no regulation of agricultural buildings); Miss. Code Ann. § 17–1–3 (1972) (no permits required for farm buildings or farm structures outside municipal limits).

Alabama only municipal corporations have the power to zone, so that rural areas are largely unaffected by zoning ordinances.

Since zoning ordinances have sometimes been used to exclude certain types of housing—such as mobile homes and industrialized housing [25]—the circumstance that in four of the States zoning does not extend with full force to the rural areas may permit utilization of housing resources that zoning may exclude from some urban areas.

Mobile Homes and Modular Housing

Uniform Standards and Inspection: As has just been noted, mobile homes and modular housing in rural areas sometimes are not subject to the same restraints that zoning imposes in the cities. Also, in those rural areas where building codes either do not apply or are not enforced, compliance with, and inspection under, those codes will not present a problem. Yet, at the same time, the purchaser of a mobile home for use in a rural area should not be left defenseless—or, at least, with no remedy except that available for any breach of warranty by the vendor of the mobile home.

Three of the States studied have attempted to deal with this problem by adopting statewide legislation concerning standards applicable to mobile homes. In 1972, Virginia adopted its Industrialized Building Unit and Mobile Home Safety Law,[26] which provides for inspection by an "approved testing facility" and for affixing a label of compliance.

The statute defines "industrialized building unit" as "a building assembly or system of building subassemblies, including the necessary electrical, plumbing, heating, ventilating and other service systems, manufactured off-site and transported to the point of use for installation or erection, with or without other specified components, as a finished building or as a part of a finished building comprising two or more industrialized building units, and not designed for ready removal to or installation or erection on another site."

A "mobile home" is "an industrialized building unit constructed on a chassis for towing to the point of use and designed to be used, without a permanent foundation for continuous year-round occupancy as a dwelling; or two or more such units separately towable, but designed to be joined together at the point of use to form a single dwelling, and which is designated for removal to, and installation or erection on other sites."

The "approved testing facility" may be either an architect or professional engineer registered in Virginia, or a testing organization determined by the Virginia Corporation Commission to be especially qualified to evaluate these units and provide adequate followup service at the point of compliance to assure that production units are in full compliance with the standards set by the Commission.

The Commission—as has been noted earlier in this report—is directed by the legislature to give due regard to the standards for mobile homes and industrialized building units which have been promulgated by certain nationally recognized organizations. Moreover, performance standards are to be used. Any industrialized building unit or mobile home which bears a label, seal, or other evidence of listing by an approved testing facility as in compliance with the standards of the Commission "shall be acceptable in all localities as meeting the requirements of this law, and shall be acceptable as meeting the requirements of safety to life, health, and property imposed by any ordinance of any local governing body of this State without further investigation or inspection, provided such units are erected or installed in accordance with all conditions of the listing." [27] However, local requirements, "including zoning, utility connections and preparations of the site and maintenance of the unit shall remain in full force and effect." Violation of the law or the rules and regulations made pursuant to it is a misdemeanor punishable by a fine of not more than $500.

Alabama has adopted The Uniform Standards Code for Mobile Homes Act,[28] which applies to "a movable or portable dwelling over 32 feet in length and/or 8 feet or more in width, constructed to be towed on its own chassis, connected to utilities, and designed without a permanent foundation for year-round living." The standards adopted by the Alabama legislature are those of the American National Standards Institute, "which shall include standards for the installation of plumbing, heating, and electrical systems in mobile homes in ANSI A–119.1–1971 and NFPA No. 501–B–1971 entitled Standards for Mobile Homes." The State fire marshal, however, may adopt and promulgate any changes in and additions to these standards. No new mobile

[25] See note 1, supra.
[26] Va. Code §§ 36–70 et seq. (Supp. 1972).
[27] Id. at §36–81 (Supp. 1972).
[28] Id. at Title 25, §§ 124 et seq. (Supp. 1971).

home may be sold in Alabama unless it has been inspected and/or approved by the State fire marshal or his representative, his seal or approval has been permanently affixed to the new mobile home, and the manufacturer of the mobile home has certified that it meets or exceeds the uniform standards code.

Similar restrictions apply to the manufacture of mobile homes in Alabama. The code also makes provision for reciprocity with any other State which "has codes, to include construction and plumbing, heating, and electrical codes, at least equal to those established" in Alabama.[29] Violation of the code or the rules and regulations of the Alabama fire marshal made pursuant thereto is a misdemeanor punishable by up to a $500 fine and/or 6 months in jail.

On almost the same date in 1971 that it approved the code for mobile homes, Alabama enacted legislation concerning factory-built housing.[30] In this connection, the legislature found "that by minimizing the problems of standards and inspection procedures it is demonstrating its intention to encourage the reduction of housing construction costs and to make housing and home ownership more feasible for all residents of the state." For purposes of its act, factory-built housing "means any structure, or component thereof, designed primarily for residential occupancy which is wholly or in substantial part made, fabricated, formed, or assembled in manufacturing facilities for installation, or assembly and installation, on the building site. Mobile homes as defined by southern standard building codes are specifically excluded from the provision of this chapter."

As to factory-built housing, the rulemaking and enforcement is vested primarily in the hands of the Alabama development office, which is to impose "requirements reasonably consistent with recognized and accepted standards adopted by the Southern Building Codes Congress, the National Fire Protection Association, and the United States Department of Housing and Urban Development." An advisory committee on factory-built housing is to advise in the drafting of the rules. Six of the committee's members are to be appointed by the Governor from specified technical and professional disciplines; the remaining five, from the governing bodies of local governments. Factory-built housing is not to be offered for sale in Alabama unless it bears the Department's seal of approval, although under some circumstances inspection and approval by a local government agency may be a substitute for such approval. Also, the statute makes provision for acceptance of factory-built housing approved by another State whose standards are at least equal to those developed by Alabama. Not only is violation of this law or the rules promulgated thereunder a misdemeanor, but also the department can obtain injunctive relief against violations, and persons injured have a cause of action.

In 1970, Mississippi enacted the Uniform Standards Code for Factory Manufactured Movable Homes Act,[31] which applies to mobile and relocatable homes. The Mississippi Commissioner of Insurance is authorized to promulgate rules and regulations "embodying the fundamental principles adopted, recommended, or issued as USA Standard A119.1 and amended from time to time by the United States of America Standards Institute (USASI), successor to the American Standards Association (ASA) applicable to factory manufactured movable homes as defined herein." Compliance with the Commissioner's rules is required for the manufacture or sale of a factory manufactured movable home in Mississippi, and every manufacturer and dealer in Mississippi must obtain a license. In applying for this license, he must certify that he will comply with the construction standards. Basically, the licensing—and the possibility of revocation or suspension of a license—seems to be the chief means of enforcement of the act; no provision is made for testing and inspection of the mobile homes or the issuance of certificates of compliance. Reciprocity with other States is authorized, since the Commissioner of Insurance may exempt movable homes "produced in other States, upon his determining that the applicable rules and codes of such State of manufacture provide safeguards equally effective to those otherwise applicable under this act and rules made pursuant thereto." [32]

A 1971 West Virginia law, previously referred to, provides: [33]

> Notwithstanding any existing provisions of law, municipal or county ordinance, or local building code, but excluding any such provisions relating to zoning or land use control, the standards for factory-built housing, housing prototypes, subsystems, materials and components certified as acceptable by the Federal Department of Housing and Urban Development are hereby deemed acceptable and approved for use in housing construction in this State. A certificate from the State director of the Federal Housing Administration of the Department of Housing and Urban

[29] Id. at Title 25, § 130.
[30] Id. at Title 25, § 114 et seq. (Supp. 1971).

[31] Miss. Code Ann. §§ 5131–101 et seq. (Supp. 1972).
[32] Id. at § 5131–108 (Supp. 1972).
[33] W. Va. Code § 8–24–50a (1972).

Development shall constitute prima facie evidence that the products or materials listed therein are acceptable and such certificates shall be furnished by the building contractor to any local building inspector or other local housing authority upon request.

Although it was not one of the seven States studied, North Carolina offers an interesting comparison in connection with standards for mobile homes. For one thing, North Carolina has long had a form of statewide building code promulgated by a State Building Code Council.[34] Also, that State undertook to prescribe uniform standards for mobile homes in 1969,[35] before Virginia, Alabama, or Mississippi did so.

North Carolina provides that its Commissioner of Insurance shall promulgate "rules and regulations embodying the fundamental principles adopted, recommended, or issued as ANSI A–119.1 and amended from time to time by the American National Standards Institute (ANSI), successor to the American Standards Association (ASA) applicable to mobile homes as defined herein." A "label of compliance" with these rules may be issued for a mobile home by a qualified person who has been licensed by the State Building Code Council. Also, a "certificate of compliance" with these rules may be issued for a mobile home by a city or county building inspector who has been licensed for this purpose by the Council. However, the "certificate" is valid only within the jurisdiction of the city or county within which it was issued. No new mobile home is to be offered for sale in North Carolina unless it bears a label of compliance or certificate of compliance. Noncompliance with the act constitutes a misdemeanor.

As an additional means of enforcement, the North Carolina statute provides that, "it shall be unlawful for any individual natural person, partnership, firm or corporation to allow any electric current for use in any mobile home to be turned on or to continue to furnish electricity for use in such mobile home without having first ascertained that either a label of compliance is permanently attached to said mobile home or a certificate of compliance has been issued for such mobile home." [36] Apparently, North Carolina has no specific statutory provision for uniform standards as to factory-built housing, although it may be able to deal with that problem adequately through its statewide building code Nor has North Carolina a specific reciprocity provision with other States. Like Alabama and Mississippi, it adopts a specific set of national standards promulgated by the American National Standards Institute.

Since mobile homes and factory-built housing will often be an important housing resource in rural areas, legislation like that of Virginia, Alabama, Mississippi, and North Carolina would seem highly desirable for adoption in almost any jurisdiction. Indeed, some group like the National Conference of Commissioners on Uniform Laws might profitably consider the feasibility of uniform legislation in this field. Regardless of uniformity, reciprocity among those States which have mobile home standards—as is provided for by Alabama and Mississippi—would seem desirable.

Since factory-built housing presents some of the same problems involved in mobile home regulation, there is good reason to follow the example of Alabama and Virginia and provide for testing and labeling of factory-built units or components. As between the two States, the Virginia decision to have the same State agency regulate both mobile homes and industrialized building units seems more advantageous than Alabama's choice to have the State fire marshal prescribe rules for mobile homes, and another department regulate factory-built housing. Interestingly, Virginia, which now provides for a statewide building code, has entrusted the promulgation of this code to a different agency than that which is responsible for the mobile home and industrialized building standards. However, it would seem simpler administratively to entrust the promulgation of all of these regulations to the same agency.

Alabama, Mississippi, and North Carolina all have moved further towards the adoption of a specific, nationally recognized code for mobile homes than has Virginia—which has, however, embraced the concept of performance standards for mobile home construction and for building codes generally. If a State chooses to adopt a specific national code, it should, at least, seek to choose one that is oriented towards performance standards. Moreover, in order to obtain full benefit of research and development by the Department of Housing and Urban Development, a State might wish to follow the West Virginia precedent and authorize an exemption from State or local building codes for materials or components that have been approved by HUD. Alabama's factory-built housing legislation, which authorizes both injunctive relief and a civil cause of action for violations, as well as criminal sanctions,

[34] N.C. Gen. Stat. §§ 143–136 et seq. (1964).

[35] Id. at §§ 143–144 (Supp. 1971). The 1969 act was substantially amended in 1971.

[36] Id. at § 143–150 (Supp. 1971).

seems to provide an effective remedy. North Carolina's prohibition of an electrical connection for a noncomplying mobile home may be a very practical enforcement tool, but some public utilities might consider this an unreasonable burden on their operations.[37]

Transportation Regulations: Every State studied has limitations on the size of mobile homes that can be transported upon the State's highways—the maximum dimensions permitted generally being 8 feet in width, 13 feet in height, and 55 feet in length. Larger units, however, may be transported with special permission from specified State officials. None of the State statutes appeared to be unreasonably restrictive of the movement of mobile homes; and probably limitations on transportation are not a major barrier to the use of mobile homes in rural areas.

Taxes: Most of the States studied have a sales tax that is either expressly applicable to the sale of mobile homes, or impliedly because the mobile homes are considered personal property. While Virginia excludes mobile homes from application of the regular sales and use tax, they are subject to the Virginia Motor Vehicles Sales and Use Tax. At least four of the States have use taxes that appear applicable to mobile homes. Although generally a mobile home is treated as personal property, West Virginia and Mississippi use a different approach. In the former State, when the mobile home is owner-occupied and the owner also owns the land on which it rests, the mobile home is classified as real estate, whether or not the wheels have been removed. However, if the mobile home is owner-occupied and its owner does not own the land on which it rests, the home is considered personal property. Mississippi follows a similar approach, except that the mobile homeowner who owns the land has a choice of treating his mobile home as either personal or real property.

Tax Assessment

In some jurisdictions there is authority for low tax assessments or tax valuation formulas for certain favored uses. California, for example, allows agricultural land to be valued for tax purposes in terms of its farm use, even though it might have a higher market value if subdivided or otherwise developed. North Carolina has just adopted similar legislation. However, none of the seven States studied seem to vary from the "fair market value" approach to tax valuation. Thus, the tax valuation of rural housing cannot be maintained at an artificially low level.

Welfare Lien Laws

Welfare lien laws are not in vogue in the seven States studied. Only Kentucky has a general welfare lien statute, under which first-class cities which have paid general assistance to any person through that city's department of public welfare have a claim against his estate. This claim has priority over all unsecured claims against his estate, except for burial expenses, administration costs, expenses of his last illness, and claims by the Commonwealth for assistance rendered by it to the decedent. The lien is enforceable against all real estate and rights to real estate belonging to or thereafter acquired by a recipient of general assistance through the city's department of public welfare. In short, the supply of rural housing in the States studied is not impaired by welfare lien laws.

Repair or Demolition of Substandard or Dilapidated Housing

All seven of the States have statutes which under some circumstances give power to local authorities to repair or demolish substandard housing in slum areas. In some instances, this power is granted in connection with urban renewal or public housing legislation and thus is rather limited in scope. Arkansas provides that first-class cities have the power to order the removal or razing of buildings which have become dilapidated, unsightly, unsafe, unsanitary, or detrimental to the public welfare;[38] and Alabama specifically authorizes its incorporated municipalities to adopt and enforce ordinances regulating repair and maintenance of all buildings used for human occupancy, the number of occupants, and the mode and manner of occupancy, and to prohibit use and occupancy of buildings which do not comply with the requirements of such ordinances.[39] Such grants of power to certain municipal corporations may, by implication, raise a question as to the existence of like power to regulate substandard housing in rural areas outside the limits of any municipality.

Virginia grants local governments the authority to make improvements in slum areas and claim a lien on the property for the cost of the

[37] Even in North Carolina there may be some question about the legality of such a provision. see *Dale* v. *Morganton*, 270 N.C. 567, 155 S.E.2d 136 (1967).

[38] Ark. Stat. Ann. § 19-2803 (1968).

[39] Ala. Code, Title 37, § 785(1) & (2) (Supp. 1971).

improvements.[40] Also, in that State local authorities may close and demolish substandard buildings which an owner refuses to repair.[41]

Kentucky and Tennessee have the most extensive legislation in this field.[42] In almost identical terms the two States authorize city and county governments to adopt ordinances relating to structures which are unfit for human habitation. Under these ordinances, an appropriate public official gives notice to an owner and conducts a hearing on charges that his structure is unfit for human habitation. Then the official makes his findings of fact and issues an order requiring the owner to repair, improve, or alter the structure to make it fit for human habitation. If, however, the repair, improvement, or alteration will cost more than 50 percent of the value of the structure in Kentucky—or more than a "reasonable cost" in Tennessee—then the owner is ordered to remove or demolish the structure. If the owner refuses to comply, then the public official can take the appropriate action with respect to the structure, and the costs incurred in doing so are secured by a lien on the property.

None of the States studied makes express provision for the appointment of a receiver to take possession of substandard housing, collect the rents, and apply them to the cost of making repairs. Nor does any of these States provide for any special housing courts or tribunals to consider matters involving substandard housing.

Landlord and Tenant Law

In some jurisdictions, landlord and tenant law has provided an important incentive for the improvement of rental housing. As was recently commented in a Tentative Draft of the Second Restatement of the Law of Property:[43]

> The common law placed the risk on the tenant as to whether the condition of the leased property made it unsuitable for the use contemplated by the parties. In recent years, the definite judicial trend has been in the direction of increasing the responsibility of the landlord, in the absence of a valid contrary agreement, to provide the tenant with property in a condition suitable for the use contemplated by the parties. This judicial trend has been supported by the statutes that deal with this problem. This judicial and statutory trend is sound because it is more likely that safer and healthier rental property will be available under the view evidenced by the trend than under the old view.

[40] Va. Code § 15.1–11.2 (1970).
[41] W. Va. Code Ann. §§ 16–18–4, 16–18–5, & 16–18–8 (1972).
[42] Ky. Rev. Stat. §§ 80.620–80.720; Tenn. Code Ann. § 13–1203 (1955).
[43] Tentative Draft No. 1, Restatement of the Law Second, Property 167 (March 23, 1973).

At least 15 States allow a tenant to withhold or suspend rental payments under varying circumstances when the premises leased are defective or uninhabitable.[44] The Uniform Residential Landlord and Tenant Act, which in 1972 was promulgated by the National Conference of Commissioners on Uniform Laws, also gives relief to a tenant.[45] However, none of the seven States studied has any such provision in their law; and apparently a tenant is not entitled to withhold or suspend his rent payments or secure other relief for defects in the premises leased unless the defects reach the magnitude of a constructive eviction.

Indeed, for the most part there has been little change in the law of any of these States with respect to the landlord and tenant relationship. Kentucky,[46] Virginia,[47] and West Virginia,[48] however, have adopted civil rights legislation which, among other things, prohibits various types of discrimination in renting.

Fire Insurance

Among the seven States studied, Virginia alone seems to have adopted a program to make fire insurance available in substandard areas, where otherwise it might not be available. The Virginia program is limited to urban areas and specifically excludes property used for farming.[49] However, it might provide a model for a similar program in rural areas if fire insurance became unobtainable there at reasonable rates.

Under the Virginia plan, the property, which may include both real and personal property, must meet certain qualifications and must be in compliance with State laws and with local building codes and ordinances. Property meeting those qualifications is inspected by an inspection bureau created for that purpose. The authorized insurers in Virginia are to formulate and administer a program for the equitable distribution and placement of applications for fire and extended coverage insurance for qualified property. To implement the program, insurers are authorized to form a direct insurance association. If, however, the State Corporation Commission finds that the program devised by the insurers is failing to pro-

[44] Id. at 167–68.
[45] Uniform Residential Landlord and Tenant Act §§ 2.103, 2.104, 4.106 (1970).
[46] Ky. Rev. Stat. § 344.360 (Supp. 1972).
[47] Virginia Fair Housing Law, Va. Code §§36–86 et seq. (Supp. 1973).
[48] W. Va. Code Ann. § 5–11–9 (1971).
[49] Va. Code §§ 33.1–746 et seq. (1970). The Basic Property Insurance Inspection and Placement Plan and Joint Underwriting Association is the title given to the association to be formed.

vide adequate insurance for qualified property, the commission may order creation of a joint underwriting association. In that event, all insurers authorized to write fire and extended coverage in the State must become members of the association as a condition for doing business. That association will have the power to cause its members to issue policies to applicants, assume reinsurance from members, and cede reinsurance. The extent of participation of member insurers in the association shall be in proportion to the member's total yearly premiums.

Usury Laws

The seven States ranged from Arkansas and Tennessee, which have a maximum interest rate prescribed in their State constitutions, to Virginia, which sets no ceiling on the interest rates in first mortgages or deeds of trust on real estate.[50] In five of the States, loans insured through the Federal Housing Administration and the Veterans Administration are exempted from the State usury restrictions. Tennessee and Arkansas grant no such exemption. Thus, if interest rates on FHA or VA loans rise above the maximum rates permitted by the usury laws of those two States, such loans would be unfeasible. Virginia not only exempts VA and FHA loans, but also those which are insured by any other Federal agency or organization and loans made pursuant to the requirements of the Federal Home Loan Mortgage Corporation. This last exemption could be important in connection with loans by savings and loan associations. In Virginia, of course, this exemption would not be as important as it might be elsewhere, since usually a federally insured loan will be secured by a first mortgage or deed of trust on real estate—in which event it would not fall under the Virginia usury laws in the first place.

Both Kentucky and Alabama relax the usury limitations for loans that exceed a certain threshold—perhaps on the reasoning that a borrower of large amounts does not need the protection of usury statutes. Thus, Kentucky permits any specified rate of interest when the obligation exceeds \$25,000. In Alabama, when corporate borrowers are involved, the maximum permissible interest rate is 15 percent on any loan greater than \$10,000 but less than \$100,000; where other borrowers are involved and the loan exceeds \$100,000, the lender may charge as much as 15 percent. The special treatment of corporate borrowers also probably reflects a view that a corporation is not as needful of protection as is an individual.

For purposes of determining the interest ceiling, all seven States include discount points in interest. In at least six of the States, simple amortization is used to determine whether inclusion of discount points makes the interest rate usurious. The major difference among the States concerns the way in which each defines "points" for purposes of the usury statutes. In the majority—West Virginia, Virginia, Tennessee, Kentucky, and Mississippi—it seems clear that whatever points the lender receives are counted as interest for usury purposes. In Arkansas, however, it is uncertain from the most recent cases whether points received from sources other than the borrower are includible in interest under the usury laws. In Alabama, contrariwise, points must be paid by the borrower to be includible in interest insofar as usury is concerned. If a State does not exempt FHA and VA loans from its usual interest ceilings, its treatment of points for usury purposes may be especially significant, since FHA loans frequently involve a payment of points to the mortgage lender by the seller—but, of course, not directly by the borrower.

A time-price doctrine has been recognized in many States as an exception to the usury laws, apparently on a theory that a seller may set whatever terms he chooses for a credit sale and will not be deemed to have engaged in usury, even though his credit price exceeds the cash price by an amount producing a return far in excess of the interest usually allowable. This exception can be quite important in installment sales of realty or of mobile homes. Kentucky, Mississippi, Tennessee, Virginia, and West Virginia recognize the time-price exception to their usury laws. In Alabama, a time-price differential may be subject to the consumer finance law which limits the permissible rate of finance charges.

Arkansas, whose usury laws reflect a strong policy embodied in the State constitution, has also recognized the time-price doctrine. However, an Arkansas Supreme Court decision now limits the scope of the exception.[51] There, the

[50] Va. Code § 61–3191 (1973), which exempts first mortgages and deeds of trust on real estate from usury restrictions does not apply if the interest rate "varies in accordance with any exterior standard," or "cannot be ascertained from the contract without reference to any exterior circumstances or documents." Virginia does not apply its usury laws to corporations and certain other organizations. Id. at § 36.1–327 (1973).

[51] *Hare* v. *General Contract Purchase Corp.*, 220 Ark. 601, 249 S.W.2d 973 (1952).

court concluded that if a seller reasonably anticipated that the commercial paper resulting from a sale would be discounted and increased his sales price accordingly, then the transaction really constituted a loan by the lender who discounted the paper and so could be attacked as usurious. Some of the other States involved in the study might be willing to accept this Arkansas view if the issue were raised there.

Usury laws may be seen from at least two different standpoints—namely, either as a protection for the necessitous borrower against extortionate lenders or as an inhibition on the availability of capital. Obviously the seven States differ markedly in their perception of the relative importance of these two perspectives. Perhaps none of the others would be willing to follow Virginia in relying solely on competitive forces to maintain reasonable interest ceilings on first-mortgage real estate loans. Where FHA and VA loans are involved, however, the controls imposed by the Federal agencies should provide adequate protection, and there should be no need to invoke usury laws. Thus, to the extent permitted by applicable State constitutions, the legislature should make an exception to usury laws for FHA and VA loans. The exception probably should be broadly stated to include other types of loans which have elements of Federal supervision—such as those loans committed by savings and loan associations to the Federal Home Loan Mortgage Corporation.[52] At the very least, the wording of any exception should be carefully studied to assure that it clearly extends to all those types of loans that fall within the policy of the exception. After all, lenders are usually conservative; an exception, to be of value, should leave no uncertainty as to its scope.

If the policy of the usury laws is accepted at all, the time-price doctrine provides an enormous loophole that probably cannot be justified solely in terms of the view that a seller may set his own price. Where a seller—like so many—is regularly engaged in discounting the commercial paper resulting from his sales transactions and has adjusted his time-price accordingly, there is a good basis for adopting the Arkansas view that usury laws apply. At the very least, legislatures might well express their own intent concerning the applicability of the time-price exception to such transactions.

Whether a corporation—especially a small corporation—is so different from an individual person that it should automatically fall outside the usury laws in whole or in part might also be questioned. Certainly where a loan to an individual is disguised by having him form a corporation and apply for the loan in the corporate name, there is considerable reason to apply the usury laws—unless, of course, the basic philosophy of those laws is rejected from the outset.

Lending Institutions

Often the terms of usury laws are less significant to a borrower than the availability of financial institutions to make loans. One factor that affects this availability is the presence or absence of branch banking in the State. The seven States studied fall into three categories: (1) Branch banking not allowed; (2) branch banking allowed if certain requirements are met and there is approval by appropriate State officials; and (3) branch banking allowed automatically if certain conditions are met. Only West Virginia fits in the first category; it prohibits all types of branch banks and engagement in business at any other place besides the principal office.

In the second and largest category are Kentucky, Mississippi, Tennessee, and Virginia. Virginia provides that the State Corporation Commission, when satisfied that the public convenience and necessity will be served, may authorize banks having unimpaired capital of a certain amount to establish branches within the limits of the city or county in which the parent bank is located, or to establish branches elsewhere by merger with banks located in another city or county. (This merger provision appears to be unique to Virginia among the States studied.) Kentucky's law is similar, except that: (a) The Commissioner of Banking must find that there is a reasonable probability of successful operation of the branch, as well as that it would be in the public interest to establish it; (b) there must not be another existing bank in the area; and (c) there is no provision allowing branches outside the city or county of the principal office. Mississippi's approach is different. It uses a noncounty radial measurement; and a branch may be authorized within 100 miles of the principal office. However, the parent bank must first obtain from the State Comptroller, Attorney General, and Governor, or a majority thereof, a certificate that public convenience and necessity will be promoted by establishment of such a bank. Tennessee law authorizes the Superintendent of Bank-

[52] Virginia has a clear exemption from usury statutes for any loan "made pursuant to the requirements of the Federal Home Loan Mortgage Corporation." Va. Code § 6.1-328 (1973). No other State studied provided a corresponding exemption.

ing to approve branch offices; but no branch may be set up outside the county where the principal office is located.

In the last category are Arkansas and Alabama. A bank in Arkansas may establish a branch if several requirements are met—namely, that the branch is within the county where the main office is located, that there is no other chartered bank within a certain distance from the branch, and that the bank has specified capital. In Alabama, the prohibition against branch banking does not apply if branch banking has been authorized in the county or if that county had a population of 200,000 persons or more in the last national census.[53]

In short, five of the seven States do not allow branch banking beyond the limits of the county where the bank's principal office is located. Virginia permits it in connection with certain mergers, while only Mississippi seems to allow it rather generally. Thus, in the area studied branch banking does not play a major role in the availability of funds for rural housing.

There is a wide range of State positions concerning jurisdictional limits on lending by State-chartered savings and loan associations. On the one hand, Kentucky, Tennessee, and West Virginia do not limit the lending area; on the other, Virginia provides that the borrower must be within the State. On middle ground are Alabama, which provides for a geographical limitation—within 50 miles of the home office of the association but not limited by the State boundaries—and Mississippi, which generally limits loans to an in-State borrower but provides that exceptions may be made. As to Arkansas, the question does not seem to be clearly covered by the State statutes.

For federally chartered savings and loan associations, the loan radius is 100 miles and may include other States.[54] While the 100-mile loan radius also applies to branch offices, the loan must then be within the State. A Federal savings and loan association which has been converted from a State-chartered association may also continue to make loans in the area which it previously served.[55]

In two of the States, Arkansas and Alabama, a bank may make loans secured by a mortgage on real estate without statutory limitations or directions other than those relating to loans in general. The other States, however, have more specific limitations on real estate loans, the most common concerning the maximum period during which property may be held. Four States have a time limitation of 5 or 10 years on the retention of real estate which is conveyed to a bank in satisfaction of a borrower's debts or is purchased at a judgment sale; but the period may be extended by an appropriate official. Kentucky has an absolute maximum of 10 years.

All seven States limit the percentage of the capital assets which a bank can lend to any one person or entity; and all provide for exceptions to that limitation. Kentucky provides that its normal 20 percent limitation is not binding if a borrower pledges good collateral with the bank or executes a mortgage upon real estate as security for the loan; in that event, the limitation is 30 percent. Tennessee allows a borrower to obtain more than the normal maximum of 15 percent of the bank's capital assets—up to 25 percent—if each specific loan in a higher amount is approved in advance by the board of directors or by the finance committee of the bank. In all of the States, the loan limitation does not apply to loans to certain governmental units; and three of the States include both municipalities and counties among the government units exempted from the loan limitation. Also, Arkansas specifically includes housing authorities among the entities to which a bank's loan limitation does not apply.

Because the restrictions on branch banking in the seven States would tend to prevent the growth of very large banks, the loan limitations would probably be of more significance than in jurisdictions where branch banking flourishes. Regardless of loan limitations, however, it is not likely that a bank would lend a very substantial portion of its assets to a single borrower to develop and construct rural housing. Of course, where the loan limits do present a problem in financing a particular transaction, a bank may seek to obtain participation in the loan by other banks.

All but one of the States require that every real estate loan of a savings and loan (or building and loan) association be secured by a mortgage or other instrument constituting a first lien upon the real estate securing the loan. If the association itself already holds a prior lien, then additional or supplementary advances secured by a second mortgage would be considered equivalent to a first lien for purposes of these

[53] See *Security Trust & Savings Bank* v. *Marion County Bank Co.*, 253 So. 2d 17 (1971), where the Alabama Supreme Court reaffirmed that travel banking could only be conducted countywide.
[54] 12 C.F.R. 545.6–6 (1973).
[55] Id.

loan requirements. Probably a "wraparound mortgage" would not qualify as a first lien for purposes of these statutes, although the statutes do not deal specifically with the question.[56] West Virginia apparently does not require by statute that a savings and loan obtain a first lien to secure its loan.

Several States provide that a real estate loan by a savings and loan association is not to exceed a certain proportion of the value of the real estate. In Tennessee, the loan is not to exceed two-thirds of the value of the real estate, as determined by the board of directors of the savings and loan association; however, this limitation does not apply to mortgage loans insured by the Federal Housing Administration. In West Virginia, the percentage requirement on a real estate loan by a savings and loan association is 95 percent, with an exception for loans insured or guaranteed by the Federal Government. Virginia's ceiling is based not only on percentage but also on actual monetary value. Except as otherwise provided in the statutes, no real estate loan can exceed $45,000 on each home or 90 percent of the value of the real estate up to $50,000. As in the case of Tennessee and West Virginia, there is an exception to these limitations for loans insured or guaranteed by a Federal agency.

None of the seven States has express statutory provisions either permitting or prohibiting "flexible" or "open-end" mortgages or deeds of trust on real estate. Alabama, however, does permit open-end credit plans and, by analogy, might therefore be receptive to open-end mortgages.

Health and Safety Regulations

All seven States attempt in some ways to regulate the building industry for the general purpose of public health and safety. The applicable regulations may be found in the health and safety statutes of some States and in the professional and occupational statutes of others. For the most part, the States have delegated to municipal and often to county governments the authority to establish building and housing codes and to regulate contractors, plumbers, and electricians. None of the States has enacted a statewide minimum housing code, although the authority to enact such codes is frequently vested in municipalities.

Five States have promulgated some type of statewide fire code or have authorized a State fire marshal to do so. Arkansas and Mississippi have no statewide guidelines, but clearly authorize municipalities to enact and enforce their own codes. Arkansas has a uniform plumbing code administered by the State health department.

All seven States have legislation concerning installation of water and waste systems; but, except for Tennessee, these statutes have little relation to lot size. As with health laws generally, regulatory responsibilities are primarily entrusted to local health boards and sanitation districts, subject only to general regulations of State health departments and performance standards imposed by State environmental and natural resources commissions.

In Tennessee, lot size requirements and their relationship to public water supplies are expressly dealt with by statute. When public water is available, the minimum lot size is 7,500 square feet; otherwise, it is 15,000 square feet. Additional lot sizes may be required when percolation tests indicate that the soil will not absorb the sewage.[57]

In Alabama, where regulation of water and waste systems is left largely in the hands of county health boards, these boards may require installation of plumbing facilities conforming to the rules of the State board of health and also may require connections to sanitary sewers where deemed necessary.[58] Issuance of permits for installation of plumbing in structures outside the jurisdiction of a municipality depends on meeting statewide requirements, and inspection is done by the county health boards. Also, in Alabama, water authorities may be created on a countywide basis and so, often, are water suppliers for rural dwellings.

In Kentucky, the Department of Environmental Protection is chiefly responsible for water and waste system control; but responsibility is shared locally with sanitation districts. Once a sanitation district is established in Kentucky, no person or public corporation may install within the district any laterals, trunk lines, interceptors for the collection or discharge of sewage or other liquid waste, treatment or disposal works, until such plans have been submitted and ap-

[56] The "wrap-around mortgage" is discussed in Gunning, *The Wrap-around Mortgage . . . Friend or U.F.O.?, 2 Real Estate Review* 5 (No. 2 1972). Note, *Wrap-around Financing: A Technique for Skirting the Usury Laws?*, 1972 *Duke L.J.* 785.

[57] See Tenn. Code Ann. § 53–2012 (1966), repealed as of July 1, 1973 by a new act adopted on May 22, 1973, chapter no. 188, Public Acts of 1973.

[58] Ala. Code, Title 22, § 140(14) (Supp. 1971).

proved by the board of directors of the sanitation district and by the Department of Environmental Protection.[59] Similarly, in Tennessee, no person may install, permit to be installed, or maintain any cross-connection, auxiliary intake, bypass, or interconnection, unless the source and quality of water from the auxiliary supply, method of connection, auxiliary intake, bypass, or interconnection has been approved by the State department of public health.[60] In Virginia, any person constructing a sewage system or water supply system having three or more connections must first obtain the approval of the county's governing body.

In their subdivision control legislation, both Virginia and Tennessee specifically deal with water supply and waste disposal. In Virginia, the county board of supervisors may require a subdivider or land developer to pay a pro rata share of the cost of providing reasonable and necessary sewage and drainage located outside the property limits of the developer but necessitated at least in part by the construction or improvement of his property.[61] This sort of regulation is not unusual; similar regulations probably exist frequently at the local level in the other States in the form of subdivision controls and zoning ordinances.

On May 22, 1973, Tennessee adopted new legislation regulating subsurface sewage disposal systems and subdivisions using such systems.[62] For these purposes a subdivision need consist only of two building lots. The Tennessee Commissioner of Public Health is to supervise the systems and establish standards for them. No county register shall file a subdivision plan that has not been approved by the Commissioner or local health authorities; and construction of a house without approval of the subsurface sewage disposal systems is forbidden.

All seven States have enacted some environmental protection laws—usually establishing a single umbrella agency but in some cases creating separate commissions to deal independently with air and water pollution. The primary thrust of both the water and air pollution control statutes is to establish minimum standards for purity of the State's water and air resources. Most of these acts are concerned with discharges, directly or indirectly, into the State's water and air. Their effect on rural housing would seem relatively minor, except that compliance will involve additional development costs that ultimately will be passed along to the homebuyer or tenant.

Perhaps the most important comment to be made about the environmental protection laws of the seven States is that none of them has any requirement for environmental impact statements remotely comparable to that imposed by the new California Environmental Quality Act, which is drastically affecting the construction industry in that State.

Of course, direct governmental regulation is not the only way in which environmental requirements are given effect. Lenders can impose requirements—for example, concerning waste and water systems—as a condition for making loans. Undoubtedly, government agencies like FHA, VA, and the Farmers Home Administration, which are involved in providing credit for home construction, will be increasingly concerned with the environmental features of the housing for which they furnish assistance. In the seven States studied, the requirements of these agencies may well have more effect on rural housing than the environmental regulations of State and local agencies.

Federal Programs and Restrictions

Several of the sections of this report concern some of the Federal laws and regulations that might be relevant to rural housing—such as the laws regulating real estate loans by federally chartered savings and loan associations, Federal laws governing real estate loans by national banks, and the provisions governing the availability of FHA mortgage insurance. No attempt will be made here to analyze these different provisions. Nor does the report discuss the regulations of the Farmers Homes Administration, as set forth in 7 C.F.R. 1800.1 et seq. Instead, the goal of this Report is to identify the provisions of State law in the jurisdictions studied which may either aid or hinder the effort to provide a more adequate supply of decent, safe, and sanitary rural housing.

Conclusion

Among the States studied, several have recently made some significant advances toward improving the housing supply—both rural and

[59] Ky. Rev. Stat. § 220.260 (1969).
[60] Tenn. Code Ann. § 53–2004 (1966).
[61] Va. Code Ann. §§ 15.1–326, 15.1–341.
[62] Chapter No. 188, Public Acts of 1973, enacted May 22, 1973 and effective July 1, 1973, which repeals and replaces Tenn. Code Ann. §§ 53–2009–53–2016.

urban. The formation of statewide housing development corporations, which can provide loans, mortgage insurance, and technical assistance is one such step forward. Another is the provision for a statewide building code in Virginia and the enactment of legislation leading to the formulation of uniform standards for mobile homes and factory-built housing. Civil rights legislation in three of the States will help assure that the existing housing supply will be made available on a nondiscriminatory basis. The usury laws in the States reflect a wide diversity of goals, but at least five of the States contain a specific exemption for FHA and VA approved loans.

Perhaps these suggestions can be safely made on the basis of the study that has been conducted:

1. Legislation modeled on that of Virginia and Kentucky should be adopted by other States to provide assistance in meeting housing needs;

2. A statewide building code should be authorized, as Virginia has recently done;

3. Such a building code should be based on performance standards, perhaps by adoption of a suitable nationally recognized code;

4. State legislation should also be adopted to provide uniform standards for mobile homes and factory-built housing; the standards should be of a performance nature and should be enforced by testing organizations authorized to issue certificates of compliance;

5. Wherever possible, reciprocity among States should be provided in the administration of the uniform standards for mobile homes and factory-built housing;

6. Legislation like that of West Virginia should be adopted to assure that local building codes do not exclude materials and methods that have been approved by the Federal Department of Housing and Urban Development;

7. To whatever extent local building codes are permitted, there should be a law, as in Mississippi, which precludes local governments from imposing requirements that have no precedent in any nationally recognized codes;

8. To whatever extent usury laws exist, specific exceptions should be made for loans that are insured or guaranteed by FHA, VA, or any similar Federal instrumentality;

9. Consideration should be given to providing, as Virginia has done, for a clear usury exemption for loans which are made in accord with the requirements of the Federal Home Loan Mortgage Corporation;

10. State usury laws should be reexamined to determine whether exceptions for corporate loans or time-price transactions should be allowed to continue;

11. Housing authorities should consider greater use of existing statutory authority to construct public housing in rural areas;

12. Legislation should be adopted in those States where it does not exist to provide explicit authority for governmental authorities to repair or demolish substandard buildings and impose a lien on the real estate for the expense of the repairs or demolition;

13. A program, modeled on Viriginia's plan for substandard urban areas, should be authorized to provide fire and extended coverage insurance at reasonable cost in any rural areas where such insurance otherwise is unavailable;

14. Existing restrictions in States which prohibit branch banking beyond the county where the bank's principal office is located should be reexamined to determine if some other limitation —such as the radial measure used in Mississippi —might be desirable;

15. The need to enact State fair-housing legislation, like that of Virginia, Kentucky, and West Virginia, should be considered;

16. State laws—like that adopted by Tennessee in May 1973—should be enacted to assure that new subdivisions have adequate underground sewage disposal systems.

Obviously there are other fundamental changes that might deserve consideration. For instance, the hostility to branch banking that seems to pervade the States studied should perhaps be reexamined in light of possible needs for larger banking institutions with access to greater loanable funds and with more diversified financial services. And Virginia's experience with an exemption from usury laws for first mortgage loans on real estate should be studied. In any event, by its comparison of the existing laws pertinent to rural housing in the seven States, this report may suggest some new legislative solutions for several old problems of rural housing.

Summary

Among the seven States studied, several have recently taken important steps to meet housing needs. Statewide housing development corporations have been created as government instrumentalities and, with funds raised from revenue bonds and otherwise, will provide technical assistance, loan funds, and mortgage insurance in some instances. Statewide building codes are beginning to emerge—especially with respect to mobile homes and factory-built housing. Fortunately, there seems to be a willingness to utilize performance standards to preclude local governments from barring the use of new materials and components that have gained national acceptance.

None of the States has a statewide housing code, but local governments have been delegated considerable power to deal with substandard housing. In some States, a substandard structure may be repaired or demolished and the cost thereof becomes a lien against the land. None of the States has authorized tenants to withhold or suspend rent payments because of defects in the premises leased; and generally the law of landlord and tenant has been left untouched in all of the States studied. In three States, however, civil rights legislation impinges on the landlord's traditional discretion to select his tenant.

The States vary in their policy towards usury, although five of them contain an express exception for FHA and VA loans. Virginia has enacted several major exemptions from the usury laws, such as those for first mortgage loans on real estate and for corporate loans. Arkansas, on the other hand, has by judicial decision restricted the time-price doctrine which has long constituted an implied exception to usury statutes.

All of the states have prohibitions or severe limitations on branch banking. They have a variety of limitations on loans that can be made by banks. Similarly, the treatment of savings and loan associations differs markedly from one State to another.

In the promulgation of health and safety regulations, considerable authority has been delegated to local governments. Some States, however, have legislated at the State level to deal with health problems, as Tennessee did on May 22, 1973, when it enacted a new law concerning subdivisions and their underground sewage disposal systems. Up to the present, however, the environmental protection efforts in the States studied have not been sweeping in their coverage or effects.

Alabama Report on Legislation

Land Use Controls

The Alabama State Planning Board was created in 1943 to design a master plan for the development of the State.[1] The board is to cooperate with the planning authorities of counties, municipalities, and neighboring States in coordinating developments and studying planning problems.[2] Areas the board is to consider are the location of open areas for conservation purposes, food and water supply, sanitary and drainage facilities, and the protection of rural and urban development.[3] While the board has no power to effectuate changes, it may submit to the Governor and the legislature drafts of legislation including zoning and land use regulations.[4] The board is also allowed to contract with individuals, corporations, private associations, chambers of commerce, etc., so far as its funds permit to promote its plans or to make more thorough studies and recommendations.[5]

The legislature also allowed the creation of city and regional planning commissions. A municipality may adopt a plan and create a commission to effectuate it.[6] Everything relating to the general development of the area is entrusted to the commission.[7] The commission has all power previously granted to zoning commissions,[8] as well as power over subdivision control.[9] A plan for a proposed subdivision must be submitted to the commission to assure that it meets their standards on streets, open spaces, minimum width and area of lots, and water and sewage facilities.[10] The commission also has power to regulate all public buildings and structures,[11] presumably including public housing projects.

Although the municipal planning commission can include in its plan the outlying areas that affect it,[12] there is no local body specially established to plan for the entire county. Both the municipal planners and the county commissioners can apply to the Governor for the creation of a regional planning commission.[13] This commis-

[1] Code of Ala. Tit. 55 § 373(4) (1960).
[2] Ibid., § 373(5) (1960).
[3] Ibid., § 373(4) (1960).
[4] Ibid., § 373(5) (1960).
[5] Id.
[6] Code of Ala. Tit. 37 § 787 (1960)
[7] Ibid., § 791 (1960).
[8] Ibid., § 796 (1960).
[9] Ibid., § 798 (1960).
[10] Ibid., §§ 798–799 (1960).
[11] Ibid., § 794 (1960).
[12] Ibid., § 791 (1960).
[13] Ibid., § 809 (1960).

sion was empowered to adopt a master regional plan and the protection of future urban developments.[14] The commission is apparently intended to control counties where urban growth has spread beyond the limits of the municipality rather than the counties where there are no plans for outlying rural areas.

In 1969, Alabama reorganized its regional planning structure. It allowed for the formation of regional planning and development commissions covering areas of at least three contiguous counties and a population of at least 100,000, upon the petition of local governmental units.[15] All previously established regional planning commissions were allowed to remain certified as meeting the new requirements for no more than 2 years.[16] Apparently, in 1971 all regional planning commissions for areas less than three counties or 100,000 people ceased to exist, and new commissions covering larger areas were to replace them.

The new commissions are to carry on planning activities, prepare a regional plan consistent with State plans setting forth policies for development, prepare an annual regional development program to implement policies, provide assistance to governmental units, borrow money, review local applications for State and Federal loans, acquire and dispose of real property, et al.[17] The newly organized agencies seem to have broader powers, and may be better equipped to deal with rural areas and to include them in comprehensive planning.

In 1963, the governing bodies of two or more counties or municipalities were empowered to create advisory regional planning commissions.[18] These commissions have no power to control zoning or land use [19] but are to provide comprehensive advisory planning and planning assistance to counties, communities, planning agencies, etc.[20]

In one special area the State does allow county governments the same regulatory powers normally granted to municipalities. A flood-prone area is one where the frequency of inundation by streams, rivers, tidal waters, or rising coastal waters is at least once in every hundred years.[21] In these areas, the county may adopt zoning ordinances and building codes for lands outside municipal limits.[22] The county may also establish comprehensive land use and control measures, control the development of subdivisions, and establish building codes and health regulations to minimize potential flood damage.[23]

In 1969, the Alabama Development Office was created, to be under the direct supervision of the Governor.[24] The Office is to provide overall State planning guidance for long term comprehensive plans. The Office seems primarily concerned with economic and industrial development.[25] These plans will obviously have some effect on housing supply and development in rural areas, but this does not appear to be the main function of the Office.

Regulations Governing the Use of Mobile Homes

Alabama passed the Uniform Standards Code for Mobile Homes Act in September 1971. It adopted the American National Standards Institute code for minimum standards of plumbing, heat producing, and electrical systems and equipment.[26] Compliance with the code is now a condition precedent to the sale of any new mobile home in the State.[27] The State fire marshal inspects the homes either where manufactured or sold [28] and affixes a seal of approval and issues certification if the standards are met.[29] Alabama will honor a seal of approval from any other State with standards as high as or higher than its own.[30]

There is no problem with the transportation of mobile homes on Alabama highways. House trailers, not exceeding a total width of 12 feet and overall length, including the towing vehicle and trailer, not exceeding 75 feet, may be moved on any highway, except for highways which are part of the interstate system, during the hours of daylight any day of the week. No permit is required.[31]

Usury Laws

Alabama's general usury statute provides that a borrower, pursuant to a written contract

[14] Ibid., § 811 (1960).
[15] Ibid., § 814(8) (1971 Supp.).
[16] Ibid., § 814(14) (1971 Supp.).
[17] Ibid., § 814(10) (1971 Supp.).
[18] Ibid., § 814(2) (1971 Supp.).
[19] Ibid., § 814(1) (1971 Supp.).
[20] Ibid., § 814(4) (1971 Supp.).
[21] Code of Ala. Tit. 12 § 341 (1960).

[22] Ibid., § 343 (1960).
[23] Id.
[24] Code of Ala. Tit. 55 § 373(6e2) (1971 Supp.).
[25] Ibid., §§ 373(6e1) 373(6e5) (1971 Supp.).
[26] Code of Ala. Tit. 25 § 126 (1971 Supp.).
[27] Ibid., § 127 (1971 Supp.).
[28] Ibid., § 131 (1971 Supp.).
[29] Ibid., § 128 (1971 Supp.).
[30] Ibid., § 130 (1971 Supp.).
[31] Code of Ala. Tit. 36 § 91(1) (1971 Supp.).

may agree to pay an interest rate of up to 8 percent a year.[32]

However, when the lender "regularly extend[s], or arrange[s] for the extension of credit for which the payment of a finance charge is required," the Alabama Consumer Credit Transaction Law of 1971 [the Consumer Finance Law] becomes effective.[33] But the Consumer Finance Law does not repeal or modify certain other relevant statutes, including Code of Ala. Tit. 9 §67(1), which provides that corporations may agree to pay an unregulated interest rate on loans having an original principal balance in excess of $100,000, and up to 15 percent a year on loans with an original balance of from $10,000 to $100,000. The provisions of Code of Ala. Tit. 9 §67(2) and 67(4), taken together, mean that debtors other than corporations may, depending on their classification, agree to pay interest at a rate up to 15 percent a year, or at an unregulated rate for loans over $100,000.

Code of Ala. Tit. 9 §67(3) exempts all debts incurred under the National Housing Act or any act of Congress relating to veteran's benefits from any Alabama usury law.

The Consumer Finance Law establishes maximum finance charges for loan transactions except under open-end credit plans.[34] The charge may equal but not exceed:

(a) (i) 15 percent a year for the first $500 of original principle amount, (ii) 10 percent a year for the amount over $500, but not exceeding $1,000, (iii) 8 percent a year for portion over $1,000 but less than $2,000 or,

(b) if the original amount of the loan exceeds $2,000, 8 percent of amount financed.

"Finance charge" shall include all charges payable directly or indirectly by the debtor and imposed directly or indirectly by the creditor as an incident to the extension of credit, including interest, time-price differential, points or discount paid directly by the debtor, service, carrying or other charge (however denominated), loan fee, credit or investigation fee; but not including permissible attorneys' fees, court costs, and official fees and taxes, points or discounts paid by someone other than the debtor, or premiums for permissible insurance as provided by this chapter.[35]

[32] Code of Ala. Tit. 9 § 60 (1960).
[33] Code of Ala. Tit. 5 §§ 316–341 (1971 Supp.).
[34] Ibid. § 317 (1971 Supp.).
[35] Ibid., § 316 (1971 Supp.).

Thus, points and discounts paid by the debtor are expressly included in the definition of a finance charge. But Code of Ala. Tit. 5 §316(a) expressly excludes "points or discounts paid by someone other than the debtor." It further provides that, "For the purpose of determining the permissible finance charge, any discount or point paid by the debtor in connection with a mortgage loan or real estate, even though paid at the time, shall be spread over the stated term of the loan . . ." [36] There is no apparent authority regarding the period over which the other "one time" charges may be amortized.

The Alabama Small Loans Act regulates loans of up to $300; the act is meant to reach small loan finance companies only, for it exempts "any person doing business under the authority of . . . any law of this State or of the United States relating to banks, savings banks, trust companies, savings or building and loan associations, credit unions, . . . [and] bona fide pawnbroking business(es)." [37] Licensees under the act may lend at a rate of 3 percent per month for the first $200, and 2 percent per month on the amount over $200 but not exceeding $300. A charge of $1 for every $5 may be made on loans of up to $75, although 15 days must be allowed for the repayment of each $5.[38] The act provides that no further charges may be made directly or indirectly.[39]

Regulations Affecting Home Building Construction Industry

Alabama requires that any structure or component designed for residential occupancy fabricated or assembled for installation on a building site meet certain standards. All such homes must bear an insignia of approval. These may be procured in several ways. The Alabama Development Office may inspect and issue them.[40] Or, if the local government inspects at the place of manufacture and finds the housing meets local building requirements in conformity with the Southern Building Codes Congress, National Fire Protection Association and HUD, then the housing will be approved.[41] Also, if housing has been approved by another State with reasonably consistent standards, approval will be given.[42]

[36] Code of Ala. Tit. 5 § 316(a) (1971 Supp.).
[37] Ibid., § 279(b) (1971 Supp.).
[38] Ibid., § 290(2) (1971 Supp.).
[39] Ibid., § 290(8) (1971 Supp.).
[40] Code of Ala. Tit. 25 § 116(a)(2) (1971 Supp.).
[41] Ibid., § 116(a)(3) (1971 Supp.).
[42] Ibid., § 118 (1971 Supp.).

Laws Enabling the Establishment of State Housing Corporations

There are no Alabama statutes enabling the establishment of a State housing corporation.

Laws Affecting the Operation of Banks and Savings and Loan Associations in the Home Mortgage Field

The operation of savings and loan associations in the home mortgage field is regulated by Code of Ala. Tit. 5 §§231, 232. Once a real estate loan is approved by the board of directors, a note for the amount is issued, stating all the terms. Every real estate loan must be secured by a mortgage constituting a first lien on the real estate securing the loan. This provides for full protection of the association with respect to the usual insurance risks, taxes, assessments, other government levies, and maintenance and repairs. The mortgages must be recorded, and no subsequent loan can establish an intervening lien. Payments by the debtor are applied first to the interest on the unpaid balance, then to the reduction of the loan. The association may pay taxes, assessments, insurance premiums, etc., for the protection of the loan and add the amounts to the unpaid balance. In addition, the association may require life insurance to be assigned as additional collateral on any real estate loan, and may require the borrower to pay the monthly equivalent of one-twelfth of annual charges to enable the association to pay its expenses.

Real estate loans may be prepaid at any time, and the association may not charge more than 1.5 percent of the amount of the anticipatory payment.

The exact rate for charges is not set in the statute. It provides that the association may require borrowing members to pay all reasonable expenses incurred in connection with the loan, and also for all necessary and incidental services rendered by it.

§232 provides that the association shall have a lien on all accounts owned by the borrower in order to secure the loan. On default on the loan, it may, without notice, cancel on its books all accounts and apply the amount to the payment of the loan.

Health Laws and Regulations as They Affect Safe and Sanitary Housing

There are apparently no health laws and regulations in Alabama that affect the supply of safe and sanitary housing.

Water and Waste Systems

The Alabama Water Quality Criteria Act, adopted in 1967, set out basic statewide waste treatment requirements. It required that all sewage discharged into State waters used as sources of public water supply or used for swimming or whole body water-contact activities receive a minimum of secondary treatment, and disinfection if necessary.[43] "Secondary treatment" is interpreted to mean "a process or group of processes capable of removing virtually all floating and settleable solids, from 75 to 95 percent of the five day biochemical oxygen demand and in excess of 75 percent of suspended solids contained in untreated sewage."[44]

Additionally, the State board of health and county boards of health are to oversee local sewage collection facilities and plumbing systems.[45] It is a misdemeanor to build or use unsanitary facilities or those likely to become a menace to public health.[46] The boards of health are to require the installation of plumbing in structures outside the jurisdiction of a municipality in a manner that conforms to the rules and regulations of the State board and/or county boards,[47] and inspection is to be done by the county boards.[48]

Much power is delegated to the municipalities to establish their own standards for sewer systems, and to construct and operate them. These systems may be constructed and maintained within and outside of corporations.[49] Also, whenever it is necessary or expedient, any city or town may extend its sewer mains to any point in its county,[50] so that city facilities could conceivably be extended to serve rural areas.

Other powers are delegated to cities with respect to areas within corporate limits. Cities may prescribe the manner of construction of plumbing facilities as well as prescribe the manner of drainage from private premises.[51] They may regulate the construction of privies and water closets, and compel connection with septic tanks.[52] If the owner fails to make the connec-

[43] Act No. 574, Acts of Alabama 1965.
[44] Id.
[45] Code of Ala. Tit. 22 § 140(14) (1971 Supp.).
[46] Ibid., § 140(3) (1971 Supp.).
[47] Ibid., § 140(14) (1971 Supp.).
[48] Ibid., § 140(18) (1971 Supp.).
[49] Code of Ala. Tit. 37 § 601 (1960).
[50] Ibid., § 603 (1960).
[51] Ibid., §§ 604, 605 (1960).
[52] Ibid., § 606 (1960).

tions, the city may make it and assess the expense against the property. Cities also have the power to forbid altogether the use of sinks, pits, cesspools, and dry wells.[53]

Water authorities may be organized as public corporations under the governing body of the county or counties they propose to service.[54] The authority is empowered to plan and operate water systems, sewer systems, and fire protection facilities at fixed rates.[55] Since the water authority is operated on a countywide basis, it may often be the source of water supply for rural dwellings.

The Solid Wastes Disposal Act authorizes the county governing body to make available to the general public collection and disposal facilities for solid wastes with either house-to-house services or placement of receptacles within a reasonable (less than 8 miles) distance from the farthest affected house.[56] An individual homeowner may file a certificate of exception setting out his own proposed method, which must comply with sanitation requirements and not create a public nuisance or hazard to health.[57] If the application is granted, the owner may store, haul, or dispose of his own solid wastes on his own land.

Environmental Protection Laws

The Environmental Improvement Authorities Act, passed in 1969, contained no provisions that directly affect housing supply. The act enabled established public corporations to undertake studies of water, air, and general environmental pollution, to construct, operate or lease equipment to control or prevent such pollution, and to lend financial assistance to municipalities, counties, and other groups.[58] While such corporations might at some time sponsor legislation to restrict land use for housing purposes, the act itself does nothing like this. The act itself declares that it is supplemental to the powers conferred on boards of water and sewer commissions created by municipalities. These may not operate to restrict the corporation's power, for it is independent of them. However, the corporation is intended to work in conjunction with the local authorities who have the power to legislate concerning water and sewer systems, and to zone the land for the safest uses environmentally.

53 Ibid., § 605 (1960).
54 Code of Ala. Tit. 50 § 101 (1971 Supp.).
55 Ibid., § 105 (1971 Supp.).
56 Code of Ala. Tit. 22 §347(a) (1971 Supp.).
57 Ibid., § 347(e) (1971 Supp.).
58 Code of Ala. Tit. 8 §§ 272, 277 (1971 Supp.).

Welfare Laws

There is no welfare lien law in Alabama. Welfare is paid in four categories—blind assistance, old age assistance, aid to dependent children, and aid to the permanently and totally disabled.[59] To qualify, one must show that he has no sufficient income and resources from all sources to provide reasonable subsistence, and that he has not directly or indirectly disposed or deprived himself of property for the purpose of qualifying for the benefits.[60] The State department of welfare establishes uniform standards of need and rules and regulations for distribution of funds.[61]

All amounts paid or payable as public assistance are tax-exempt, and exempt from levy, garnishment, attachment, and any other process.[62]

Taxation

Alabama requires that all persons or corporations selling house trailers at retail prices pay a license tax equal to 1.5 percent of all gross proceeds of the sale.[63] The licensed sellers are then required to add to the sales price a 4 percent State sales tax.[64] These requirements also apply to anyone "in business of selling at retail any tangible personal property whatsoever, including merchandise and commodities of every kind and character."[65]

The State also imposes an excise tax on a number of goods. An excise tax of 1.5 percent of sale price is levied on the storage, use, or other consumption of house trailers.[66] However, any trailers for which the usual 4 percent sales tax is paid are exempted from the excise tax.[67] Furthermore, credit will be given for a sales or use tax paid in another State so long as the tax equals 4 percent and the State reciprocates.[68]

Building materials sold to contractors, and building materials sold to the manufacturers of modular homes to become part of real estate in Alabama are considered retail sales and exempted from the excise tax.[69]

This excise or use tax is intended to cover articles purchased out-of-State for which Ala-

59 Code of Ala. Tit. 49. § 17(14) (1971 Supp.).
60 Id.
61 Ibid., § 17(6) (1971 Supp.).
62 Ibid., § 17(22) (1971 Supp.).
63 Code of Ala. Tit. 51 § 786(3) (1971 Supp.).
64 Ibid., § 786(25) (1971 Supp.).
65 Ibid., § 786(3) (1971 Supp.).
66 Ibid., § 788(c) (1971 Supp.).
67 Ibid., § 789 (1971 Supp.).
68 Ibid., § 789(3) (1971 Supp.).
69 Ibid., § 787(e) (1971 Supp.).

bama received no sales tax, or inventories of dealers or merchants for which no sales tax is collected. It does not affect the in-State consumer who pays the usual sales tax.

Taxation of Mobile and Modular Units

Mobile homes and modular units are treated differently for tax purposes. Modular homes are apparently treated as real property,[70] while mobile homes are taxed as personal property, like motor vehicles.[71]

The property tax provision governing modular homes is: "Every parcel of land, including all things pertaining to such land, and all structures and other things so annexed or attached thereto as to pass to a vendee by conveyance of such land" are taxed as real property.[72] There is a $2,000 homestead exemption.[73] The property is taxed at a rate of 65 percent[74] of the assessed value, which is either 15 percent or 20 percent of fair market value.[75] Mobile homes are assessed every year for ad valorem taxation, and taxes are paid in the same manner in which motor vehicles are taxed.[76] The valuation is 60 percent of fair market value.[77] Or a mobile homeowner may have to pay an annual registration fee of $3 unless the house trailer has been "assessed for ad valorem taxes as part of the realty." [78]

Codes and Inspection Procedure

There is no statewide building code for private buildings such as homes. There is legislation requiring a State building code for public buildings such as theaters and hotels[79] and enabling municipalities and counties to adopt and expand the code through local ordinances.[80] There is enabling legislation for the State building commission to provide adequate inspection to insure compliance.[81] Apparently no statewide housing code has been adopted, so municipalities and counties may have no building codes.

Since mobile homes are inspected under the standards of the American National Standards Institute,[82] they are presumably exempted from the requirements of whatever local building code there may be.

There is apparently no statewide minimum housing code. However, cities are authorized to enact ordinances setting minimum standards for dwellings.[83] They may regulate "use, control, repair and maintenance of buildings, dwellings and structures of all types, the numbers of occupants, mode and manner of occupancy to insure a healthful, safe environment." Cities may also compel owners or managers to reconstruct or modify an unsafe building, and may prohibit the use and occupancy of a building until the rules are complied with.[84]

There is no State legislation to permit tenant suits for damages when the landlord fails to meet the codes. Cities should be able to enact ordinances to that effect, however, since Tit. 37 §785(2) declares that it vests additional authority in municipalities to adopt ordinances for the establishment and enforcement of codes.

Landlord and Tenant Law

There is no statute giving the tenant the right to withhold rent if the unit does not comply with the minimum housing code. Presumably, municipalities could adopt such a policy through ordinances pursuant to a program of code enforcement.[85]

The caselaw in the area of housing repairs gives no authority for rent withholding in this situation. In the absence of a special agreement at the time of the rental contract, the landlord need not keep the premises in repair.[86] However, where the lease obligates the landlord to keep the premises in a state of good repair, the tenant may be able to repair and deduct the cost.[87]

Local governments are able to adopt repair and deduct ordinances empowering local housing authorities to improve substandard housing, as a part of their general power to enforce codes.[88] There is no statute specifically permitting them to do this, however.

The State fire marshal has wider powers than any agency in the area of requiring repairs or demolishing substandard housing. If an owner fails to comply with the marshal's order to repair

[70] Ibid., § 21 (1971 Supp.).
[71] Ibid., § 704(2) (1971 Supp.).
[72] Ibid., § 21 (1971 Supp.).
[73] Ibid., § 15 (1971 Supp.).
[74] Ibid., § 18 (1960).
[75] Ibid., § 17 (1971 Supp.).
[76] Ibid., § 704(2) (1971 Supp.).
[77] Ibid., § 704 (1971 Supp.).
[78] Ibid., § 704(1) (1971 Supp.).
[79] Code of Ala. Tit. 55. § 367 (1960).
[80] Ibid., § 367(11) (1960).
[81] Ibid., § 367(12) (1960).
[82] Code of Ala. Tit. 25 § 126 (1971 Supp.).

[83] Code of Ala. Tit. 37 § 785(2) (1971 Supp.).
[84] Id.
[85] Code of Ala. Tit. 37 § 785(2) (1971) Supp.).
[86] *Lusco* v. *Jackson* 27 Ala. App. 531, 175 So.566 (1937).
[87] *McKenna* v. *Rowlett* 68 Ala. 186 (1880); *Stripling* v. *Odum* 267 Ala. 201, 101 So.2d 328 (1958).
[88] Code of Ala. Tit. 37 § 785(2) (1971 Supp.).

or dismantle dilapidated and dangerous property, the marshal may order the building repaired at the owner's expense.[89] He is also empowered to have the building demolished at the owner's expense.[90] If the owner refuses to reimburse the marshal for the expenses of such work, the cost becomes a lien on the repaired property and/or real estate on which it is located.[91]

There is no housing court, nor is there any authority for court appointment of a receiver to collect rents and make improvements.

Alabama State taxes are due October 1. After January 1, the collector makes a demand for payment from delinquent taxpayers. If the taxes are not paid, the collector levies upon the delinquent's personal property and sells it, after 10 days notice, to the highest bidder.[92] Enough property must be sold to cover taxes, fees, and expenses of the sale. A second method authorized is garnishment of any money, property, or choses in action belonging to the taxpayer and under the control of another person.[93] A third possibility is the levy and sale of shares of stock of private corporations belonging to delinquents.[94] When there is no personal property available for sale, or when the sale price is insufficient to pay the taxes, the collector may sell the real property on which the taxes are a lien.[95] This procedure is strictly a last resort; the other methods are far easier, and less harsh on the delinquent taxpayer. The statute says that "the failure of the tax collector to so exhaust such personal property shall not invalidate the sale of any real estate."[96] But tax sales have been held void for lack of showing that the collector reported to the probate court that he was unable to collect without such tax sale.[97]

There is no legal authority concerning assessment rates for improved substandard housing. Since the assessment rate is generally 15–20 percent of fair market value,[98] taxes presumably rise when the market value rises through improvements.

Mortgages

There is no authority permitting flexible mortgage financing, and there is no specific mention of open-end mortgages in Alabama legislation.

Mortgages are discussed generally under the savings and loan section. There appears to be no authority for any out-of-the-ordinary financing terms.

Insurance

There is no statute requiring that insurance companies doing business in the State write fire insurance for substandard areas.

Among the criteria to be considered in rate-setting are construction, protective facilities, and other conditions that materially affect the hazard or peril.[99] If an area is dangerously susceptible to fire through faulty construction and inadequate protective facilities, the rates will undoubtedly be set so high that no one living there will be able to afford them.

Housing Authorities

There is no statewide housing authority in Alabama, although the State allows the establishment of county, municipal, and regional authorities.[100] No authority is required by State law. The existence is determined by the initiative of the citizens or local commissioners.

A county authority may be established if 25 citizens petition the commissioners, setting out a need. A public hearing is held. If the commission finds unsanitary housing conditions, it may establish the authority.[101] A regional authority may be established in two or more contiguous counties if their governing bodies determine that there is such a need. When the regional authority is established, it assumes all the powers of the county authorities which cease to exist.[102]

Wide powers are vested in the county and regional authorities.[103] They may prepare and operate housing projects, provide for the construction and repair of projects, acquire property, insure, and borrow money. They are also given all powers necessary and convenient to carry out and effectuate these provisions.[104] All projects are subject to local zoning laws and building codes.[105]

The authorities are also empowered to mortgage property,[106] and to contract with the Fed-

[89] Code of Ala. Tit. 55 § 42 (1960).
[90] Id.
[91] Ibid., § 43 (1960).
[92] Code of Ala. Tit. 51 § 201 (1960).
[93] Ibid., § 204 (1960).
[94] Ibid., § 207 (1960).
[95] Ibid., § 208 (1960).
[96] Id.
[97] *Henderson* v. *Simmons* 235 Ala. 329, 174 So. 491 (1937).
[98] Code of Ala. Tit. 51 § 17 (1971 Supp.).

[99] Code of Ala. Tit. 28A § 262 (1971 Supp.).
[100] Code of Ala. Tit. 25 §§7, 33, 59 (1960).
[101] Ibid., § 33 (1960).
[102] Ibid., § 59 (1960).
[103] Ibid., §§ 38, 47, 53, 65 (1960).
[104] Ibid., § 38 (1960).
[105] Ibid., § 43 (1960).
[106] Ibid., § 47 (1960).

eral Government in any way necessary to secure their financial aid.[107]

Alabama also has an interesting provision for housing in rural areas.[108] The authority may enter into long term leases or purchase agreements to rent or sell housing to persons of low income in rural areas. The owner of land on which there is an unsafe or unsanitary dwelling may file an application requesting the authority to build a safe and sanitary dwelling.

A provision added later clarified the details of authority-built rural housing. Until the purchaser makes full payment, it remains the tax-exempt property of the authority, although the landowner may continue to claim homestead exemption.[109]

The rental rate to be charged by the authorities is carefully regulated.[110] Rentals are never to be a source of income for the town or city. The authorities are to procure revenue only to:

- Pay the principal and interest on bonds and obligations;
- Meet the cost of maintenance, operation, and administrative expenses;
- Create a reserve sufficient to meet the largest principal and interest payments due the following year.[111]

The management must observe several rules with regard to tenant selection.

- It must lease only to persons lacking income necessary to enable them, without assistance, to live in decent uncrowded dwellings.
- It must lease only at a rental within the financial reach of such persons.
- It must lease only the number of rooms necessary.
- It must not accept anyone as a tenant if the persons occupying the rooms have an aggregate net income (less exemptions) greater than 5 times the annual rental. (All utilities are considered part of the rental.)[112]

Housing Development Corporations

There is no Alabama legislation regulating the creation and operation of housing development corporations.

[107] Ibid., § 53 (1960).
[108] Ibid., § 55 (1960).
[109] Ibid., § 93 (1971 Supp.).
[110] Ibid., § 87 (1960).
[111] Id.
[112] Id.

Arkansas Report on Legislation

Land Use Controls—Generally

Governments: Arkansas classifies its incorporated municipalities into three categories, as follows:

- cities of the first class—those over 2,500 in population;
- cities of the second class—those over 500 but less than 2,500 in population;
- towns—less than 500 population.[1]

Towns of less than 500, however, can vote to become classified as second-class cities,[2] and cities of 1,500 to 2,500 can vote to have themselves classified as first-class cities.[3] In addition, there is the general category of counties, which is made up of all remaining unincorporated land and is dealt with separately in Title 17 of the Arkansas Statutes.

State Planning: Arkansas has had a State planning commission of one sort or another since 1935.[4] The present commission,[5] like those before it, is designed to be an advisory board. Its primary function is the ongoing development of a State plan, and the furnishing of advice and expertise to State and local officials.[6] One of the most important functions of the commission is to serve as Arkansas' ambassador to the Federal Government for the purpose of obtaining Federal funds and benefits.[7]

The Arkansas General Assembly has recently added a second arm to its planning and conservation program by enabling the creation of regional multicounty planning and development organizations.[8] By this act, the State Planning Commission is instructed to aid and advise these regional and locally controlled planning districts, but no standards or guidelines are set out and no real power over them is conferred upon the State commission.[9] In no legislation has the General Assembly laid down concrete standards, nor has any board or commission been given power to promulgate and enforce regulations. It is therefore submitted that the Arkansas planning legislation is relatively insignificant in terms of drafting Federal housing legislation.

Municipal Planning and Zoning: Municipal zoning in Arkansas is accomplished through au-

[1] Ark. Stat. Ann., § 19–202 (1971 Supp.).
[2] Id., § 19–215 (1968).
[3] Id., § 19–202 (1971 Supp.).
[4] Id., §§ 9–301—§ 9–306 (1971 Supp.).
[5] Id., § 9–306 (1971 Supp.).
[6] Id., §§ 9–316—9–318 (1971 Supp.).
[7] Id., §§ 9–320—9–323.
[8] Id., §§ 9–324—9–328.
[9] Id., § 9–324.

thority of a few broad and indefinite enabling statutes, the first of which was passed in 1875.[10] All municipal corporations have the power to regulate the construction, alteration, and repair of buildings for limited purposes—primarily fire prevention.[11] In addition, cities of the first class have the power to regulate construction of houses by requiring a building permit.[12] The statutory criteria for denying a permit are safety hazards, poor sanitation, obnoxiousness, and detrimental to the public welfare.[13] All municipal corporations have the power to order the removal or razing of buildings or houses which in the opinion of the city council are dilapidated, unsightly, unsafe, unsanitary, obnoxious, or detrimental to the public welfare.[14]

The public policy of Arkansas with respect to zoning is expressed in the following statute.[15]

> 19-2804. Zoning regulations by cities—Declaration of purpose.—It is recognized and hereby declared that the beauty of surroundings constitutes a valuable property right which should be protected by law, and that this is particularly true of residential sections where people have established their homes. [Acts 1924 (3rd Ex. Sess.), No. 6, § 1, p. 60; Pope's Dig., § 10055.]

This policy is effectuated through a statute which enables cities of the first and second class to establish zones limiting the character of the buildings that may be erected therein.[16] This statute provides only for three broad zones: (1) Manufacturing; (2) business other than manufacturing; and (3) residential. Since the passage of this very general enabling statute in 1924, the legislature has chosen to enable further, more detailed zoning through municipal planning acts. Apparently as a result of confusion created by these old zoning enabling statutes and the more recent planning acts, the statute quoted in text, supra, was amended in 1965, to make it clear that no municipality had zoning authority beyond its corporate limits.[17] However, cities with a navigable stream can zone along the stream for a distance of 5 miles beyond their corporate limits in either direction, for a distance of 2 miles laterally from the thread of the stream.[18]

The heart of zoning and land use control legislation in Arkansas today is in the 1957 Municipal Planning Commission Act.[19] This act provides extensive authority for the creation of planning commissions in all incorporated municipalities regardless of class. For the purposes of this study on housing law, the two most important functions of these planning commissions are the recommendation of zoning ordinances to the city council, and the control and administration of the development and subdivision of land.[20] A glance at this statute indicates that it is only an enabling provision, with little or no substantive information regarding what one could expect to find in any particular municipality. Moreover, the land use plan which the planning commission is required to prepare does not in and of itself constitute a zoning ordinance.[21] It may all be somewhat academic for the purposes of rural housing anyway, because it seems probable that the smaller the town and the more rural the community, the less likely it is that such commissions have even been formed.[22]

A further segment of State legislation regarding land use planning and zoning is an act enabling and encouraging contiguous cities, towns, and counties jointly to exercise planning powers, duties, and functions.[23] The act provides for creation of a joint or "metropolitan" planning commission to lend coordination and uniformity to the overall planning efforts of a region. This commission, however, is without any real power because the act specifically reserves to the cooperating cities and counties all of their power and authority to zone and plan within their own jurisdictional limits—the joint commission is purely supplemental.[24]

County Planning and Zoning: The final piece in the fragmented puzzle which constitutes public authority for land use planning in Arkansas is a 1937 act which gave basic planning, zoning, and subdividing authority over unincorporated territory to the respective counties.[25] The county judge is given authority to appoint a 5- to 12-man County Planning Board whose members serve voluntarily without compensation.[26] This Board's primary function is to develop an official County Plan,[27] which will divide, plat, and zone the unincorporated territory within the county.[28]

[10] Id., § 19-2801 (1968).
[11] Id.
[12] Id., § 9-2802 (1968).
[13] Id.
[14] Id., § 19-2803.
[15] Id., § 19-2804.
[16] Id., § 19-2805.
[17] Id., § 19-2804.1 (1971 Supp.).
[18] Id., § 19-2804.2.
[19] Id., §§ 19-2825—19-2831 (1968). See appended statute D.

[20] Id., § 19-2829.
[21] *Economy Wholesale Co.* v. *Rodgers*, 232 Ark. 835, 340 S.W.2d 583 (1960).
[22] I have no authority for this conclusion, it is merely my personal opinion.
[23] Ark. Stat. Ann., §§ 19-2820—19-2824 (1968).
[24] Id., § 19-2824.
[25] Id., §§ 17-1101—17-1106.
[26] Id., § 17-1101.
[27] Id., § 17-1103A.
[28] Id., § 17-1103D.

Significant for purposes of low income housing, however, is the fact that the board is expressly denied authority to regulate the cost of buildings and structures.[29] The stated purposes and goals of the county plan are not inconsistent with development of low income housing.[30] The county planning board has the same control and authority over the subdivision of unincorporated land as the municipalities have over land within their corporate limits.[31]

Of possible significance to low income housing proposals brought within the framework of a public housing authority is a provision of the act which states that once a county plan is adopted and put into effect, no improvements shall be made or authorized and no property shall be acquired by any county or public agency, which has, or is likely to have, definite part in, or relation to, the official county plan unless the proposal shall have been submitted by the agency concerned to the County Planning Board, and a report and recommendation of the said board thereon shall have been received.[32] If after 30 days the Board takes no action, the concerned agency may proceed without its approval.[33] It is not clear whether a public housing authority project would have to comply with this requirement.[34]

Regulations Affecting the Homebuilding Construction Industry

Arkansas does not have a statewide building code. As developed below, the State has chosen to regulate the construction industry in piecemeal fashion by imposing registration and licensing requirements upon certain tradesmen. However, the various municipalities and governmental units do have the authority to impose building regulations, and presumably could draft or adopt their own building code.[35]

Arkansas has created a State Licensing Board for Contractors[36] which administers an act designed to license and regulate general contractors in the building industry.[37] By a 1967 amendment, however, the entire act was made not applicable to contractors of single family residences.[38] The act does apply to virtually all other types of construction and repair contracting when the aggregate cost of such work is $200,000 or more.[39] Criteria considered in granting a license are (1) ability, (2) experience, (3) character, (4) the manner of performance of previous contractors, (5) financial condition, (6) equipment, (7) any other fact tending to show ability and willingness to conserve the public health and safety, and (8) default in complying with the provisions of the act, or any other law of the State.[40] The board does have power to act upon complaints, hold hearings, and revoke licenses.[41] The act does not apply to contractors engaged in construction for the United States Government, because it would interfere with the Federal Government's right to select contractors.[42]

Architects[43] and engineers[44] are also required to be licensed by State boards and regulated thereby. This is standard regulation of professional occupations, and needs no description.

The most extensive and comprehensive piece of Arkansas legislation which affects the homebuilding industry is an act regulating plumbers and the plumbing trade in general.[45] The basic mechanism of plumber regulation is a mandatory registration and permit or licensing system which is administered by the State Board of Health.[46] The act sets out detailed requirements for the registration, training, examination, and licensing of master plumbers, journeyman plumbers, and apprentices.[47] The Board of Health is given significant powers to promulgate a State plumbing code, and actively to inspect, investigate, and regulate the plumbing industry in Arkansas.[48]

SCOPE OF CODE. The provisions of the state plumbing code and amendments thereto as adopted by the Board defining plumbing work, prescribing minimum requirements for design, materials, appliances, workmanship and methods of installation shall after publication in any legal publication in the state once each week for three (3) weeks have the effect and force of law in the form of minimum standards state-wide in application and shall apply to all types

[29] Id.
[30] Id., § 17-1104.
[31] Id., § 17-1106.
[32] Id., § 17-1105.
[33] Id.
[34] Compare § 17-1105 with § 19-3011 (1971 Supp.) which describes the powers of housing authorities: "[No] provisions of law with respect to the acquisition, operation or disposition of property by other public bodies shall be applicable to an authority unless the legislature shall specifically so state."
[35] See discussion of municipal planning and zoning, supra p. 2, and accompanying footnotes.
[36] Ark. Stat. Ann., § 71-702 (1971 Supp.).
[37] Id., §§ 71-701—71-724.
[38] Id., § 71-702.
[39] Id.
[40] Id., § 71-709.
[41] Id., § 71-711.
[42] *Leslie Miller, Inc.* v. *Arkansas*, 352 U.S. 187 (1956).
[43] Ark. Stat. Ann., §§ 71-301—71-314 (1971 Supp.).
[44] Id., §§ 71-1001—71-1024 (1957).
[45] Id., §§ 71-1205—71-1217.
[46] Id., §§ 71-1206, 71-1207, 71-1210.
[47] Id., § 71-1207. Note that this statute requires the Board to recognize the National Plumbing Apprenticeship Standards for the training of plumbers' apprentices.
[48] Ark. Stat. Ann., §§ 71-1206, 61-1216(2) (1957).

of buildings, private or public, rural or urban, including buildings owned by the state or any political subdivision thereof. All plumbing installations shall be made to conform with such code. Cities and towns may make additional regulations not in conflict with such code.[49]

In addition to this statewide code, the act directs that cities of the first or second class having a system of waterworks or sewerage shall, and an incorporated town or any metropolitan sewerage commission may, by ordinance, prescribe rules and regulations concerning plumbing to safeguard the public health, not in conflict with the minimum standards prescribed by the board.[50] Moreover, nothing in the act "shall prohibit cities and towns from having full authority to provide full supervision and inspection of plumbing and plumbers by the enactment of codes, rules and regulations in such form as the council may determine appropriate." [51] The only exceptions to the coverage of the act are: (1) Plumbing work done by a property owner in a building owned and occupied by him as his home, except where such license is required by local ordinance, and (2) plumbing work to farm buildings located outside the incorporated limits of any city or town unless such buildings are connected to a public water or sewer system.[52]

Mobile Homes and Modular Housing

Taxation: The State of Arkansas has a 3 percent sales tax, and it is applicable to the sale of mobile homes.[53] In addition, Arkansas has a Compensating Tax Act,[54] which is also a 3 percent tax, and it applies to all personal property. The compensating tax is an excise tax for the privilege of storing, using, or consuming personal property within the State.[55] For purposes of taxation, mobile homes are considered personal property in Arkansas.[56] This conclusion is not expressly codified, but the general framework of mobile homes on resale implies that the Arkansas General Assembly considers them to be personal property.[57] There are apparently no conditions or circumstances under which mobile homes will be taxed as real property.[58]

There are no statutes whatever concerning modular housing. With respect to taxation of modular housing, it is likely that the personal property status of mobile homes would be analogized and followed.[59]

Regulations Governing Use and Highway Restrictions: There are no statutes regarding the uses to which mobile homes may be put. There are, however, statutes regulating the sale of mobile homes and the transportation of them upon the roads and highways of the State.

All persons selling house trailers or mobile homes must obtain and hold a permit from the Commissioner of Revenues, and make a monthly report to the commissioner.[60] These reports include a copy or copies of invoices, sales ticket, or bills of sale reflecting the date of all sales of such house trailers or mobile homes; the purchaser's name and address; the make, year, model, and serial number, and gross sales price of each house trailer or mobile home; and the amount of tax collected from the purchaser.[61] The sales tax or compensating tax, if once paid in Arkansas for the sale or possession of a house trailer or mobile home, is not required to be paid a second time upon resale or possession by a second owner.[62]

In 1971, the Arkansas General Assembly enacted a relatively comprehensive act to regulate the transportation of oversized trailers and mobile homes.[63] Mobile homes larger than 8 feet in width and/or 60 feet in length are defined as oversized, and a special permit from the State Highway Department must be obtained before they can be moved on State highways.[64] No home in excess of 14 feet in width (exclusive of clearance lights) may receive a permit.[65] The cost of the permit is $5.[66] The most significant regulations in the act concern who may obtain such a permit.[67] The statute is written so as to make it impossible for a private individual to se-

[49] Id., § 71–1216(2).
[50] Id., § 71–1208.
[51] Id., § 71–1209.
[52] Id., § 71–1216(1).
[53] Id., §§ 84–1901—84–1929 (1960).
[54] Id., §§ 84–3101—84–3128.
[55] Id., § 84–3105.
[56] Bartke & Gage, *Mobile Homes: Zoning and Taxation*, 55 *Corn. L. Rev.* 491, 521 (1970); Note, *Taxation—Property Tax on House Trailers—Real or Personal Property*, 8 *Ark. L. Rev.* 188 (1954).
[57] *Ark. Stat. Ann.*, § 84–1934 (1971 Supp.): "It is the intent of this Act (§§ 84–1933—84–1936) that used house trailers or mobile homes once having been subjected to either the Gross Receipts or Compensating Tax shall on subsequent sale be exempted."
[58] See supra, note 56.
[59] See E. F. Roberts, *Land Use Planning*, pp. 4–270 (1971). It should be pointed out that these taxing statutes and the regulatory statutes, infra notes 60–72, are written in terms of "house trailers or mobile homes." It is certainly not unreasonable to predict that modular housing will be interpreted to come within the meaning of "mobile home" despite the illogical result of taxing them as personal property.
[60] Ark. Stat. Ann., § 84–1933 (1971 Supp.).
[61] Id.
[62] Id., § 84–1934.
[63] Id., §§ 75–828—75–835.
[64] Id., § 75–829.
[65] Id.
[66] Id., § 75–830.
[67] Id., § 75–831.

cure a permit for a home wider than 12 feet, and almost impossible if the home is more than 8 feet in width.[68] A licensed carrier, dealer, or manufacturer may obtain a permit upon proof of minimum insurance coverage (i.e., $100,000 for first bodily injury or death, $300,000 for bodily injury or death for each accident, and $100,000 for property damage).[69] An individual, on the other hand, may obtain a permit himself only if: (1) The home is not over 12 feet wide; (2) it is registered to him; (3) it is not for the purpose of sale; (4) he has a truck of at least 1 ton and it is in compliance with appropriate ICC safety regulations; (5) the driver is experienced at pulling wide loads; (6) minimum insurance coverage, supra, is proven; and (7) the individual has title.[70] Obviously, the act is designed to keep the amateur trailer-puller off of the State highways.

In addition, the act gives to the State Highway Department the duty to promulgate rules and regulations in accordance with the act.[71] Finally, the act sets out broad guidelines for the size of trailers allowed on roads of various widths (subject to Highway Department discretion to grant exceptions), and generally prohibits the transportation of oversized trailers on weekends or holidays.[72]

State Housing Corporations

Arkansas has very extensive legislation regarding the creation and operation of public housing authorities.[73] The legislation can be divided in terms of housing authorities, redevelopment agencies, and urban renewal projects, but for the purposes of this study there is little to be gained by doing so—the rights and powers bestowed do not vary significantly.

Each governmental agency in the State is entitled to create a housing authority.[74] The powers of these housing authorities are quite comprehensive.[75] The housing authorities are nonprofit [76] public corporations whose only masters are the various city councils and county governments who create them by resolution. All housing authority projects are subject to the planning, zoning, sanitary and building laws, and ordinances and regulations applicable to the locality in which the housing project is situated.[77] Also, in the planning and location of any housing project, an authority is required to take into consideration the long range city, county, or regional plan as promulgated by a planning commission.[78] Cooperation between housing authorities and various planning boards and commissions is expressly encouraged.[79]

Housing authorities are given power to sell projects to the Federal Government,[80] and otherwise to seek and accept aid from the Federal Government.[81] The property of a housing authority is declared to be public property and therefore is exempt from all taxes and special assessments of the State or any public body thereof.[82]

County and regional housing authorities are authorized to create rural housing projects; it appears, however, that these projects are solely for the benefit of low income farmers.[83] Housing authorities have the power to undertake redevelopment projects of blighted areas,[84] and where housing authorities have not been created or have been inactive in redevelopment, the governing body is empowered to create urban renewal agencies for that purpose.[85] Although there is no authority for statewide housing authorities, there are several provisions enabling regional or interjurisdictional housing authorities.[86] Both housing authorities [87] and urban renewal agencies [88] have the power of eminent domain to aid them in the effectuation of their projects.

The Horizontal Property Act

Arkansas has enacted a so-called "Horizontal Property Act" for the purpose of accommodating the condominium concept in the State's property law.[89] The act, by permitting the sale and financing of condominiums, allows builders and building owners to take advantage of Section 104 of the Federal Housing Act of 1961,[90] which makes mortgage insurance available on separate units in such properties.[91] Basically,

[68] Id.
[69] Id., § 75–828(c).
[70] Id., § 75–831.
[71] Id., § 75–835.
[72] Id., § 75–832.
[73] Id., §§ 19–3001—19–3076 (1968).
[74] Id., § 19–3004.
[75] Id., § 19–3011 (1971 Supp.).
[76] Id., § 19–3012 (1968). This statute also set out guidelines for fixing maximum rental rates.

[77] Id., § 19–3016.
[78] Id.
[79] Id., § 19–3029.
[80] Id., § 19–3024.
[81] Id., § 19–3023. Redevelopment Projects and Urban Renewal Agencies have similar powers. See § 19–3061 (1968).
[82] Id., § 19–3027.
[83] Id., §§ 19–3053—19–3055.
[84] Id., §§ 19–3056—19–3063.
[85] Id., § 19–3063.2.
[86] Id., §§ 19–3014 and 19–3038.
[87] Id., § 19–3015.
[88] Id., § 19–3075 (1971 Supp.).
[89] Id., §§ 50–1001—50–1023 (1971).
[90] Public Law 87–70, 75 Stat. 149 (30 June 1961).
[91] Legislation—*Horizontal Property Act—The Concept of Condominiums,* 15 *Ark. L. Rev.* 430 (1961).

the act provides for the ownership and conveyance of apartment units as though each were a traditional tract of real estate. The details of the procedure for qualification, registration, and operation of condominiums are fairly simple and do not need to be analyzed for this study. If a condominium concept were used in low income housing, the act would have to be followed, but it would be no burden, because it presents no impediments to such housing. Indeed, the Horizontal Property Act encourages the development of condominium living arrangements.

Usury Laws

In Arkansas, interest rates are restricted by the State constitution, which provides that "[all] contracts for a greater rate of interest than 10 percent per annum shall be void as to principal and interest . . ." [92] This constitutional provision has been codified [93] so as to authorize parties to a contract to agree in writing for the payment of a rate of interest not in excess of 10 percent per annum.

The Arkansas Supreme Court held at an early date that it is not usurious to provide for the calculation of interest on interest that has actually accrued, but that it is usurious to provide for the calculation of interest on interest that will only accrue subsequently.[94] In a later case, the court stated:

> The true test is: Has the debtor the absolute right to discharge and satisfy the contract at maturity by paying the principal debt and lawful interest. If he has, the contract is not vitiated by providing for the payment of an additional sum.[95]

The Arkansas Constitution makes no distinction between FHA or VA and conventional loans, and, since the usury statutes in Arkansas are of constitutional origin, the legislation has been and is precluded from unilaterally making such a distinction.[96] The criterion that has governed the determination of usury has been stated as being:

> . . . whether the total amount to be paid under (a loan agreement's) terms by the borrower in the event of performance, is in excess of the principal received plus 10 percent interest per annum for the term thereof.[97]

The language used by the court in expressing these criteria indicates that any lump sum payment by the borrower to the lender which is considered interest will be spread over the entire term of the loan for the purpose of determining the presence of usury; however, the computational procedure to be used in amortizing such sums has not been made clear by the Arkansas courts. The wording of these criteria also suggests that charges paid by someone other than the borrower would not be included as interest. The validity of this suggestion has again not been made clear by the courts, but it must be noted that the underlying constitutional provision makes no such distinction and, indeed, the Arkansas Supreme Court has stated that a "contract to pay directly or indirectly a greater rate of interest than 10 percent," would constitute usury under the Arkansas constitution.[98]

Broker fees have been held not to constitute interest unless the broker is an agent of the lender, and the lender is aware of, or may by law be presumed to be aware of, his agent's actions.[99] Broker fees which are paid to the broker as an agent of the borrower, and which are then shared with the lender, are included as interest; such payments, however, are not so included if the broker acts "on his own account" and not as an agent for the borrower.[100]

A borrower may contract with a lender to pay "certain valid and reasonable charges, paid to a third party, and incurred for the borrower's benefit in procuring the loan." [101] Such "valid and reasonable" charges have been held to include costs of abstracts paid to a third party, costs of title opinions paid to an attorney, recording fees paid to an official, and insurance premiums paid to a third party, but charges for a credit report have been held to be included as interest because such a report is for the sole benefit of the lender.[102] A charge which consists merely of a percentage of the lender's overhead expenses is also included as interest.[103]

Discounts which are chargeable to the borrower have been held to constitute interest.[104] Whether this decision would be applicable to "points" paid by a seller would be a determination to be based on the factors discussed above.

[92] Ark. Const. art. 19, § 13.
[93] Ark. Stat. Ann., § 68–602 (1957).
[94] *Grider* v. *Driver*, 46 Ark. 50 (1895).
[95] *Carney* v. *Matthewson*, 86 Ark. 25, 109 S.W. 1024 (1908).
[96] *Winston* v. *Personal Finance Co. of Pine Bluff*, 220 Ark. 580, 249 S.W.2d 315 (1952).
[97] *McDougall* v. *Hachmeister*, 184 Ark. 28, 41 S.W.2d 1088, 1090 (1931).
[98] *Smith* v. *Eason*, 223 Ark. 747, 749, 268 S.W.2d 389, 390 (1954).
[99] *Valhberg* v. *Keaton*, 51 Ark. 534, 11 S.W. 878 (1889).
[100] *Jones* v. *Phillippee*, 135 Ark. 578, 206 S.W. 40 (1918).
[101] *Smith* v. *Eason*, 223 Ark. 747, 268 S.W.2d 389, 390 (1954).
[102] Id., *Winston* v. *Personal Finance Co. of Pine Bluff*, 220 Ark. 580, 249 S.W.2d 315 (1952).
[103] *Strickler* v. *State Auto Finance Co.*, 220 Ark. 565, 249 S.W.2d 307 (1952).
[104] *Public Loan Corp.* v. *Weaver*, 223 Ark. 902, 270 S.W.2d 888 (1954).

The time-price differential, or "credit price rule," has been recognized in Arkansas as applying to all credit sales in which a credit and cash price were quoted to the buyer.[105] In 1952, however, the Arkansas Supreme Court in *Hare* v. *General Contract Purchase Corp.,*[106] issued a caveat as to future recognition. The court, after noting that prior cases could not be overruled retroactively, stated that thereafter, while the doctrine of time-price differential would still be applicable to bona fide transactions, a question of fact may arise "as to whether the so-called credit price was bona fide as such, or only a cloak for usury." [107] The determining inquiry was said to be "whether the seller increased his cash price with a reasonable assurance that he could . . . discount the paper to (an) individual or finance company," and "[if] that reasonable assurance existed, then the transaction is in substance a loan and may be attacked for usury." [108] An indication of such assurance is the fact that a finance company or other "purchasers of title paper" have supplied the seller with forms and credit schedules.[109] Thus, under present Arkansas law, a conditional sale is, prima facie, exempt from the usury laws, but if the transaction is shown not to be bona fide according to the criteria set forth in *Hare,* supra, it nevertheless may be attacked as usurious.

Arkansas does not have a comprehensive retail installment sales law; therefore, if a transaction is a bona fide conditional sale, there is no limitation on the amount of time-price differential or finance charge which may be charged.

Laws Affecting Banks and Savings and Loan Associations in the Home Mortgage Field

The statutory limitation upon the size of loans that a bank in Arkansas can make involves a very complicated and confusing formula.[110] Suffice it to state that this general formula is not really relevant in terms of home mortgage loans. There is no special legislation regulating banks in the home mortgage field in Arkansas. Savings and loan, and building and loan associations, however, are regulated by the following statutory limitations.

> 67–831. Restrictions as to loans.—No Building and Loan Association shall make a mortgage loan to an officer, director or employee of such association, either directly or indirectly, unless such loan be first approved unanimously by the members of the board of directors present at the next regular board meeting, such approval to be recorded by aye and nay vote in the minutes of the meeting of the board.
>
> No Building and Loan Association shall make loans exceeding in the aggregate $5,000 to one (1) borrower upon real estate security if the assets of the association do not exceed $50,000; nor shall any such association make loans exceeding in the aggregate $10,000 to one (1) borrower upon real estate security if the assets of such association do not exceed $200,000; nor shall any association make any loans exceeding in the aggregate $15,000 to one (1) borrower upon real estate security if the assets of such association do not exceed $500,000; nor shall any such association make any loan exceeding in the aggregate $25,000 to one (1) borrower upon real estate security if the assets of such association do not exceed $2,500,000; provided that, any Building and Loan Association whose assets are in excess of $2,500,000 may make loans not to exceed the aggregate sum of one per cent (1%) of the assets of said association to one (1) borrower on real estate security.[111]

There does not appear to be any geographic limitation upon either banks or savings and loans in terms of their power to make home mortgage loans. Presumably, a bank or savings and loan can make such mortgages anywhere in the State.

Miscellaneous

This category consists of brief summaries of those broad areas of law for which I was unable to find any significant legislation that would even indirectly affect the supply of housing in Arkansas.

Health Laws and Regulations as They Affect Safe and Sanitary Housing: There is no health legislation directly concerning or affecting housing on the State level. As discussed previously, all regulation and control over housing conditions and quality are in the hands of the various local governments.[112]

Environmental Protection Laws: Arkansas has laws for the protection of both its air [113] and water [114] resources, but these laws are directed at industry and community governments in general, and not directly at the individual homeowner. The water pollution control act cre-

[105] *Smith* v. *Kaufman,* 145 Ark. 548, 224 S.W. 978 (1920).
[106] 220 Ark. 601, 249 S.W.2d 973 (1952).
[107] Id. at 609, 249 S.W.2d at 978.
[108] Id.
[109] Id.
[110] Ark. Stat. Ann., § 67–507 (1971 Supp.).

[111] Id., § 67–831 (1966). This statute is applicable to savings and loan associations as well as to building and loan associations.
[112] See supra, discussion of Municipal Planning and Zoning. Recall also that plumbing is regulated by the state board of health and local governments. This is the primary means of regulating sanitation conditions in housing. See supra, notes 45–52 and accompanying text.
[113] Ark. Stat. Ann., §§ 82-1901—82-1914.17 (1971 Supp.).
[114] Id., §§ 82-1931—82-1943.

ates a commission which is to administer and enforce it. The State commission also has authority to issue orders and regulations,[115] but, to date, no regulations directly effecting housing have been issued.[116] That is to say that the commission does not prescribe what sort of plumbing or septic tank must be used. The commission does prescribe what the allowable level of various pollutants in the State's waters shall be, and effectuates these orders by regulating the operation of sewage and disposal systems. Thus, it is the local municipalities and county governments that actually implement guidelines and minimum standards through local building codes and ordinances in order to comply with State pollution regulations.

Significantly, there is no requirement for an environmental impact statement prior to any construction or land development. Presumably, such prior restraint upon building is exercised by the local or regional planning and zoning commissions.

Requirements Regarding Water and Waste Systems; Effect on Lot Size: It follows from what has just been said that there are no uniform laws or regulations concerning water and waste systems that affect lot size. No doubt such regulations do exist in local building and plumbing codes, as discussed previously.

Welfare Laws: There is no welfare lien law in Arkansas, nor do any other welfare laws appear to have any effect upon the supply of housing.

Specific Points

Codes and Inspection Procedures: There is no statewide building code, nor is there a State minimum housing code. While there is no express authority for the adoption of minimum housing codes by cities, there is authority to enact building and plumbing codes,[117] and a minimum housing code almost certainly seems authorized for cities of the first class.[118] Arkansas has no legislation permitting tenant suits for damages in cases of a landlord's failure to meet codes.

Landlord and Tenant Law: The tenant does not have the right to withhold payment of rent if the unit does not comply with the minimum housing code. Local agencies are not authorized to make repairs on substandard dwellings and to make the cost a lien on the dwelling, and there is no legal authority for the closing, vacating and demolition of substandard housing.[119] Similarly, no housing court or similar court exists, nor is there any authority for court appointment of a receiver to collect rents and make improvements.

As to foreclosing on tax delinquent dwellings, the provisions concerning the collection of delinquent taxes from real property are anything but quick and simple.[120] Delinquent tax liens are published in appropriate newspapers once each year and a public sale is held. If they are not sold to the public, the State of Arkansas buys them, and in either event there is a 2-year period during which the property may be redeemed by the payment of all taxes, penalties, and cost, plus a 10 percent interest charge. Therefore, at the very least, no foreclosure can become final in less than 2 years.

No legal authority authorizes tax officials to maintain existing levels of assessment following improvement of substandard housing.

Mortgages: State legislation does not expressly permit "flexible" mortgage financing, e.g., interest abatement during the early years of mortgage payments on low and middle income housing. There is very, very little regulation of mortgage financing in Arkansas, and none which appears even indirectly related to flexible financing procedures. On the other hand, there is no prohibition of it either.

With regard to open-end mortgages (that can be increased periodically to permit financing for rehabilitation), there is no special legislation concerning this particular practice—either enabling or prohibiting it. I do not see why it could not be done so long as a proper memorandum of the agreement is placed with the official mortgage deed in the recorder's office and is attested to and dated by the clerk.[121]

[115] Id., § 82–1904.

[116] I have reached this conclusion after examining the Arkansas water pollution control regulations as set out in the B.N.A. *Environmental Law Reporter*.

[117] See generally notes 11–50 and accompanying text, supra.

[118] Ark. Stat. Ann. § 19–2802 (1968). The statute does not expressly mention minimum housing codes, but such a code would seem to be implicit within the authority conferred to cities of the first class.

[119] Id. at § 19–2803. Moreover, the city need not pay compensation if the demolition is necessary to abate a sanitation nuisance and protect the public health and welfare. *Springfield* v. *Little Rock*, 226 Ark. 462, 290 S.W.2d 620 (1956).

[120] See generally Ark. Stat. Ann., Title 84, Chapters 10, 11, 12 & 14 (1960).

[121] By analogy, Ark. Stat. Ann. § 51–1010 (1971), which prescribes this procedure for the extension of maturity for mortgages, would seem to allow open-end mortgages if the recording procedure were followed.

Insurance: State legislation does not require insurance companies doing business in the State to write fire insurance in substandard areas.

Housing Authorities: The State allows inter-jurisdictional housing authorities,[122] but not statewide housing authorities.

Housing Development Corporations: The State does not regulate the creation and operation of housing development corporations; there is no legislation whatsoever regarding housing development corporations.

Kentucky Report on Legislation

State Legislation Prescribing Land Use Controls and Affecting Local Zoning Ordnances

Land use planning controls generally are left to the county and city authorities. However, there is State legislation governing this topic.

Before any planning operations may begin, a "planning unit" must be formed and designated. Planning units may consist of a city or county acting independently in accordance with §100; cities and their county; or in groups of counties and their cities regionally.[1] Any city or county may establish a planning program as an independent operation if a certain required procedure outlined in §100.117 is unsuccessful in establishing a joint planning unit encompassing the county and cities therein. Legislative bodies of cities and the fiscal court of the county containing the cities may enter into an agreement to form a joint planning unit by combining planning operations in order that they may carry out a joint city-county planning program.[2] Finally, legislative bodies of cities and counties comprising two or more adjacent planning units, whose combined territory forms a logical functional area, or portion thereof, may enter into an agreement to form a regional planning unit.[3]

An independent city planning unit may exercise extraterritorial jurisdiction for the purposes of subdivision regulations and, with the consent of the fiscal court, other regulations up to 5 miles from all points upon the city's boundary, but not beyond the county boundary, nor within the boundary of any city not in such a planning unit. The jurisdiction of joint and regional planning units is coterminous with their political boundaries. However, any planning unit may make planning studies of areas located outside its jurisdiction.[4]

Before a planning unit may engage in planning operations, a planning commission must be appointed for the unit in conformance with an adopted regulation or agreement.[5]

The planning commission of each unit prepares a comprehensive plan, which serves as a guide for public and private actions and decisions to assure the development of public and private property in the most appropriate manner.[6] The comprehensive plan must contain, as a minimum, a statement of goals and objectives to serve as a guide for the physical development and economic and social well-being of the planning unit; a land use plan element, showing proposals for the most desirable patterns for the general location of the manner in which the community should use its public and private land, covering public and private, residential, commercial, industrial, agricultural and recreational land uses; a transportation plan element; and a community facilities plan element showing proposals for the appropriate pattern for the location of public and semipublic buildings and land.[7]

Cities and counties which are members of a planning unit having adopted a land use plan element may divide the territory within their area of jurisdiction into zones to promote public health, safety, morals, and general welfare of the planning unit and to regulate population density and intensity of land use to provide for adequate light and air. Zoning may also be employed to provide for vehicle parking and loading space, to facilitate fire and police protection, and to prevent the overcrowding of land, blight, danger, and congestion in the circulation of people and commodities. Finally, zoning may be employed to protect airports, highways and other transportation facilities, pubiic schools and historical grounds, and business districts and natural resources.[8]

§100.203 provides that cities and counties may exercise the power to zone through zoning regulations, and indicates that cities and counties may regulate:

[122] Ark. Stat. Ann. §§ 19–3014 and 19–3038 (1968). See also notes 73–88 and accompanying text, supra.

[1] Kentucky Revised Statutes, § 100.113 (1969) [hereinafter cited as KRS].

[2] Id., § 100.121.

[3] Id., § 100.123.

[4] Id., § 100.131.

[5] Id., § 100.133ff.

[6] Id., § 100.183.

[7] Id., § 100.187.

[8] Id., § 100.187.

- Activities on the land;
- The size and location of structures, buildings, and signs;
- Minimum or maximum areas of open spaces left to be unoccupied and minimum distances between buildings;
- The intensity of use and the density of population floor area;
- Special districts like planned neighborhood and group housing districts and historical districts;
- Fringe areas of each district;
- Activities and structures of land near major thoroughfares.[9]

Before any zoning regulation may have legal effect within the planning unit, a board or boards of adjustments must be appointed for the planning unit to serve as the administrative body [10] (§100.217). The board has the power to hear and decide applications for conditional use permits [11] and applications for dimensional variances.[12]

On the State level, Chapter 147 of the Kentucky Revised Statutes sets up the Kentucky Progress Commission. It also provides guidelines for the State planning functions of the Governor's cabinet. Among the latter are making surveys of rural land utilization with a view to the determination of the areas suitable for field crops, reforestation, watershed protection, recreation, and urban expansion. The Governor's cabinet may also make maps, planning studies, and surveys relating to zoning, soil conditions, land use and classification, population distribution, schools, park and playground development, water supply, drainage and sewerage, long range financial programs, real property inventories, tax maps, building and housing conditions, subdivision control, and subjects affecting the general health and welfare.[13]

§147.610 enables any two or more adjacent counties, one of which has a city having a population of more than 50,000 and less than 200,000 inhabitants to establish an area planning commission (as provided by §100). Procedure for establishing a commission can be found in §147.620.

The master plans of all participating units of government, including all zoning ordinances and all action taken under authority of such ordinances, will continue and be in effect unless they are in conflict, as to planning, with actions taken by the Area Planning Commission.[14]

Besides having the power to tax,[15] the area planning commission also has the power and duty to establish a master plan of the entire area within its jurisdiction, including a land use plan with zoning areas.[16] The area land use plan may include the zoning plans now adopted by the various cities affected, but also include a map of the entire area of its jurisdiction showing the land use districts into which it is divided. The governmental unit under the jurisdiction of the area planning commission may adopt more strict regulations or impose higher standards of land use than adopted by the land use plan.

Another problem in the area of zoning is that of determining who is immune from local zoning ordinances. Generally, governments are only immune when the activities undertaken are of a governmental and not of a proprietary or corporate character.[17] Government projects, however, can be made subject to zoning regulations or exempted from them by the wording of the statute creating the project.[18] This question has not yet been litigated in Kentucky, however.

The primary Kentucky statute in this field is §80.110, which declares that all low cost housing projects are subject to the planning, zoning, sanitary and building laws, ordinances, and regulations applicable to the locality in which the project is situated. This seems consistent with the general rule enunciated above because a government housing project is more of a proprietary undertaking than a government function.

Regulations Governing Mobile Homes

Kentucky's laws governing mobile homes are found in §219 of the statutes. This act, the Kentucky Mobile Home and Recreational Vehicle Park Act, was passed in 1972.

Mobile home parks are under the control of the State Department of Health. Anyone wishing to operate a mobile home park must apply to the Department for a permit with a fee of $25, which is good for 1 year. Anyone wishing to construct a new park or to alter an existing one must apply for a permit and pay $25 also. No change in sanitary facilities—including the water supply, sanitary sewer, waste disposal system, sanitary

[9] Id.
[10] Id., § 100.217.
[11] Id., § 100.237.
[12] Id., § 100.241.
[13] Id., § 147.100.
[14] Id., § 147.650.
[15] Id., § 147.650.
[16] Id., § 147.660.
[17] § 1 ALR.2d 970, 973.
[18] Id. at 987.

station, watering station or service building—and no change in the plan of any existing park, or in any proposed park for which a permit to construct has been issued, is made without first having obtained a construction permit, except that a change from a private water supply or sewage system to a public water supply or sewage system does not require a construction permit.

A permit to construct, alter, or operate a park does not relieve the applicant from securing a local building permit if required, or from complying with any local zoning or other legal requirements.[19]

The board of health is authorized to adopt rules and regulations to effectively administer §219.310 to §219.410, which may include standards for park construction and layout, service buildings, watering stations, sanitary stations, sanitations, site planning, lot size, water supply, sewage disposal, lighting, refuse handling, insect and rodent control, inspections, hearings, issuance, suspension and revocation of permits, and such other matters as may be necessary to insure a safe and sanitary park operation. Officials and employees of the Department and of local health departments are empowered to enter upon the premises of any park at any reasonable time to inspect the premises. The local health department concerned, after notice to the applicant or holder of a permit, is authorized to deny, suspend, or revoke a permit where it finds a failure to comply with §§219.310–219.410, subject to hearings held in accordance with the regulations of the board of health. The county attorney, city attorney, attorney general, etc., are to enforce these provisions within their respective jurisdictions.

Nothing in §§219.310–219.410 is construed to include mobile homes or recreational vehicles maintained by any person on their premises and used exclusively to house their own farm labor.

Kentucky does have size limitation on house trailers that can travel on state highways—width not more than 8 feet and length nor more than 55 feet. A permit for a larger vehicle can be acquired from the department of highways under a display of special circumstances.[20]

Usury Laws

An outline of the current usury laws in Kentucky appears on the paper done for the Legal Research and Writing Program at Duke Law School (See Exhibit 1).

One important point to highlight is that two levels of acceptable maximum rates of interest are allowed in excess of the legal 6 percent rate. A maximum rate of 8.5 percent per annum may be charged 1) where a loan obligation in writing is secured by a "lien on one single family residential real estate property" [21] or, 2) where the original principal amount of the loan obligation in writing is $25,000 or less.[22] However, where a loan obligation in writing is in excess of $25,000 (and is not secured by a "lien on one single family residential real estate property"), the parties may contract to pay any rate of interest.[23]

Banks, trust companies, and other mortgagees approved by the Secretary of HUD, the FHA, and the Veterans' Administration are authorized to make certain loans that exempt them from the State usury laws.[24]

Finally, no corporation may plead or set up the taking of more than the legal rate of interest as a defense to any action brought against it to recover damages on, or to enforce payment of any mortgage, bond, note, or other obligation assumed by it.[25] This does not apply, however, to a corporation whose principal asset is the ownership of a one- or two-family dwelling.

Regulations Affecting the Homebuilding Construction Industry

Kentucky has no laws affecting the "home building construction industry" as such. However, it does have general regulations concerning the acquisition of land and the erection of buildings.

The fiscal court of any county is authorized to establish a land and building fund to be used for the purpose of acquiring lands and improving same, and for the erection, maintaining, improving, and reconstruction of necessary buildings in that county.[26] The fiscal court may purchase lands as it sees fit—title to be taken in the name of the county—and erect such improvements on it as the court deems necessary and proper. The fiscal court may fix a tax levy to be part of and included in the general fund levy. The amount realized from this levy is to be set aside for the building fund. Nothing in §68.125 is to be con-

[19] KRS, § 219.360(5) (1960).
[20] Id., § 189.275.

[21] Id., § 360.010(1)(a) and (2).
[22] Id., § 360.010(1)(b).
[23] Id., § 360.010(1)(c).
[24] Id., § 386.030, 69 Op. Atty. Gen. 35 (1969).
[25] Id., § 360.025(1).
[26] Id., § 68.125.

strued as affecting or limiting the right of any county to acquire lands or to improve lands, or erect or maintain buildings, as otherwise authorized by law.

Kentucky also has a State Property and Buildings Commission.[27] However, this authority is primarily concerned with State-owned buildings and property used for State purposes, particularly with respect to public school financing.[28]

State Housing Corporation

In 1972, the Kentucky legislature passed a bill creating the Kentucky Housing Corporation, currently codified in §198 A (Low Cost Housing) of the Kentucky Revised Statutes. The purpose of the bill is to create safe and sanitary housing in rural and urban areas that have deteriorated in recent years through the spread of slum conditions. Private enterprise and investment have not produced the needed amount of low cost housing, and State action is thought to be necessary to achieve this objective.

The corporation is governed by a board of directors and has the necessary powers to effectuate the legislation. Among these powers are: To make insured construction and/or mortgage loans to sponsors of land development or residential housing; to purchase insured mortgage loans made to such sponsors; to acquire real property by purchase, foreclosure, or otherwise; to sell all or any part of a mortgage or any document securing a construction, land development, or loan; to insure against loss; to consent to a modification of the usury rates; and, most importantly, to acquire, establish, and operate residential housing for persons and families of lower income.

Moreover, the housing corporation act does not stop merely at the construction of low cost housing. §198 A. 050 authorizes the director of the corporation to provide that training and employment arising in connection with the planning, construction, rehabilitation, and operation of housing assisted under such programs be given to persons of lower income residing in the area of such housing, wherever feasible. It provides further that contracts for work be awarded to individuals and business firms doing business in the fields of design, architecture, building construction, rehabilitation, maintenance, or repair, located in or owned in substantial part by persons residing in the area of such housing. Thus, the act encourages active participation by those it is created to help, by providing employment opportunities and stimulating business in the areas involved. This is an excellent idea in theory, but it is too early to tell how well it is working in practice.

The Commonwealth of Kentucky is not responsible in any way for any debts, liabilities, or obligations issued under the act.[29] These are payable solely from the revenues or assets of the corporation. The taxing power of the State is not used to assist in the payment of obligations of the corporation.

The act also created a housing loan fund, known as the Housing Development Fund, to be administered by the corporation as a trust fund separate and distinct from any other moneys or funds administered by the corporation. It is comprised of funds and contributions and of fund notes issued by the corporation.[30] The purpose of the fund is to provide a source from which the corporation may make temporary loans at such interest rates as may be determined by the corporation to be for its best interests for the purposes of defraying development costs of sponsors, developers, and builders of residential housing; or providing to families of lower income applying for mortgages funds to make downpayments and pay closing costs; or participating in construction loans which are not federally insured to sponsors, builders, and developers. Construction loans, however, will only be made from the fund when such loans are not otherwise available from private lenders upon reasonably equivalent terms.

The corporation is authorized to issue $200 million in bonds of the corporation to carry out is purposes, and may issue bond anticipation notes, interim receipts, or temporary bonds.[31]

In the discretion of the corporation, any obligations it undertakes may be secured by a trust agreement by and between the corporation and a corporate trustee, which may be any trust company or bank and trust company within or outside the State.[32]

Laws Affecting the Operation of Banks and Savings and Loan Associations in Home Mortgage Field

Any trust company or bank empowered to act as a fiduciary under Kentucky law and subject to examination by either State or Federal

[27] Id., § 56.450.
[28] Id., § 162.540.

[29] Id., § 198A.070.
[30] Id., § 198A.080 (1972 Supp.).
[31] Id., § 198A.090.
[32] Id., § 198A.100.

banking authorities, may set up a separate real estate mortgage fund, issue against such investment fund participation certificates covering fractional interests therein, and invest trust funds in its hands for investment in such participation certificates.[33] To provide for losses that might occur in such an investment fund, the bank or trust company may reserve, from the interest collected on the mortgages held in the fund, not over .5 percent per annum on the principal of such mortgages. The reserved amount is to be set aside in a separate account and used primarily to cover losses sustained in connection with any of the mortgages or in foreclosing mortgages. That reserve account, or any balance thereof after the payment of any losses, belongs to the beneficial owners of the investment fund.[34]

Every real estate loan must be evidenced by a note or bond for the amount of the loan, specifying the amount, rate of interest terms of repayment, and other pertinent information. Every such loan must be secured by a mortgage or other instrument constituting a first lien on the real estate securing the loan. The mortgage is to protect the savings and loan association and has to be properly recorded. Mortgages may also be made to secure existing debts or obligations, to secure debts created simultaneouly with the execution of the mortgage, and to secure future advances to be made at the option of the parties; all such debts and future advances are secured by such mortgage equally with all persons who acquire any right in the mortgaged real property subsequent to recording. Savings and loan associations may also pay taxes, assessments, insurance premiums, and other similar charges for the protection of its real estate loans. Such payments are added to the unpaid balance of the loan and are equally secured by the first lien on the property. An association may require life insurance to be assigned as an additional collateral upon any real estate loan. In that event, the association must obtain a first lien upon the policy and may advance premiums thereon. Such premium advances are to be added to the unpaid balance of the loan and equally secured by the first lien on the property.[35]

Health Laws and Regulations Affecting Safe and Sanitary Housing

Provisions dealing with safe and sanitary housing conditions are found in numerous parts of the Kentucky Revised Statutes.

Chapter 80 of the statutes deals with the powers of city and county governments. One of the powers granted is that to establish a local housing commission. One cannot be established, however, unless the local governing body finds that unsanitary or unsafe inhabited dwelling accommodations exist in such city or county, or that there is a shortage of safe or sanitary dwelling accommodations in such city or county available to persons of low income at rentals they can afford, and that these conditions can be best remedied through the exercise of the powers of a housing commission.[36] In determining whether dwellings are unsafe or unsanitary, a governing body takes into consideration the safety and sanitation of the dwellings, the light and air space available to the inhabitants thereof, the degree of overcrowding, the size and arrangement of rooms, and the extent to which conditions exist in such dwellings that endanger life or property by fire or other causes.[37]

Besides the city and county governments, the State Board of Health and local boards of health may also examine all nuisances, sources of filth, and causes of sickness that may be injurious to inhabitants of any county, whenever these are found to exist on any private property. The State Board of Health or local board of health may order the owner or occupant of the dwelling, in writing, to remove the nuisance at his own expense within 24 hours, or within such reasonable time thereafter as the board may order.[38] Local boards require the owner of any building containing two or more apartment units to provide waste receptacles for the purpose of eradicating rats and other unsanitary nuisances.[39]

The county, city-county, and district health departments may also issue written orders to the owner or occupant of any property, commanding compliance with applicable public health laws and regulations of the State and county boards of health. Any health officer may also institute and maintain mandatory or prohibitory injunction proceedings in the State circuit courts to abate nuisances and compel compliance with public health laws and regulations. The departments may also inspect any premises and view evidence and interrogate persons to the extent required. They may also issue subpenas, subpena

[33] Id., § 287.240 (1969).
[34] Id., § 287.250.
[35] Id., § 289.441.

[36] Id., § 80.380.
[37] Id., § 80.390.
[38] Id., § 212.210(1) (1973 Replacement Unit).
[39] Id., at (4).

duces tecum, and all necessary process in proceedings brought before or initiated by the department or board.[40]

The city-county board of health is authorized to make and enforce all reasonable regulations controlling or affecting the health of its citizens. Such regulations should generally be uniform throughout the county; however, the board is not precluded from making specific health regulations applying only to such sections of the county as may be deemed to require special treatment (§212.600). The board has the power to order the owner or occupant of property containing a nuisance in violation of any laws or regulations to correct and remove it.[41]

Another area involving safe housing is that of fire prevention. The commissioner of the State Department of Public Safety[42] is authorized to supervise and make periodic inspections of all property within the State, and assist cities having fire departments in making like periodic inspections of all property in such cities except occupied private dwellings.[43] The commission is also required to promulgate standards of safety for fire prevention and protection.[44]

This exception for private dwellings seems hard to explain except for the reason that local fire officials are more concerned with multifamily dwellings, which are probably owned by someone who does not live there and would have less desire to adhere diligently to the required fire regulations. In any case, it appears to serve no purpose to exclude occupied private dwellings entirely from the statute.

Finally, the Commissioner of Environmental Protection is empowered to establish sanitation districts within any county in the Commonwealth.[45] The purposes of such sanitation districts are to prevent pollution of streams, regulate the flow of streams for sanitary purposes, clean and improve stream channels for sanitary purposes, and to provide for the collection and disposal of sewage and other liquid wastes in the district.[46]

Requirements for Installation of Water and Waste Systems

A metropolitan area is authorized to create a joint metropolitan sewer district.[47] Briefly stated, the district has control and possession of the existing sewer and drainage system of cities and is empowered to maintain, operate, and improve it. It is also empowered to acquire by purchase, gift, condemnation, or otherwise, any real property needed to construct additions to the sewage system.[48] The district is also empowered to change rates and rentals for the use of the facilities.[49] The district may also approve the construction of private sewage systems subject to its examination and investigation.[50]

Counties are enabled to establish, by resolution of the fiscal court, a county public improvements finance commission, which is to be concerned with the construction and improvement of public facilities of the county, roads, expressways, drainage, and sewerage. The fiscal court may make appropriations for these facilities and improvements.[51]

Finally, where sanitation districts have been established in a county pursuant to §220.020, no person or public corporation is permitted to install within the district any laterals, trunk lines, interceptors for the collection or discharge of sewerage or other liquid waste, or treatment or disposal works, until such plans have been submitted to and approved by the board of directors of the district and the department of environmental protection.[52] Nothing in the chapter on sanitation districts[53] will limit or interfere with the right of public corporations to install, maintain, and operate sewerage systems as otherwise permitted by law.[54]

Environmental Protection

Kentucky Revised Statute (1969) §224.031 creates the department of environmental protection, headed by the commissioner. The duties and powers of the committee are many (see §224.033). One of the most important duties is to encourage industrial, commercial, residential, and community development that provides the best usage of land areas, maximizes environmental benefits, and minimizes the effects of less desirable environmental conditions.[55] There also exists an environmental quality commission, which serves basically in an advisory capacity to the commissioner.

[40] Id., § 212.245(b)(7).
[41] Id., § 212.620.
[42] Id., § 17.010 (1969).
[43] Id., § 227.220 (1973 Replacement Unit).
[44] Id., § 227.300.
[45] Id., § 220.020.
[46] Id., § 220.030.
[47] Id., § 76.010 and §§ 76.080—76.100 (1969).
[48] Id., § 76.080.
[49] Id., § 76.090.
[50] Id., § 76.085.
[51] Id., § 66.550.
[52] Id., § 220.260 (1973 Replacement Unit).
[53] Id., § 220.
[54] Id., § 220.280(3).
[55] Id., § 224.033(3).

The substantive provisions control throwing waste into waters in the State,[56] disposing waste on land,[57] noise pollution,[58] and air pollution.[59] Whenever the commissioner finds a violation of the statute, he orders the violator, in writing and without prior hearing, to discontinue the activity. He is also empowered to adopt any rules and regulations prescribing the procedure to be followed in the issuing of such orders.[60]

Any corporation authorized to do business in the State, and organized for the purpose of constructing, maintaining, and operating sewer lines and sewage treatment facilities, may condemn rights-of-way necessary for operating and constructing its pipelines under certain conditions; before it does this, however, the corporation must have presented plans and specifications to the department of environmental protection and received a permit from it to operate and maintain sewage treatment facilities.[61] (§224.130). Also, any person having primary responsiblity for the operation of any sewage system—whether publicly or privately owned—must pass an examination prescribed by the department testing his skill before he will be allowed to operate the system.[62]

There also exists the Kentucky Pollution Abatement Authority, a public corporation and government agency of the State.[63] The Authority is authorized to make State grants, as funds are available, to any governmental agency to assist such agency to carry out the construction of waste water treatment works which will constitute an eligible project.[64] The Authority also may levy a tax on every purchase of water service in the Commonwealth, subject to restrictions.[65]

Welfare Laws

The Department of Economic Security exercises all State functions in relation to, inter alia, the administration and supervision of all forms of public assistance including general home relief.[66] There also exist departments of welfare in first-class cities,[67] with essential powers relating to unstable families, delinquency, special homes for the infirm, and other local problems.[68]

First-class cities that have paid general assistance to any person through the department of public welfare of that city have a claim against the estate of any such deceased person. The claim has priority over all unsecured claims against such estate, except the burial expenses of the decedent, the cost of administration of his estate, the cost of his last illness, and claims by the Commonwealth of Kentucky for public assistance rendered by it to the decedent.[69]

The city also has a lien on all real estate and rights to real estate belonging or thereafter acquired by any recipient of general assistance through the city's department of public welfare. The lien includes all payments made to the recipient and continues until it is satisfied. However, the lien is not effectual as against any mortgagee, purchaser, or judgment creditor without actual notice, until notice has been filed by the director of public welfare with the clerk of the county court. The lien is not enforceable while the real estate is occupied by the surviving spouse (or until she remarries) or is occupied by a dependent child, provided no other action is brought to settle the estate. Wherever it appears to be in the best interests of the recipient to sell his real estate and reinvest the proceeds in other real estate, the department may grant permission and waive the lien to the extent necessary for the purpose of effecting the transfer, but such lien attaches to the reinvested property.[70]

A county department of welfare may also be created in any county containing a first-class city, whenever the fiscal court for that county so resolves.[71]

Sales Tax

There is a 5 percent tax on all retailers' gross receipts on sales made in Kentucky. The tax has been in effect since April 1, 1968.[72]

Taxation of Mobile and Modular Units

The statutory law in Kentucky is that if the wheels or mobile parts have been removed from a housetrailer or mobile home, and the unit rests on a fixed, permanent foundation, it shall be classified as real estate.[73] Generally, however,

[56] Id., § 224.060.
[57] Id., § 224.255, 260.
[58] Id., § 224.065.
[59] Id., § 224.330.
[60] Id., § 224.071.
[61] Id., § 224.130.
[62] Id., § 224.135.
[63] Id., § 224A.030.
[64] Id., § 224A.040.
[65] Id., § 224A.060.
[66] Id., §§ 195.010 to .020 (1969).
[67] Id., § 83.160.

[68] Id., § 98.010.
[69] Id., § 98.012.
[70] Id., § 98.013.
[71] Id., § 98.300.
[72] Id., § 139.200.
[73] Id., § 132.750.

housetrailers are termed as personal property, and the presumption is that they are subject to local property taxes wherever they are found.[74] This seems consistent with §132.485(2), which dictates that housetrailers be assessed at the same standards as those used for valuing motor vehicles.

I was unable to find any material on whether mobile and modular units were taxed as personal or real property as they left the factory, but it would seem from the above that at least mobile homes would be classified as personal property.

Building Standards

The fiscal court of any county has the authority to adopt and enforce regulations governing the construction, reconstruction, repair, and maintenance of buildings, except for buildings for agricultural purposes.[75] The fiscal court of any county containing a first-class city may, after a public hearing, adopt and enforce similar regulations concerning buildings located within unincorporated areas of the county, and also within the corporate limits of any city in such county not having such regulations (except for buildings used solely for agricultural purposes located on premises used solely for agricultural purposes).[76] If a first-class city has, in effect, a building ordinance, the fiscal court of the county in which the city is located may adopt the provisions of such ordinance, or any part thereof, for the area of the county outside the corporate limits of that city.[77] The fiscal court of any county containing a first- or second-class city may appoint a "building inspector." No person is allowed to build, remodel, or repair any building without first obtaining a building permit from the building inspector.[78]

Thus, Kentucky has no uniform State building code, but leaves such regulation to the individual counties and cities. Buildings must also meet the health regulations discussed below.

Suits if Landlord Fails to Meet Codes

In case any building or structure is or is proposed to be erected, reconstructed, repaired, or maintained in violation of any reasonable regulations adopted by the fiscal courts of the counties, the county attorney, or any property owner or occupant who would be damaged by such violation, may in addition to other remedies provided by law institute injunction, mandamus, abatement, or other approriate action to prevent, enjoin, or remove such unlawful activity.[79] Tenant suits for damages are thus permitted if a landlord fails to meet the building codes.

Tenant's Right to Withhold Payment if Unit Does Not Comply with Housing Code

There is no statutory law in Kentucky justifying a tenant's withholding payment of rent if the unit he lives in does not comply with the minimum housing code. Generally, whether a tenant can withhold rent under these conditions depends on whether there is a warrant of habitability in the lease.[80] One Kentucky case[81] held that a clause in a lease permitting surrender of the premises in case of accident by fire and the elements and other unavoidable accidents so as to make the premises untenantable, does not justify surrender if the premises become infested with vermin. Another case[82] held that the lessee of property damaged by flood who exercises an option to cancel the lease, but refuses to surrender the property to the lessor, is liable for rent.

The exact question at issue, however, has not been litigated in Kentucky. Courts in other States with statutes exempting the tenant from paying rent under these circumstances have been inconsistent in construing the statutes.[83] The only Kentucky statute in the field provides that a tenant, unless he otherwise contracts, is not liable for the remainder of his term for the rent of any building leased by him and destroyed during the term by fire or other casualty without his fault or neglect.[84]

Repair, Closing, or Demolition of Unfit Structures by Cities and Counties

If an owner fails to comply with an order to repair, alter, improve, or vacate the structure, the public officer authorized by county law may cause the structure to be repaired, altered, im-

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[74] Op. Atty. Gen. 70–768.
[75] KRS, § 67.380 (1969).
[76] Id., § 67.390.
[77] Id., § 67.400.
[78] Id., § 67.410.
[79] Id., § 67.420.
[80] 61 ALR.2d 1445.
[81] *Owens v. Ramsey*, 213 Ky. 279, 280 S.W. 1112; 52 ALR 149 (1926).
[82] *Brunswick Corp. v. Goodie Investments*, 451 S.W.2d 421 (1970).
[83] *Tompkins Square Holding Co. v. Gilson*, 167 Misc. 77, 2 NYS.2d 714 (1938); compare *Burlington and S. Apartments v. Manolato*, 233 Iowa 15; 7 N.W.2d 26; 144 ALR 251 (1942).
[84] KRS, § 383.170 (1969).

proved, vacated, and closed, or demolished. The amount of the cost of repairs, alterations or improvements, vacating, and closing or demolition will be deemed a lien upon the real property upon which cost was incurred. If the structure is removed or demolished by the public officer, he sets the materials of the structure and credits the proceeds of such sales against the cost of the removal; any balance remaining is deposited in the circuit court by the public officer, and disbursed by that court to the persons found to be entitled thereto.[85]

(The full procedure to be followed can be found in Kentucky Revised Statutes (1969), §§80.620–80.720, Repair, Closing or Demolition of Unfit Structures by Cities and Counties.)

Housing Courts

There are no housing courts as such in Kentucky. Matters dealing with real property are dealt with by two different types of State courts—circuit courts and fiscal courts.

The circuit courts are courts of record. They have original jurisdiction of all matters, in law and equity, in which the jurisdiction is not exclusively delegated to some other tribunal. They also have jurisdiction in all cases where title to land is in question, or in which it is sought to enforce a lien upon, or to subject, land by provisional remedy to the payment of debt.[86]

Fiscal courts serve an altogether different function. One is located in each county, and they act in a proprietary capacity for the county government. They are empowered to appropriate county funds; sell real estate for the county; buy real estate for the county for the purpose of erecting public buildings thereon; appoint commissioners to do such selling or buying; erect and keep in repair necessary public buildings, bridges, and other structures; secure a sufficient jail and a place for holding court; and regulate and control generally the fiscal affairs of the county.[87]

Court Appointment of a Receiver

In Kentucky, a circuit court is empowered to appoint a receiver in an action by a mortgagee for the sale of the mortgaged property if it appears that the property is in danger of being lost or injured, or if the condition of the mortgage has not been performed and the property is insufficient to discharge the mortgage debt.[88] Although the appointment of a receiver is subject to the discretion of the court, there is much support for the appointment of one to collect rents on mortgaged property securing them for the benefit of the mortgagee. However, where the property itself is sufficient to satisfy the mortgage debt, the appointment of a receiver to collect rents has been denied.[89]

The court may also appoint a receiver to take charge of any property or fund during the pendency of the action and may order the delivery of it to him on the motion of any party to an action who shows that he has, or probably has, a right to, a lien upon, or an interest in, the property or fund, the right to which is involved in the action, and that the property or fund is in danger of being lost, removed, or materially injured. The order of the court or of the judge thereof, appointing or refusing to appoint a receiver, is—for appeal purposes—a final order.[90]

The receiver has power, under the control of the court, to bring and defend actions, to take and keep possession of the property, to receive rents, collect debts, and generally to do such acts respecting the property as the court may authorize.[91]

Thus, there is no statutory authority for a court to appoint a receiver to make improvements as such. Although there is no direct authority under Kentucky law, however, the rule elsewhere is that a receiver who is appointed with authority "to make such repairs as are necessary for the proper maintenance of the property in his charge" may make immediate minor repairs upon rented property without application to the court if the existing or probable income therefrom justifies it, or if such minor expenditure are necessary to conserve the property. If the expenditures for the proposed repairs are unusual or substantial, however, the receiver should apply to the court for authority to make them, and notice should be given to interested parties, thus giving them an opportunity to be heard.[92]

Foreclosing on Tax Delinquent Dwellings

The Kentucky statutes do provide for a method of foreclosing on tax delinquent dwell-

[85] Id., § 80.670.
[86] Id., § 23.010.
[87] Id., § 67.080.

[88] Id., § 27.035.
[89] *Mortgage Union* v. *King,* 245 Ky. 691; 54 S.W.2d 49 (1932).
[90] KRS, § 27.061 (1969).
[91] Id., § 27.064.
[92] *American Savings Bank Co.* v. *Union Trust Co.,* 124 Ohio 126; 177 N.E. 199; 79 ALR 160 (1931).

ings in first-class cities, but it can be used only where the taxpayer has no personal property out of which the tax bill can be collected. If this is the case, the local tax receiver will sell for cash a sufficient amount of the real property belonging to the taxpayer to pay taxes, interest, and costs. The sale will be at public auction, in the same manner that property is sold under execution, except that the sale is to be held at the door of the city hall in the city where the land lies, and the land need not be appraised or levied on. The sale is to be advertised by posting a written or printed notice at the city hall door for 15 days before the sale, and by publication pursuant to Kentucky Revised Statute §424.[93]

Not less than 15 days before the sale, the tax receiver will mail to the taxpayer a postcard notifying him of the time and place of sale. To cover the cost of advertisement and notification, the tax receiver will collect a fee of $2 from each person whose property is advertised, and shall pay the fee into the city treasury.[94]

The failure of the tax receiver to send, or of the taxpayer to receive, notice of the sale will not invalidate the sale or any subsequent proceedings thereunder, and no levy or attempted levy upon personal property will be necessary to validate any sale of real property, whether for taxes on real property, personal property, or both.[95]

Legal Authority for Tax Officials to Maintain Existing Levels of Assessment Following Improvement of Substandard Housing

There is no legal authority in Kentucky authorizing tax officials to maintain existing levels of assessment following improvement of substandard housing.[96]

Mortgages

There is no Kentucky legislation permitting "flexible" mortgage financing. There is no State legislation permitting open-end mortgages either.

Insurance

There is no Kentucky legislation requiring insurance companies doing business in the State to write fire insurance in substandard areas. Insurers are permitted to invest in stock or obligations of every housing company or redevelopment company, or of any corporation, organized for the purpose of owning and operating any housing project under the laws expressly designed to promote housing for persons of low or moderate income.[97]

Housing Authorities

Kentucky allows both county and regional housing commissions under the provisions of §80.310 and the following materials. County commissions are created for only one county, but the regional commissions can be created by the governing bodies of two or more contiguous counties.[98] The area of operation of such a regional housing commission will be the counties for which it is established; this area may be increased to allow the addition of one or more contiguous counties not already within a regional housing commission.[99] The area of operation of a regional housing commission may also be decreased from time to time to exclude one or more counties from the area.[100] No housing commission may be established without a finding by the governing body within the city or county involved that, first, there are unsanitary or unsafe inhabited dwellings in the city or county, or that there is a shortage of safe or sanitary dwellings for people of low income; and, second, that these conditions can be best remedied through the exercise of the powers of a housing commission.[101]

There is no authority for the creation of statewide housing authorities except insofar as the areas of regional housing commissions can be increased through the procedure of §80.340. There does exist in Kentucky a State Property and Buildings Commission, but that commission only undertakes building projects for State agencies.[102]

Housing Redevelopment Corporations

Kentucky Revised Statute (1969) §99.100 authorized the creation of redevelopment corporations by interested persons. That statute, however, placed a 20-year time limit on the creation

[93] KRS, § 91.480(1) (1969).
[94] Id. at (2).
[95] Id. at (3).
[96] See 90 ALR 1137 for a good study of "public property" subject to special assessment for improvement, but the section specifically excludes cases dealing with assessment for local improvements to property of quasi-public corporations as beyond its scope.

[97] KRS, § 304.7–220 (1969).
[98] Id., § 80.320.
[99] Id., § 80.340.
[100] Id., § 80.350.
[101] Id., § 80.380.
[102] Id., § 56.450.

of such corporations commencing on June 1, 1942, and it is unclear whether this period has been extended. If it has not been, then the broad regulations of the sections following §99.100 pertain only to such corporations founded between June 1, 1942, and June 1, 1962.

The purposes of redevelopment corporations are the founding and putting into effect of a development plan, and the acquisition of real property for such a redevelopment plan. General corporation law applies to such corporations.[103] Land may be condemned for the use of the corporation upon proper showing of necessity for such condemnation by it.[104] A redevelopment corporation may borrow money and execute mortgages.[105] Certificates, bonds, and notes secured by a first mortgage on the real property in a development area are securities which may be legally invested in by various entities.[106] Obligations that are insured under the Federal Housing Act are not subject to investment limits.[107]

Exhibit 1: Usury Laws

Aside from the 6 percent legal rate of interest, Kentucky completely revised its basic usury statute in 1972 to create an interest structure with two levels of acceptable maximum rates. Ky. Rev. Stat. Ann. §360.010 (1), 2 CCH Cons. Or. Guide, Ky. ¶6401 (1972). A maximum rate of 8.5 percent per annum may be charged in two situations: (1) Where a loan obligation in writing is secured by a "lien on one single unit family residential real estate property" (Id., §360.010 (1)(a)), and (2) where the original principal amount of the loan obligation in writing is $25,000 or less (Id., §360.010 (1)(b)). On the other hand, where the loan obligation in writing (other than that mentioned in §360.010 (1)(a) above) is in excess of $25,000, the parties may contract to pay any rate of interest. Id., §360.010 (1)(c).

Corporations may not plead usury as a defense, §360.025(1), unless the corporation's principal asset is a one- or two-family dwelling. §360.025(2). See also 70 Op. Att'y Gen. 727 (1970), taking the position that §360.025 does not constitute an arbitrary and unreasonable classification and is therefore constitutional. This section also precludes individual guarantors, sureties, and endorsers on corporate obligations from injecting a usury defense. *E'Town Shopping Center, Inc.* v. *Lexington Finance Co.*, 436 S.W. 2d 267 (Ky. Ct. App. 1969). Further, FHA and VA loans are considered to be excluded from the coverage of the foregoing statutes, 70 Op. Att. Gen. 782 (1970); 69 Op. Att'y Gen. 35 (1969).

The attorney general of Kentucky has taken the position that points are considered to be interest and must be amortized over the life of the loan for calculation of the applicable percentage rate. He stated that: "A lender may collect 'points' when prorated over the full term of the loan and added to the stated interest does not result in total interest being collected in excess of the maximum interest rate." (70 Op. Att'y Gen. 284 (1970).) He further defined "points" as being synonymous with bonus, premium, discount, or any one-time consideration paid by the borrower to the lender at the inception of the loan as additional compensation therefor.

In Kentucky, service charge may be lawfully charged to the borrower in addition to the maximum interest. Such charge, however, must represent reasonable expenses incident to the making of the loan *Harding* v. *Kentucky Title Trust Co.*, 269 Ky. 622, 108 S.W. 2d 539, 548 (1937); accord, *Ashland National Bank* v. *Conley*, 231 Ky. 844, 22 S.W. 2d 270 (1929); 70 Op. Att'y Gen. 276 (1970)). While a borrower may pay a brokerage fee or commission to his own agent for procuring a loan, such charges by a lender or his agent will be considered interest (*Union Central Life Insurance Co.* v. *Edwards*, 219 Ky. 748, 294 S.W. 50 (1927)).

While subject to disclosure and prepayment controls (Ky. Rev. Stat. Ann. §§371.220(g), 371.260(2)) a time-price differential is specifically authorized by statute (§371.260(1)). Even though there is no case law specifically exempting a time-price differential from the general usury statute, the language of §371.260(1), viz.: "Notwithstanding the provisions of any other law, a retail installment contract . . . may provide for, . . . a time price differential," could be fairly read as precluding control of retail installment contracts charging time-price differentials by the general usury law. This statute however, does not itself set maximum limits on time-price differentials; therefore, the only limits thereon appear to be the market and the omnipresent doctrine of unconscienability, cf. *Williams* v. *Walker-Thomas Furniture Co.*, 121 U.S. App. D.C. 315, 350 P. 2d 445. 18 A.L.R. 3d 1297 (1965).

[103] Id., § 99.150.
[104] Id., § 99.220.
[105] Id., § 99.260.
[106] Id., § 99.270.
[107] Id., § 99.280.

Mississippi Report on Legislation

Land Use Planning and Zoning

In the State of Mississippi, the local units of government are charged with the responsibility of controlling land use. On the county level, the board of supervisors—the governing unit at the county level—is empowered to zone unincorporated portions of the county according to such factors as the size and height of buildings, location and use of buildings, density of the population, and the percentage of any lot which may be occupied by structures.[1] Agricultural buildings and land used for agricultural purposes are exempted from the county zoning power.[2]

Counties are given broad power to enforce zoning regulations, including restraining con-

[1] Miss. Code Ann., § 17–1–3 (1972).
[2] Id., § 17–1–3.

struction, causing repair, and preventing occupancy of any structure or land which is in violation of the provisions of local zoning laws.[3]

In conjunction with the authority to zone, counties are also authorized to regulate the development of subdivisions in the State. Each county may impose restrictions on a subdivision necessary to effectuate local zoning ordinances and may require approval by the board of supervisors before a subdivision or plat is recorded in the county.[4]

Zoning is not limited in its scope to the confines of any one county. All of the local units of government, municipalities, and counties are permitted to act with other local units to achieve uniform planning consistent with public health and welfare goals.[5]

To achieve the goals of county zoning and planning more effectively, counties are authorized to create planning commissions to develop comprehensive plans for county development.[6] Two or more counties may create a regional planning commission to achieve the same purposes, but on a broader, more comprehensive scale.[7] Where the necessity arises, interstate regional planning is authorized by statute.[8]

Building and Housing Codes

Counties are authorized to adopt building codes for the unincorporated portions of the county, but are restricted to adopting a code no stricter than that promulgated by a national code group.[9] Such building codes may set minimum standards for electrical work, plumbing, gas, and sanitary facilities.[10] Such codes will not be applied to farm buildings and structures. No statutorily defined method of enforcement of the adopted codes is prescribed. This seems to indicate that the counties may promulgate their own enforcement procedures as a necessary extention of their authority to adopt a code.

Municipalities are not restricted in regard to the type of building codes they adopt, but are authorized to promulgate codes concerning electrical work, plumbing, gas, and sanitary facilities.[11]

There is no authority for permitting county boards of supervisors to adopt minimum housing codes, and it appears that the power of that body is an extremely limited one. The State constitution leaves the matter of the scope of county board of supervisor's power to the discretion of the State legislature.[12] The State legislature appears not to have adopted legislation granting general power to the counties to promote public health and welfare. Without a board grant of power or the specific grant of power to promulgate a housing code, it is, at least, uncertain whether county governments have the requisite power to establish minimum housing codes in their respective jurisdictions. This lack of power is of some advantage to a Federal housing effort. Where there is no regulation of any sort, great flexibility in the form of the Federal approach may be permissible.

The State of Mississippi has not adopted a statewide minimum housing code or a statewide building code.

Very little innovation has been added to the law of landlord and tenant since the initial codification of that body of law in 1848.[13] Thus there is little in the way of landlord-tenant law that is designed to induce the enforcement of local building codes or housing codes. (This assumes that housing codes are a permissible function of the county board of supervisors). Specifically, there are no provisions of statutory law nor any case law that indicate that a tenant may withhold payment of rent if the rented premises are substandard. Indeed, following the basic common law position, it is not incumbent on a lessor to repair the leased premises at all.[14] Any such responsibility is a creature of contract and must be incorporated in the lease agreement to be enforcible against the lessor.[15]

Other innovations in landlord-tenant law fail to appear in the statutory or case law. For instance, there is no provision for a receiver to collect rent and make the necessary repairs on housing which is substandard, but there does appear a provision for a municipality to make repairs on substandard housing and retain a lien on that housing for the amount of the repair cost. (See Miss. Code Ann. §43–35–105). Similarly, there appears to be no specialized adjudi-

[3] Id., § 17–1–19.
[4] Id., § 17–1–23(1), (2).
[5] Id., § 17–1–5.
[6] Id., § 17–1–11.
[7] Id., § 17–1–29.
[8] Id., § 17–1–29.
[9] Id., § 19–5–9.
[10] Id., § 19–5–9.
[11] Id., § 21–19–25.

[12] Mississippi Constitution Art. 6, § 170, Miss. Code Ann., § A–3–41 (1972).
[13] See, Miss. Code Ann., § 897 et seq. (1956).
[14] *Cousey* v. *Norwood*, 156 So.592, 170 Miss. 874 (1934).
[15] *Miller* v. *Miller* 64 So.2d 1739, 217 Miss. 650, 38 A.L.R.2d 674 (1953); *Rich* v. *Swalling*, 137 So.325, 161 Miss. 503 (1931).

catory body which hears only housing-related matters.

On the county level, the power to repair, renovate, and remove substandard housing resides in the county housing authorities which the board of supervisors of each county are empowered to activate.[16] The housing authorities, to promote the goal of providing safe and sanitary housing, are empowered to purchase, lease, or exercise the power of eminent domain.[17] Obviously, the power to renovate, repair, and remove substandard housing is highly circumscribed by the limited sphere of the housing authority power. The county board of supervisors is not specifically granted such power, and it appears unclear whether it may do so.[18]

On the municipal level, the local governing authority is specifically authorized to enact ordinances governing what constitutes housing unfit for human habitation.[19] And they are empowered to appoint an official whose function it is to inspect, and order the necessary repairs or demolition, as each case would require.[20] State law outlines the criteria which the local municipality must follow in enacting the appropriate legislation.[21] Among these are defects which increase the chance of fire or accident; lack of adequate light; ventilation or sanitary facilities; and dilapidation, disrepair, or structural defect.[22]

Outside of local building code regulation, there appears to be no other restriction on construction of buildings in the State of Mississippi. The State fire marshal is not empowered to promulgate regulations concerning such things as electrical wiring, nor does he have any jurisdiction over residential housing unless it should come to his attention that a hazardous condition exists in any building.[23] If this happens, the fire marshal is authorized to take appropriate action through the attorney general's office.[24] But it would appear that this kind of weak regulation does not present any problems in the context of implementing a Federal program of rural housing.

Environmental and Health Regulations

There exists little health or environmental legislation in the State of Mississippi which has any significant impact on rural housing. The Mississippi Department of Public Health is largely an advisory and information-gathering body and wields no effective regulatory or enforcement power.[25] On the other hand, the Mississippi State Board of Health is empowered with extensive rulemaking authority to deal with problems impinging on public health.[26] One area in which the board of health is specifically charged with establishing health regulation concerns the sanitary facilities of mobile homes and trailer parks.[27] Within this responsibility lies a permissive grant to promulgate regulations concerning maintenance, regulation, inspection, equipment, and control of house trailers as well as house camps. Also included in the board's authority is the power to register the trailers.[28]

Enforcement of board of health regulations is carried out by board-appointed county health officers.[29] Because these officers are appointed by the State board and for a 2-year term, it would appear that the State board has effective control over the enforcement process. This would seem to be true even in the face of the existence of county boards of health. This is due to the limited advisory, publicity, and information-gathering functions that the county boards perform.[30] County health departments are also authorized, but it seems—although it is unclear—that they operate essentially as arms of State health operations. They are funded by the individual counties.[31]

Other than the specific authorization to promulgate rules concerning mobile homes, there appear to be no other specific legislative directives to promulgate housing-related regulations.

In the environmental area, Mississippi has enacted the "Mississippi Air and Water Pollution Control Act." [32] The act creates the Air and Water Pollution Control Commission, which has the authority to set standards for water quality.[33] The act makes it unlawful to discharge wastes below commission standards [34] and requires that a permit be procured from the commission whenever waste disposal systems are modified or constructed.[35] The commission may also require that plans for waste disposal system be

[16] Miss. Code Ann., § 43-33-5 (1972).
[17] Id., §§ 43-33-11, 43-33-13.
[18] See, Id., § 19-3-41.
[19] Id., § 45-35-103.
[20] Id., § 45-35-105.
[21] Id., § 45-35-107.
[22] Id.
[23] Id., § 45-11-3.
[24] Id.

[25] Id., § 45-1-7.
[26] Id., § 41-3-17.
[27] Id., § 41-25-13.
[28] Id.
[29] Id., § 41-3-41.
[30] Id., § 41-3-55.
[31] Id., § 41-3-53.
[32] Id., §§ 49-17-1 et seq. (1956).
[33] Id., § 49-17-19 (1972).
[34] Id., § 49-17-29(b).
[35] Id.

submitted for commission approval prior to their construction.[36] It is unclear what impact this commission would have on the development of rural housing, but it seems reasonable to assume that regulations will be promulgated and designed to affect the "big" polluters—for example, large industrial concerns—and not housing.

Other environmental constraints, such as the Mississippi Solid Waste Regulation,[37] have no substantial impact on the development of low cost rural housing.

Mobile Homes and Modular Housing

Besides the regulations promulgated by the State board of health, mobile homes are regulated by two separate legislative acts, "The Uniform Standards Code for Factory Manufactured Movable Homes Act" [38] and "The Uniform Highway Traffic Regulation Act." [39]

The Uniform Standards Code Act is aimed at the problem of inspection of already-constructed mobile homes and other factory-built housing. The commissioner of insurance is authorized to promulgate rules and regulations relating to the properties of the construction materials, and the standards for construction of electrical, plumbing, and other systems pursuant to U.S.A. Standard A119.1, recommended by the United States of America Standards Institute.[40] To insure that these standards are followed, the commissioner is granted broad power to specify the procedure necessary for inspection or other procedures of enforcement.[41]

All manufacturers and dealers of factory-built housing are required to obtain licenses annually upon certification that the applicable construction standards will be met.[42] Licenses can only be revoked after the appropriate hearing and notice, when there has been noncompliance with the applicable regulations.[43]

The other area in which State regulation affects mobile homes concerns the regulation of size and length of vehicles on State highways. The permissible width of any vehicle on State highways is 8 feet.[44] The maximum length permitted is 35 feet, whether the vehicle is a single unit or a combination of units.[45] At first blush, these regulations seem to present a problem for the transportation of mobile homes and modular units in the State, but the State highway commission is authorized to issue, at its discretion, permits authorizing loads in excess of statutory standards upon application of the party seeking to move the load.[46]

The State of Mississippi has an interesting approach to the taxation of mobile homes. Each mobile homeowner is required to register his home with the county assessor in the county where his home is located.[47] At that point, the assessor issues a registration sticker and assesses the value of the mobile home.[48] If the mobile home is situated on land that does not belong to the owner of the mobile home, the owner must declare his mobile home as personal property at the time of assessment.[49] Mobile homes which are situated on property owned by the owner of the mobile home may be declared, at the time of assessment, either personal or real property, at the owner's discretion.[50] Once the owner has treated his mobile home as personal property, he may later treat it as real property if he so chooses.[51] Mississippi law clarifies the problem that often arises concerning taxation of mobile homes that are transported over the highways. Section 27–15–5 of the 1972 code specifically exempts mobile homes from the ad valorem taxation of motor vehicles.

There are no specific legislative enactments dealing with the question of how modular housing is taxed, but, viewing the general language of the statute on ad valorem real estate taxation [52] and the treatment of mobile homes for tax purposes, it appears that they may be taxed as real property rather than as personal property; but this is not totally clear.

Finance and Usury

Outside of the usury laws, there is little in the way of legislation that impinges on the ability of savings and loan associations and banks to use innovative mortgage arrangements. The law concerning such approaches as flexible mortgages or open-end mortgages is nonexistent. It therefore must be assumed that such ap-

[36] Id., § 49–17–19.
[37] *BNA-Environmental Reporter, State Solid Waste—Land Use,* p. 1221–0501.
[38] Miss. Code Ann., §§ 5131–101 et seq. (1972).
[39] Id., §§ 63–5–1 et seq.
[40] Id., § 5131–103 (1972 Supp.).
[41] Id.
[42] Id., § 5131–105.
[43] Id., § 5131–107.
[44] Id., § 63–5–13 (1972).
[45] Id., § 63–5–19.
[46] Id., § 63–5–51.
[47] Id., § 27–53–5.
[48] Id., § 27–53–7.
[49] Id., § 27–53–13.
[50] Id., § 27–53–15.
[51] Id., § 27–53–15.
[52] Id., § 27–35–49.

proaches are presently permissible in Mississippi.

Savings and loan associations have some restrictions in the mortgage arrangements they may deal in. They may only lend money on secondary mortgages if they own all the paramount liens on the mortgaged property.[53] Savings and loan associations cannot deal in loans secured by personal property unless it is in conjunction with real property.[54] But outside of these relatively minimal restrictions, there is no other regulation of mortgage financing.

The maximum rate of interest on loans in Mississippi is 8 percent.[55] However, loans insured by the Federal Housing Administration or guaranteed by the Veterans' Administration are specifically exempted from the constraints of the usury laws.[56]

It appears that both discounts and points are included in interest for usury purposes.[57] The statutes speak in terms of the amount received, directly or indirectly, by the lender as includible in interest.[58] The Mississippi Supreme Court has specifically recognized that discounts are interest.[59]

Certain other charges made to compensate for expenses in making a loan have been determined not to be interest. Such reasonable charges are not deemed to be consideration for the loan but, rather, compensation for services rendered.[60]

Mississippi has long recognized the time-price differential as being exempt from the usury laws if the sale was bona fide.[61] The only area in which the time-price differential is regulated is in the area of motor vehicle financing, when the cost of the vehicle is less than $7,500.[62]

Housing Law and Housing Authorities

Mississippi has no law enabling the establishment of State housing corporations, nor is there any legislation concerning housing development corporations.

The main body of housing law in Mississippi concerns the local housing authorities, although regional authorities are authorized. Under the "Housing Authorities Law," each municipality and county is authorized to activate a local housing authority.[63] Each county housing authority is governed by a five-member commission appointed by the county board of supervisors.[64] The authorities are empowered to exercise the necessary functions to establish low cost housing for low income people.[65] Among these powers are the power to buy, sell, rent, contract, and exercise the power of eminent domain.[66]

Each housing authority is required to fix rentals at the lowest possible rate consistent with the goal of providing safe and sanitary housing and meeting the demand of the financing of such housing.[67] Persons admitted to projects administered by any housing authority may not earn more than 5 times the annual rental of a unit in the project, subject to the proviso that $100 may be deducted for each minor dependent of any person seeking admission.[68]

Local regulations, including zoning and land use planning ordinances, are applicable to all housing authority projects,[69] but they are exempt from property taxes.[70]

An interesting feature of the "Housing Authority Law" is the provision that individual farmers may apply to county or regional housing authorities for housing for those farmers who operate or work on the owner's farm.[71]

Both cooperative [72] and regional [73] housing authorities are permitted by present legislation. A regional authority may be created when the boards of supervisors of two or more contiguous counties determine that there is need for an agency to exercise the powers of a housing authority on a broader scale.[74] The powers of the regional housing authority are essentially the same as those granted to county and municipal housing authorities.[75] Importantly, county and regional authorities are specifically authorized to engage in the establishment of rural housing projects (e.g., projects outside of the corporate boundaries of any municipality).[76] This is of some significance because it is clear that au-

[53] Id., § 5288–15 (1972 Supp.).
[54] Id.
[55] Id., § 36 (1966).
[56] Id., § 43–33–307 (1972).
[57] Id., §§ 36, 37 (1966).
[58] Id.
[59] *Hyde* v. *Finley*, 26 Miss. 468 (1853); accord *Hiller* v. *Ellis*, 72 Miss. 701, 18 So.95 (1895); *Polkinghorne* v. *Hendricks*, 61 Miss. 366 (1883).
[60] *Johnson v. Caster* 203 Miss. 38, 33 So.2d 296 (1948).
[61] See *Bryant v. Securities Investment Co.*, 233 Miss. 740, 102 So.2d 701 (1958).
[62] Miss. Code Ann., §§ 8075–1—8075–24 (1956).

[63] Id., § 43–33–5 (1972).
[64] Id., § 43–33–7.
[65] Id., § 43–33–11.
[66] Id.
[67] Id., § 43–33–13.
[68] Id., § 43–33–15.
[69] Id., § 43–33–21.
[70] Id., § 43–33–37.
[71] Id., §§ 43–33–121, 43–33–123.
[72] Id., § 43–33–17.
[73] Id., §§ 43–33–101 et seq.
[74] Id., § 43–33–103.
[75] Id., § 43–33–117.
[76] Id., § 43–33–119.

thorities need not create projects near population centers.

Foreclosure of Tax Delinquent Housing

Mississippi has a relatively quick, simple method of foreclosing on tax delinquent dwellings. The tax payments are due on February 1, May 1, and August 1, in the year after assessment.[77] If taxes levied against real property are due and remain unpaid after February 15 and August 15, the realty is to be sold.[78] After adequate notice, the realty is to be sold by the collector on the first Monday of April and the third Monday of September.[79] After the taxes become delinquent, and before the sale, the taxpayer can redeem his property by paying the tax, interest, and cost accrued.[80] The sale is to the highest bidder for the taxes, fees, penalties, and damages provided by law.[81] The subsequent filing of the list of realty sold with the chancery court vests in the purchaser title to the property subject to the former owner's right of redemption.[82] After the sale, the former owner, or any person acting for him with his consent, or any person with an interest in the land, may redeem the property with a 2-year limit on the right of redemption.[83] Within 90 days, but not less than 60 days before the expiration of the right of redemption, the clerk of the chancery is required to notify the former owner and the lien holders on the realty.[84]

Maintaining Present Levels of Tax Assessment

There is no legal authority authorizing tax officials in Mississippi to maintain existing levels of assessment following improvement of substandard housing.

Fire Insurance

Mississippi does not have State legislation requiring insurance companies doing business in the State to write fire insurance in substandard areas.

[77] Id., § 27–41–1.
[78] Id., § 27–41–5.
[79] Id., § 27–41–55.
[80] Id., § 27–41–17.
[81] Id., § 27–41–59.
[82] Id., §§ 27–41–79; 27–41–81.
[83] Id., § 27–45–3.
[84] Id., §§ 27–43–1, 27–43–5.

Welfare Lien

There currently exists no welfare lien in the State of Mississippi.

Tennessee Report on Legislation

Planning and Zoning Authority in Tennessee Is Decentralized and Dispersed

Because there are several tiers in the structure of Tennessee law relating to planning and zoning, this section is divided into several categories, based on the level of government involved.

State Role: The State's role in this area relates primarily to the State planning office's power to create planning regions and to define their boundaries.[1] Basically, it is the function and duty of a regional planning commission to make and adopt a general regional plan for the physical development of the territory of the region.[2] It is important to note that all reports and plans of the planning office and/or of any regional planning commission are merely advisory and do not mandate compliance.[3] (The chief legislative body of a municipality may, however, choose to designate the regional planning commission as the municipality's planning commission.) [4] In one respect, regional planning commission regulations must be complied with; in terms of platting authority, no plat of a subdivision of land within such a region, other than land located within the boundaries of a municipal corporation, can be filed for record or recorded until it has been approved by the commission.[5]

The State planning office is authorized to create planning regions for unincorporated communities and to establish regional planning commissions for them, provided that such a region does not exceed 10 square miles nor contain less than 500 inhabitants.[6] Such a commission has more power than a regular regional planning commission because it also has the powers of a municipal planning commission,[7] discussed under subpoint C, following.

Counties: (The quarterly county court is the legislative and governing body of the county [8] and consists of the justices of the peace of the

[1] Tenn. Code Ann. § 13–107 (1955). (Hereinafter cited as T.C.A.)
[2] Id., § 13–108.
[3] Id.
[4] Id., § 13–204.
[5] Id., § 13–302.
[6] Id., § 13–210.
[7] Id., § 13–211 and 13–212.
[8] Id., § 5–528 (1971).

county.)[9] The quarterly county court of any county is empowered to regulate, in the portions of the county that lie outside of municipal corporations, such typical zoning matters as building height and size, percentage of a lot which may be occupied, and land uses.[10] The county units have no planning function per se.

A significant exemption from county zoning regulations is buildings on, and uses of, agricultural lands, with certain limited exceptions.[11]

As to amendments of zoning regulations, they must be submitted for approval or for suggestions to the appropriate planning commission, but if disapproved by that body may still be made operative by a majority vote of the entire membership of the county court.[12]

Municipal Level: Planning and zoning functions are both granted to municipalities. With respect to planning, the chief legislative body (regardless of the term used to designate it) is authorized to establish a municipal planning commission.[13] Such a commission is charged with the function of making an official general plan for the physical development of the municipality, including any area outside of its boundaries which in the commission's judgment bears relation to the planning of the municipality.[14] Once the commission has adopted a plan, no street or other public way, public building, or public utility may be constructed in the municipality without approval by the planning commission; however, a majority vote of the chief legislative body (or of the body authorities or financing the project) may override the commission's disapproval.[15]

With regard to platting authority, there is a provision similar to the regional planning commission's power.[16]

Zoning authority is granted to the chief legislative body of the municipality,[17] with a planning commission's zoning plan apparently being a necessary prerequisite to action by the legislative body: "[w]henever the planning commission of the municipality makes and certifies. . . a zoning plan, . . . then the chief legislative body may exercise the powers granted . . . in §13–701. . . ." [18] The planning commission must approve changes in the municipal zoning plan, unless a majority of the legislative body overrides its disapproval.[19]

§13–711 grants power to the chief legislative body of any municipality to establish by ordinance zones or districts in territory adjoining but outside such municipalities, and lying within the planning region in which the municipal planning commission has been designated as the regional planning commission by the State planning commission under §13–202 (which requires that no part of the territory may be over 5 miles beyond the limits of the municipality) and in which territory the county has no zoning already in force. Generally, this outside land is treated as though it were part of the municipality for zoning purposes; [20] thus, extraterritorial zoning is explicitly authorized. Municipal zoning power over such territory is automatically superseded and repealed when the county adopts county zoning covering that area.[21] These provisions would have an impact on rural housing when such housing is located within 5 miles of a municipality's borders. Presumably, agricultural lands, by analogy,[22] would be excluded in any case.

General: Several points should be mentioned which transcend the specific categories above.

Preexisting private acts are not affected by the above provisions.[23]

Whenever regulations made under authority of Chapter 4 (county zoning regulations) and Chapter 7 (municipal zoning regulations) conflict with any statute, the higher standard (e.g., lower building size or greater percentage of unoccupied land) governs.[24]

Historical structures and zones are authorized by §§13–416 and 13–716, which have identical language. Such structures and zones may be established by the chief legislative body of the municipality or county, which shall then create a historic zoning commission. The commission is given exclusive jurisdiction relating to historical matters.[25]

Finally, as a general point with respect to application of zoning laws, the Tennessee Supreme Court has repeatedly taken the position that they should be construed strictly in favor of

[9] Id., § 5–501.
[10] Id., § 13–401 (1955).
[11] Id., § 13–414.
[12] Id., § 13–405.
[13] Id., § 13-501.
[14] Id., § 13–503
[15] Id., § 13-507.
[16] Id., § 13–602.
[17] Id., §§ 13-701 & 13–702.
[18] Id., § 13–702
[19] Id., §§ 13–703 & 13–704.
[20] Id., § 13–714.
[21] Id., § 13–715.
[22] See T.C.A., § 13–414.
[23] Id., §§ 13-309, 13–415, 13–609 (under this section, the private acts are supplemented by the statutory provisions), and 13–710 (but the provisions of the chapter not inconsistent with the provisions of the special or private act also apply).
[24] Id., §§ 13–412, 13–709.
[25] Id., §§ 13–416(d), 13–716(d).

the common law property right of unlimited user. For example, see *State ex rel Wright* v. *City of Oak Hill,* in which the court indicated that: [26]

> Zoning laws are in derogation of the common law, and operate to deprive an owner of a use of land which might otherwise be lawful. So, in application, such laws should be strictly construed in favor of the property owner.

Regulations Governing the Use of Mobile Homes Are Generally Implicit Rather Than Explicit

Motor Vehicle Registration and Licensing: § 59–103 declares that " 'motor vehicle' shall also mean any mobile home or house trailer as . . . defined in § 59–105 . . . ," which in turn defines "mobile home or house trailer" as meaning any vehicle or conveyance not self-propelled, designed for travel upon the public highways, and designed for use, inter alia, as a residence or apartment.

Mobile homes or house trailers are subject to the registration and certification of title (license) provisions when they are occupied.[27] There are several exceptions to this requirement,[28] relating to all motor vehicles, and the one of greatest possible significance for housing purposes is that of vehicles owned by the Government of the United States. If future Department of Housing and Urban Development (HUD) programs were to supply rental mobile housing directly, such mobile home units would not have to follow the ordinary registration process.

As for the registration fee, mobile houses or house trailers are designated Class (F) and are subject to a fee ranging from $18 to $50, depending upon the width and length of the vehicle.[29] For purposes of the registration fee, mobile home or house trailer includes a trailer or semitrailer which is designed and equipped as a dwelling or sleeping place, either temporarily or permanently, and is equipped for use as a conveyance on streets and highways.[30] The Tennessee Supreme Court has held that nothing in this section prohibits a county from levying and collecting a privilege tax on motor vehicles. *Adkins* v. *Robertson County*.[31] See § 5–802.

Mobile homes of over 35 feet in length must obtain a permit to be moved upon the public roads or highways, with a fee of $3 or $5 (if over 50 feet) being charged.[32] Manufacturers and dealers of mobile homes or houses trailers licensed to do business in Tennessee are exempt from these requirements.[33]

Operation of Vehicles—Rules of the Road: Historically, Tennessee's rules of the road were patterned in almost verbatim conformity with the Uniform Vehicle Code, but since 1955 have received little amendment to conform to the Uniform Vehicle Code changes that have been made.[34]

With regard to speed limits, the applicable provision [35] does not mention trailers or mobile homes. While the general definition of "truck" is a motor vehicle designed, used, or maintained primarily for the transportation of property,[36] subsection (c) of § 59–852 defines truck as any motor vehicle of 1½ or more tons rated capacity. If this does include mobile homes with the requisite capacity, they must conform to the reduced speed limits for trucks.

In any event, determining the speed laws for mobile homes is not such a simple matter as looking at the limits in § 59–582, for § 59–583 empowers the bureau of highways to lower the speed limits wherever and whenever the bureau determines that it is in the interests of public safety to require a reduction. Furthermore, the legislative authority of a town or city has the power to prescribe such lower speed limits within certain areas or zones of its jurisdiction.[37] Municipalities may also make additional regulations for the operation of a vehicle, so long as such regulations do not conflict with the provisions of sections in the code.[38] For example, in *Baumgartner* v. *Town of South Pittsburgh,*[39] the Tennessee Supreme Court held a town parking meter ordinance valid. Thus, local regulations are of considerable importance in this area.

The State does not operate a periodic motor vehicle inspection system itself, but as of 1972 five cities had such a program.[40]

Size, Weight, and Load: Every vehicle must conform to the size, weight, and load requirements that are prescribed by the department of highways and the department of safety.[41]

No motor vehicle, as defined in § 59–103, whose length (including any part of body or

[26] 321 S.W.2d 557, 559 (Tenn. 1959).
[27] T.C.A., § 59–301 (1968).
[28] Id.
[29] Id., § 59–421.
[30] Id.
[31] 201 Tenn. 596, 301 S.W.2d 337 (1957).
[32] T.C.A., § 59–454 et seq.
[33] Id., § 59–461.
[34] *Study of the State's Motor Vehicle Laws 1972,* Final Report of the Legislative Council Committee, FR–1972–BZ, at 64.
[35] T.C.A., § 59–852.
[36] Id., § 59–801.
[37] Id.
[38] Id., § 59–1028.
[39] 195 Tenn 53, 256 S.W.2d 705 (1953).
[40] Motor Vehicle Laws Study, supra n. 34, at 49.
[41] T.C.A., § 59–1101.

load) exceeds 40 feet, and no motor vehicle with trailer or semitrailer attached, the total length of which combination (including any part of body or load) exceeds 55 feet, may be operated on any highway.[42] With respect to maximum width and height, no motor vehicle as defined in §59–103, or any trailer or semitrailer, whose width (including any part of body or load) exceeds 8 feet or whose height (including any part of body or load) exceeds 13½ feet, may be operated on any highways, with certain exceptions not here relevant.[43] Special permits for movement of equipment exceeding 8 feet in width may be issued by the Commissioner of Highways. See State of Tennessee Department of Highways Temporary Revision Notice Concerning Rules and Regulations for overweight and overdimensional movements on Tennessee highways, effective Oct. 1, 1971.

Except when a special permit is issued by the commissioner of highways,[44] no vehicle can be operated over the public highways when the gross weight exceeds 73,280 pounds.[45]

A Note on Zoning Laws: *State* v. *City of Nashville*[46] indicated that although a zoning ordinance fails to mention house trailers by name, when their use would violate the letter and the spirit of the zoning ordinance, they may be prohibited.

Usury Laws

"Interest" and 'Usury": Interest is defined in the Tennessee code as "the compensation which may be demanded by the lender from the borrower, or the creditor from the debtor, for the use of money."[47] According to §47–14–104, the legal rate of such interest is 6 percent per annum, but contracts may be made in writing for the payment of a rate of interest not greater than 10 percent per annum payable on the unpaid principal: "[e]very excess over these rates is usury, except as otherwise provided." This maximum is in accord with Article 11, Section 7, of the Tennessee Constitution, which grants the legislature the power to fix the rate of interest, but with the limitation that such rate is "not to exceed ten per centum per annum."

Moreover, no discount may be charged on any loan contracted under the above provision, resulting in an effective rate of interest of greater than 10 percent per annum over the stated term of the loan.[48] No distinction is made whether the seller or the buyer first pays the points.

There are no special provisions for FHA, VA, or other governmental housing loans in the code. As to compound amortization, there are no statutes or cases prohibiting it (provided that the effective rate of interest does not exceed 10 percent per year over the stated term of the loan).

Exceptions: Under the terms of §47–14–104, the 10 percent contract rate does not apply to loans or credit extended under the "Industrial Loan and Thrift Companies' Act,"[49] in which event the maximum rate at which interest can be deducted is 7.5 percent per annum; nor does it apply to installment loans of banks and trust companies and building and loan associations on which interest is deducted in advance or added to the principal, as provided in §§45–433 and 45–1412, in which cases interest computed on the principal amount of the loan for the entire term is not to exceed 6 percent per annum.

Rates Above the Statutory Maximum not Constituting Usury: *Silver Homes, Inc.* v. *Marx & Bensdorf, Inc.*[50] reiterated the Tennessee rule that the consideration which the lender may legally demand is not determined by what the borrower pays, but by what the lender receives. Thus, in that case, the Tennessee court held that an FHA mortgage loan bearing 5.75 percent interest per annum and requiring additional premiums making the total rate go above 6 percent (the then statutory maximum) was not a violation of the usury laws, since the additional payments were not for the benefit of the mortgagee but were required to be turned over by him to the Federal Housing Administration.

With regard to whether a "late charge" in excess of the legal rate of interest constitutes usury depends on whether the charge is made as consideration for extension of time for payment or as compensation for the damage done to the creditor by the debtor's failure to pay the debt when due; the former constitutes usury, but not the latter. *Wilson* v. *Dealy*.[51] In *Wilson*, the Tennessee court upheld a late payment penalty fee that was reasonably related to the lender's actual damages suffered because of the borrower's tardiness. This rationale would seem to be applicable to penalties for other than tardiness.

[42] Id., § 59–1107.
[43] Id., § 59–1108.
[44] See § 59–1111.
[45] Id., § 59–1109.
[46] 207 Tenn. 672, 680, 343 S.W.2d 847, 850 (1961).
[47] T.C.A., § 47–14–103 (1972 Supp.).

[48] Id.
[49] Id., § 45–2007 (f).
[50] 206 Tenn. 361, 333 S.W.2d 810 (1960).
[51] 222 Tenn. 196, 434 S.W.2d 835 (1968).

It is well settled in Tennessee that when credit is advanced by the seller to the buyer, the parties may contract for a higher rate of interest without its constituting usury—the stipulation for the greater rather than the usual rate of interest being consideration for a deferral of payment. See *First Nat. Bank* v. *Mann.*[52]

Compound interest contracted for or agreed upon when the debt is created, or subsequently in the extension of the same, is not usury and, therefore, is not illegal. *Woods* v. *Rankin.*[53]

For other aspect of the question of what is usurious, as expressed in State case law, see 84 T.C.A. 666–675.

Relief Against Usury: A defendant sued for money may avoid the excess over legal interest, by a plea setting forth the amount of the usury;[54] while if usurious interest has been paid, the same may be recovered by the party from whom it was taken.[55]

The remedy given at law against usury does not prevent the party from having relief in equity.[56] But where a court of law first obtains jurisdiction, its judgment will be conclusive, and chancery will not entertain a bill to disturb it, except in special cases. See *Parker* v. *Bethel Hotel Co.*[57]

A usury claim after 2 years from the date of the payment of the debt upon which such claim for usury is based is barred.[58] In the case of continuous usurious transactions, the statutes of limitation do not commence to run until the principal, with the legal interest thereon, is paid. *Star Sav. & Loan Ass'n* v. *Woods.*[59]

The "Tennessee General Act" and the Establishment of Housing Corporations

Acts 1968, ch. 535, §1 (17.02) repealed the then existing corporate laws and replaced them with the "Tennessee General Corporation Act." While this act contains no specific provisions regarding the establishment of housing corporations, they are clearly permissible under §48–401, which states that "[a] corporation may be organized under this act for any lawful purpose. . . ."

As to whether such a corporation can be regarded as nonprofit in nature, it should be noted that §48–102(i) defines a "corporation not for profit" as meaning a domestic corporation, no part of the income or profits of which is distributable to its members, directors, or officers, except as provided in the title. If it does not fit that definition, the corporation is considered as one for profit.[60] This "economic approach" to determining nonprofit status makes the economic relationship between the corporation and its members the crucial point.[61]

Detailed Laws Affecting the Operation of Savings and Loan Associations in the Home Mortgage Field

Banks: All banks are endowed with the powers and rights conferred upon banking corporations for profit by the Tennessee General Corporation Act, mentioned in the preceding section, subject to regulation by the superintendent of banking.[62] In other words, they are treated basically as regular corporations and are specifically given the power to secure any of their obligations by mortgages, or to receive, sell, and otherwise deal in and with them.[63] Furthermore, a corporation has the power to guarantee obligations of any other entity and to secure such guarantees by mortgage, pledge, or otherwise.[64] No specific statutory regulations exist as to banks in general, and mortgages, apart from those applicable to corporations.

Building and Loan Associations: (Building and loan associations are now commonly referred to as savings and loan associations.)[65] In contrast to banks in general, there are detailed requirements for building and loan associations. §45–1301 defines a building and loan association in a somewhat circuitous manner: Any association or corporation which is chartered under any building and loan law to carry on the business of a building and loan association. The following material, dealing with Title 45, Chapter 14—Loans and Investments by Building and Loan Associations—merely hits the highlights of the provisions contained therein. See Title 45, Chapter 14 for a more comprehensive description.

Savings and loan associations licensed to do business in Tennessee are required to main-

[52] 94 Tenn. 17, 27 S.W. 1015, 27 L.R.A. 565 (1894).
[53] 49 Tenn. 46 (1870).
[54] T.C.A. § 47–14–112 (1955)
[55] Id., § 47–14–117.
[56] Id., § 47–14–116.
[57] 96 Tenn. 252, 34 S.W. 209 (1896).
[58] T.C.A., § 47–14–118 (1955).
[59] 100 Tenn. 121, 42 S.W. 872 (1897).

[60] T.C.A., § 48–102(h) (1972 Supp.).
[61] Comment, *Nonprofit Corporations,* 35 *Tenn. L. Rev.* 340, 342 (1969).
[62] T.C.A., § 45–501 (1972 Supp.).
[63] Id., § 48–402(g) and (h).
[64] Id., § 48–403.
[65] *Study on the State's Building and Loan Association Laws 1968,* Final Report of the Legislative Council Committee, FR-1968-B7, at 8.

tain a department to service the loans and property securing such loans, including investigation of applicants and enforcement of contractual and governmental obligations. Such associations are authorized to collect a service fee not exceeding 2.5 percent per annum of the unpaid balance to defray the expense of providing such a service department; the fee may be made payable in periodic installments running throughout the life of the loan.[66]

Building and loan associations or building associations may lend their funds to their stockholders or members according to terms prescribed by the corporation's constitution and bylaws, with the limitation that all such loans be secured by first liens upon real estate, the loan in no case to exceed in amount ⅔ the value of the real estate as determined by the board of directors.[67] This limitation does not apply to mortgage loans issued by the FHA.

Multiple loans upon the same property may be made by a building and loan association, provided that the total of the first and additional loans does not exceed ⅔ of the appraised value of the real estate and that such association hold no junior mortgage without holding the senior mortgage or mortgages.[68] Any real estate mortgaged or conveyed in trust to secure a debt to the association may be purchased by it at a judicial, execution, or trustee sale.[69]

§45–1412 deals with home improvement installment loans or loans for the purchase of mobile homes which Federal savings and loan associations have the power to make, and lays down special provisions as to interest and necessary expenses. The following section in the code authorizes a Federal savings and loan association, in making an installment loan of over $300 to require the borrower to issue insurance on tangible personal property or on the life of the borrower.

A special privilege tax is assessed on building and loan associations by §45–1501, the nature of which tax is spelled out in §45–1502; basically, it is 7 percent on the net income, with the proviso that the amount of the tax be not less than 1.5 percent of the association's gross income for the previous fiscal year. Definitions of "net income" and "gross income" are contained in this section.

The privilege tax is exclusive, and all other taxes except the ad valorem taxes upon real estate and tangible property owned by an association are not applicable.[70]

Health Laws and Regulations Contain Most of the Nonzoning Restrictions and Requirements for Building Construction

Building Regulations: Chapter 25 of Title 53 (Health and Safety) is concerned with building regulations, and for this reason the latter are included here. As to the application of these regulations:

> This chapter is declared to be remedial, and shall be liberally construed to secure the beneficial interests and purposes hereof which are public safety, health and welfare, through structural strength and stability, means of egress and safety to life and property from fire and hazards incident to the design, construction, alteration and repair of buildings or structures.[71]

No building or structure may be constructed, altered, or repaired except in conformity with the provisions of the chapter, and it is unlawful to maintain, occupy, or use a building or structure or part thereof that has been erected or altered in violation of them.[72] Furthermore, it is unlawful to alter a structure in such a way as to violate regulations of the fire marshal issued under the chapter. The provisions apply with equal force to municipal, county, or State buildings as they do to private buildings, except as specifically provided for by statute.

Exceptions are spelled out in §53–2502. For our purposes, the important exception is that nothing contained in the chapter applies to buildings, whether heretofore or hereafter constructed, which are "occupied exclusively as dwellings or having not more than two (2) apartments. . . ." This would appear to exclude one-family units and duplexes from the building regulations. According to *Wyatt* v. *State*,[73] "dwelling" refers to a place in which a person or family resides. While there is no case law or statutory explanation of the word "dwellings" in the expression "occupied exclusively as dwellings," it is only logical to assume that it refers to single-family dwellings. Otherwise, "or having not more than two (2) apartments" would be superfluous. Indeed, exempting all residential buildings from the building regulations would defeat the whole purpose of the act.

The following provisions of Chapter 25 refer to various aspects of the health and safety build-

[66] T.C.A., § 45–1401 (1964).
[67] Id., § 45–1402.
[68] Id., § 45–1409.
[69] Id., § 45–1410.
[70] Id., § 45–1504.
[71] Id., § 53–2543 (1966).
[72] Id., § 53–2501.
[73] 467 S.W.2d 811, 814 (Tenn. 1971).

ing regulations:

- §§53–2503—53–2506: exit requirement.
- §53–2507: interior stairways.
- §53–2510: exterior stairways.
- §53–2511—53–2515: fire escapes.
- §53–2512: passageways.
- §53–2513: width of hallways.
- §53–2514: doorways.
- §§53–2516 & 53–2517: changes in occupational uses.
- §§53–2518—53–2542: fireproofing and other fire prevention requirements.

With regard to the important area of fire protection, the regulations and standards promulgated by the State fire marshal to effectuate the chapter have the same force and effect as provisions of the chapter.[74] In promulgating these rules, the fire marshal is instructed to base them upon the standards of Federal or State bureaus, national technical organizations or fire underwriters, including the National Fire Codes.[75] For the purpose of approving new materials and techniques, the Southern Standard Building Code is also to be relied upon.[76]

Enforcement of Chapter 25 regulations is spelled out in §53–2539, which basically grants concurrent jurisdiction to the State fire marshal and his staff and to local officials. No regulation can be issued or enforced by any official which is in conflict with the provisions of the chapter, but stricter local laws are, by implication, valid; the section states that provisions of the chapter supersede all less stringent provisions of municipal ordinances.

Two recent additions to the chapter are the "Tennessee Public Buildings Accessibility Act" of 1970 [77] and §§53–2549—53–2554 (1971) dealing with safety glazing materials. The former provisions refer to the physically handicapped and affect any building and grounds appurtenant thereto, the cost of construction or operation of which is paid (entirely or partially) by the State, any government or political subdivision thereof, any agency of the State, or any agency of any governmental or political subdivision of the State, which is used generally by the public.

Basically, under §§53–2549—53–2554, safety glazing material must be used on glass doors or glass panels to minimize the likelihood of injury resulting from contact with such doors or panels. §53–2554 provides that whenever the glazing provisions in the act conflict with any local, municipal, or county ordinance or resolution, or parts thereof, the more stringent provision shall apply.

Elevators, Dumbwaiters, and Escalators: These are dealt with in Chapter 26 of Title 53. An elevator safety board [78] has the duty to license inspections and to issue regulations, consulting with engineering authorities and organizations studying and developing safety codes (including the American Standards Association) for elevators, dumbwaiters, and escalators.

The chapter provides for registration, periodic inspection, and operating permits (for which a token fee is charged). No State permit is issued for elevators located in municipalities where elevator inspection ordinances are in force under §53–2611, it being the responsibility of such municipalities to make the inspections and collect permit fees.[79] There is a $25 fee for elevator construction permits.[80]

Municipal laws, ordinances, or regulations in substantial conformity with the commonly accepted standards of health and safety concerning elevators, dumbwaiters, or escalators, and in substantial conformity with the published standards of the American Standard Safety Code for Elevators, Dumbwaiters, and Escalators, are not replaced by provisions of the chapter.[81] Such local laws may be exclusively regulated or enforced by the officials or boards of the respective municipality. In addition, for the erection of elevators, dumbwaiters, or escalators, one must first obtain a building permit from the proper municipal authority, in compliance with local laws and ordinances.

Boiler Inspection, Erection, and Repair: §§53–2701 and 53–2702 of Chapter 27 set up a board of boiler rules to formulate definitions, rules, and regulations based upon the generally accepted nationwide engineering standards and practices. The board may by resolution adopt an existing published codification thereof, known as the Boiler Construction Code of the American Society of Mechanical Engineers.

Complete exemptions include boilers under Federal control, while boilers exempt from the inspection requirements of the act include boilers located on farms and used solely for agricultural purposes, and boilers of below a certain pressure located in private residences or in apartment houses of less than six families.[82]

[74] T.C.A., § 53–2536(a) and (d) (1966).
[75] Id., § 53–2536(a).
[76] Id., § 53–2536(b).
[77] Id., §§ 53–2544—53–2548 (1972 Supp.).
[78] Id., §§ 53–2602 & 53–2603 (1966).
[79] Id., § 53–2608(b) & (c).
[80] Id., § 53–2608(b) & (c).
[81] Id., § 53–2611.
[82] Id., § 53–2705.

Municipal laws or ordinances which are in substantial conformity with the commonly accepted standards of safety and in substantial conformity with the commonly accepted standards of the Boiler Construction Code of the American Society of Mechanical Engineers are not superseded, and such local laws may be exclusively regulated or enforced by the local officials or boards.[83] Again, erection of a boiler requires a building permit from the proper municipal authority in compliance with local law.

An inspection certificate is necessary,[84] the inspection fee being based on the maximum length of the vessel, multiplied by the maximum width of the diameter.[85]

§§53–2717 to 53–2724 deal with license requirements of engaging in the erection or repair of boilers. Local laws are not affected, and there is exclusive local control over local licensing requirements.[86] Thus, there is dual licensing of boilers in the State.

Trailer Court Regulations: Tennessee is considered a State having detailed regulations with respect to mobile home parks.[87] (It should be noted that the terms "trailer" and "mobile home" are interchangeable, the latter having replaced the former.) [88]

Under the definitions section, "trailer court" means any plot of ground within the State upon which two or more trailer coaches are occupied for dwelling or sleeping purposes, while "trailer coach" refers to any vehicle used or so constructed as to permit its being used as a conveyance upon the public streets or highways, and constructed in such manner that will permit occupancy thereof as a dwelling or sleeping place for one or more persons.[89] These broad definitions would appear to cover a park of mobile homes, each of which is a self-contained unit (i.e., having its own water and sewage facilities).

General supervision over the planning, location, and method of operation of trailer courts, and the adoption of rules and regulations pertaining thereto, is vested in the commissioner of public health.[90]

§53–3203 provides for a permit requirement for a trailer court, while §53–3204 gives inspection duties to the commissioner or to local health officers.

[83] Id.
[84] Id., § 53–2711.
[85] Id., § 57–2713.
[86] Id., § 57–2722.
[87] Bartke & Gage, *Mobile Homes: Zoning and Taxation*, 55 Corn. *L.Q.*, 491, 513 n. 103 (1970).
[88] Id., at 493.
[89] T.C.A., § 53–3201 (1966).
[90] Id., § 53–3202.

Various health and safety requirements (such as water supply and sewage disposal) are found in §§53–3205 to 53–3217. It is the duty of local health officers or the commissioner—when the commissioner determines that the provisions of the chapter are not being adequately enforced —to enforce such provisions. All ordinances, rules, and regulations adopted by boards of health or local governing bodies must at least conform to the reasonable requirements that may be established by the department, and cannot be inconsistent with the department's rules and regulations.[91] This language is a bit confusing. First, "reasonable requirements" is not used elsewhere in the health and safety laws, and its meaning is not clear. Second, it is unclear from the statutory language whether stricter local requirements are valid, in that they "at least conform," or improper because they are "inconsistent." They would appear to be invalid, based on §53–3220, which explicitly provides that where provisions of the chapter conflict with provisions of any private or public act or local ordinance or code existing as of March 21, 1957, the provision which establishes the higher standard shall prevail.

Requirements for Installation of Water and Waste Systems May Have an Effect on Lot Size

General Water and Sewage Requirements: §53–2004 provides that no person shall install, permit to be installed, or maintain any cross-connection, auxiliary intake, bypass, or interconnection, unless the source and quality of water from the auxiliary supply, the method of connection, and the use and operation of such cross-connection, auxiliary intake, bypass, or interconnection has been approved by the State department of public health. The arrangement of sewer, soil, or other drain lines or conduits carrying sewage or other wastes in such a manner that the sewage or other waste may find its way into any part of the public water supply, is prohibited.

The department of public health exercises general supervision over the construction of public water supplies and public sewer systems, and their operation and maintenance,[92] and the department may enforce any standards, policies, orders, rules, or regulations issued by it, to control public water supplies and public sewer sys-

[91] Id., § 53–3218.
[92] Id., § 53–2003.

tems; such suits as may be necessary to carry out the provisions of the chapter effectively may be instituted by it in any court of competent jurisdiction.[93]

County and municipal health boards or administrative agencies may require that buildings be connected with the public sewerage facilities.[94]

Sewerage Disposal Systems of Subdivisions: For purposes of §§53–2009 to 53–2016, "subdivision" is defined as any tract or parcel of land divided or proposed for division into five or more lots, sites, or other divisions, for the purpose of immediate or future building of houses or other developments, requiring that a maximum lot size in any subdivision be 40,000 square feet or less, to a minimum of 15,000 square feet. This "requiring a maximum. . ." provision is unclear in meaning.[95]

The State department of public health is authorized to exercise general supervision over the planning, construction, and operation of individual sewage disposal systems for proposed subdivisions, where public sewerage systems are not available, except within the corporate limits of municipalities, and to establish standards for individual sewage disposal systems.[96]

The owner of a proposed subdivision is required to submit detailed information—including a map of the surrounding area and of the area to be subdivided—showing (inter alia) proposed lot sizes and location of supply lines.[97] He must also furnish such additional data as required by the local health officers as a basis for determining the suitability of individual lots.[98]

Lot size requirements dependent upon the availability of public water supplies are dealt with in §53–2012. When such supplies are available, the minimum lot size is 7,500 square feet; when not available, 15,000 square feet. Minimum distances from a water well or other source may be specified, additional lot size may be required as indicated by percolation tests, or the particular lot or lots may be disapproved when it is determined that the soil will not absorb the sewage. This section does not apply within the corporate limits of municipalities.

Local health officers are given the duty to enforce the terms of §§53–2009—53–2016 when the commissioner of public health determines that they are not being complied with.[99] All rules and regulations adopted by county boards of health or other governing bodies, except municipal governing bodies, must conform to the minimum requirements established by the department (this suggests that stricter standards are permissible). The health officer makes investigations and recommendations and reviews plans as necessary to enforce the terms of §§53–2009—53–2016.

It should be noted that the sections are not applicable to counties or municipalities wherein a comparable system of supervision over the planning, construction, and operation of a sewerage disposal system had theretofore been enacted by any private act or effective local ordinance.[100]

The commissioner or local health officer may institute a civil action in chancery court for injunctive relief to prevent violation of these sections. Furthermore, no proposed subdivision, except those within the corporate limits of a municipality, can be approved by the local planning commission unless the plan for sewerage disposal has been approved by the local health officer.[101]

In sum, subdivision regulation with regard to water and sewerage facilities is quite involved, both in terms of administration and substantive requirements.

Environmental Laws May Affect the Construction and Operation of Housing Units

Air Pollution: The key legislation here is the Tennessee Air Quality Act[102] administered by an air pollution control board.

Air pollution from apartment houses or private dwellings is clearly covered by the act: §53–3409(b) provides that "air contaminant source" is any and all sources of emission of air contaminants, whether private or publicly owned, including all types of commercial, residential, and industrial buildings.

§§53–3411 and 53–3412 establish the board mentioned above and spell out its powers and duties, principally to promulgate rules and regulations to effectuate the purpose of the act (no specific technical standards are spelled out in the various sections.) In addition, the board is authorized to issue an emergency stop order for air contaminant sources—any other provision of the law to the contrary notwithstanding—if the

[93] Id., § 53–2008.
[94] T.C.A., §§ 5–1608 & 6–1403 (1971).
[95] T.C.A., § 53–2009 (1966).
[96] Id., § 53–2010.
[97] Id., § 53–2011 (1)(a) (1972 Supp.).
[98] Id., § 53–2011(1)(c).
[99] Id., § 53–2013 (1966).
[100] Id.
[101] Id., § 53–2014.
[102] T.C.A., §§ 53–3408—53–3422 (1972 Supp.).

commissioner of public health finds that emission from the operation of one or more air contaminant sources is causing imminent danger to the public health and safety, and the Governor approves the order.[103] Furthermore, the board has a right to injunctive relief via any court of competent jurisdiction, to prevent violation of any duly promulgated rule or regulation.[104] But existing civil or criminal remedies for wrongful action are not impaired by the act,[105] nor are private rights affected.[106] Thus, while individual citizens have no right to bring an action for violation of the act, they do have channels of redress.

Any municipality or county may enact, by ordinance or resolution, air pollution control regulations consistent with the standards ordered for the State.[107] The municipality or county must first apply for and secure from the board an exemption (unless it had an exemption as of March 24, 1967, in which event the exemption continues until a determination is made that the State standards are not being complied with or not being enforced.)

Any city, town, or county having a population of 600,000 or more, according to the most recent census, is authorized to enact ordinances or regulations no less stringent than the provisions of §§53–3408 to 53–3422 [108] (ordinances or regulations enacting air pollution regulations must be exempted by the board.) [109] Therefore, cities or counties with the requisite population can have stricter requirements than the State.

For specific requirements promulgated under the act, see the Tennessee Air Pollution Control Regulations (adopted Jan. 25, 1972), contained in BNA Environmental Reporter 2 State Air Laws 47 (1972). Open burning regulations are found in Chapter 4 of the regulations.

Water Pollution: The Tennessee Water Quality Control Act of 1971 [110] is the applicable State legislation. Owners of apartment houses and other residential buildings are clearly covered by its provisions: §70–326 (10) defines "person" as meaning any and all persons, including individuals, firms, partnerships, associations, public or private institutions, municipalities or political subdivisions or officers thereof, departments, agencies, or instrumentalities, or public or private corporations. Obviously, this definition was meant to be practically all-inclusive.

A Water Quality Control Board was created by the act, and it has the duties of establishing and enforcing standards of quality for all the waters in the State.[111] The commissioner of the board may assess the liability of any polluter or violator for damages done to the State by the persons polluting or violating,[112] in addition to the criminal penalties under §70–337. Injunctive relief to stop or prevent pollution or violation is available to the commissioner, in any appropriate court.[113] The court may grant the injunction without the necessity of showing a lack of adequate remedy at law. The commissioner may also bring suit for injunctive enforcement of any order made by him, and all findings of fact contained in the order and complaint are deemed to be final.

Any person may file with the commissioner a standard complaint against any person allegedly violating the act (contrary to the Air Pollution Control Act, the difference in treatment not being a rational one), and nothing in the act is designed to abridge or alter equitable or common law rights of act,[114] such as nuisance.

All sections of the act are to be liberally construed for the accomplishment of the purpose of preventing water pollution.[115] For regulations promulgated under the act, see BNA Environmental Rptr. 2 State Water Laws 65 (1972).

Other Environmental Matters: Noise pollution might be a problem in certain instances, and thus merits some discussion. At the present time, there are few laws in Tennessee that deal with noise pollution or dangerous noise.[116] As far as community noise is concerned, the only existing applicable State laws are embraced in the law of nuisance.[117] There are local antinoise ordinances and zoning laws in several municipalities, however, including Memphis.[118]

Tennessee Has No Welfare Lien Law

There is no welfare lien provision in the State laws. Prior to its repeal in 1953, there was a rather narrowly drawn provision [119] that on the death of any recipient of old-age assistance,

[103] Id., § 53–3416.
[104] Id., § 53–3418.
[105] Id., § 53–3420.
[106] Id., § 53–3421.
[107] Id., § 53–3422.
[108] Id., § 53–3423.
[109] Id.
[110] Id., §§ 70–324—70–342.

[111] Id., §§ 70–327 & 70–328.
[112] Id., § 70–338.
[113] Id., § 70–339.
[114] Id., § 70–340.
[115] Id., § 70–342(b).
[116] *Study on Noise & Air Pollution Laws and Refuse Dumping 1970,* Final Report of the Legislative Council Committee, FR-1970–B9, 72.
[117] Id., at 73.
[118] Id.
[119] Public Acts 1937, Ch. 49, § 12.

a lien was created in favor of the State for the amount of such assistance, after funeral expenses not exceeding $100, and limited to cases where there was fraud by the recipient and where the heirs were morally responsible for the care of the recipient and able but unwilling to provide it.

Somewhat analogously, however, with request to eligibility for old-age assistance,[120] aid to the disabled,[121] and aid to the blind,[122] one of the conditions is that within the 5 years immediately preceding application or during receipt of assistance, the person has not, in order to evade any provision of the chapter, made an assignment or transfer of property, the proceeds from which, at the fair market value (irrespective of the actual consideration received), would under the State standards of need still be available to meet the needs of the individual. Any transfer of property to a husband, wife, son, daughter, son-in-law, daughter-in-law, nephew, or niece, within the period above mentioned, is considered prima facie evidence that the transfer was made with the intent to evade the provisions of the applicable chapter.

State Sales Tax and Mobile Homes

Sales Tax: The "Retailers' Sales Tax Act" [123] provides basically for a sales tax at a rate of 3 percent of the sales price of each item or article of tangible property.[124]

A use tax is imposed on imports; [125] all tangible personal property imported from other States and used by the "dealer" [126] is subject to the tax imposed by the chapter.

Agricultural products are exempted,[127] as are all sales made the State of Tennessee or to any county or municipality within the State.[128]

Taxation of Mobile and Modular Units: With regard to the taxing of mobile homes, the statutes do not give a definitive answer. §67–612 mentions, as a class of personal property, farming implements, wheeled vehicles, automobiles, etc. Enumerating motor vehicles separately from automobiles lends itself to the conclusion that mobile homes with wheels are considered personal property; it is hard to determine, however, what the taxing situation is meant to be if the wheels are removed or indeed never installed in the first place.

§67–507 does provide that the property of housing authorities be exempt from all taxes and special assessments of the State or any city, town, or political subdivision thereof; while the more general exemption from taxes for government property is §67–502: All property of the United States, the State, or any county or incorporated city, town, or taxing district, that is used exclusively for public or municipal purposes, is exempt. Neither the State nor any of its arms or agencies is liable to taxation, unless expressly so declared by statute, for they are impliedly excluded from the general tax laws. *Henson* v. *Monday.*[129] It appears, therefore, that if a mobile home park and the trailers therein are owned by a governmental unit, they will not be taxed.

No Building Codes Per Se in the Tennessee Code

In only a few places of the health and safety building regulations chapter are materials to be used in construction specified beyond the generic category. For example, interior stairways are to be made of "noncombustible materials throughout" except in buildings of frame construction and in buildings less than 30 feet high and occupied by less than 40 persons,[130] and spiral, slide, or tubular fire escapes must be made of "noncorrodible" sheet metal.[131]

A few sections are more precise. Fire walls are to be constructed of solid brick masonry laid in Portland cement mortar or cement lime mortar or of reinforced concrete,[132] fire retardant ceilings must be constructed of specific types of material,[133] and stand-pipes must be constructed of wrought iron or steel.[134]

Safety glazing materials must comply with the requirements of the ANSI Standard Z–97.1–1966, as well as with further department of public health regulations.[135]

In short, specifications of materials in the building regulations are not extensive and are confined to narrow categories. (The fire marshal may issue regulations supplementing the provisions of the chapter, however. See §53–2536.)

[120] T.C.A., § 14–203(e) (1955).
[121] Id., § 14–403(e).
[122] Id., § 14–504(d).
[123] Id., §§ 67–3001—67–3056 (1972 Supp.).
[124] Id., § 67–3003.
[125] Id., § 67–3005.
[126] Defined in § 67–3017.
[127] Id., § 67–3011.
[128] Id., § 67–3012.

[129] 143 Tenn. 418, 224 S.W. 1043 (1920).
[130] T.C.A., § 53–2507(1)(a) (1966).
[131] Id., § 53–3507(11).
[132] Id., § 53–2523(a).
[133] Id., § 53–2525.
[134] Id., § 53–2530(4)(a).
[135] Id., 53–2550 (1972 Supp.).

Minimum Housing Code

(See Health and Safety Laws, §7 supra; T.C.A. §53–2611 re municipal laws and elevators; and §53–2722 dealing with municipal laws regarding boilers.)

The State has no minimum housing code, but municipalities may promulgate and enforce requirements that are more stringent than those of the State; thus, a locality can formulate such a building code.

With regard to minimum housing codes on the local level, §53–2539 provides that no appropriate local official can issue or enforce any regulation chapter, and that the provisions of the act supersede all less stringent provisions of municipal ordinances. It seems, therefore, that stricter local housing laws and/or housing codes are permissible.

There is no legislation permitting tenant suits for damages in cases of landlord's failures to meet the housing code.

The tenant has no right to withhold payment or rent if the landlord does not comply with the minimum housing code. Violations of the building regulations,[136] elevator requirements,[137] and boiler regulations [138] are misdemeanors. Nothing is said about the right to withhold rental payments, either in these sections or anywhere else in the code.

Local Agencies Explicitly Authorized to Make Repairs on Substandard Dwellings

It is provided in Title 12 of Chapter 13 (Slum Clearance) that the public officer may order an owner of a dwelling to repair, alter, or improve the dwelling, or to vacate and close it; [139] if the owner fails to comply, the public officer may cause the dwelling to be repaired, altered, or improved, to be vacated and closed, or to be removed or demolished; [140] the amount of the cost of such becomes a lien against the real property upon which the cost was incurred.[141]

There is a statutory provision authorizing the closing, vacating, and demolition of substandard housing. (See the preceding point.)

Housing Authority

It might be noted that as of 1972, the governing bodies of homerule municipalities are authorized to establish city courts to try violations of municipal ordinances.[142]

Little authority exists to allow for court appointment of a receiver to collect rents and make improvements. Chapter 12 of Title 13 on slum clearance [143] makes no reference to this kind of power and, aside from the lack of statutory endorsement of the power, several decisions of the Tennessee court make appointment of a receiver for such purposes appear doubtful, although it has never been directly prohibited.

In *Orman* v. *Bransford Realty Co.*,[144] the State high court indicated that the power to appoint a receiver should be exercised with caution and only in extreme cases, under extraordinary circumstances or circumstances requiring summary relief. The case can be distinguished from the other situation in that it involved a minority stockholder of a corporation seeking appointment of a receiver, but the court's broad statements urging caution appear applicable here as well.

Brashears v. *Hartsook*,[145] a much more recent case, refined *Orman* by holding that when a judgment creditor has an adequate remedy at law by way of garnishment, the remedy of bringing a bill in chancery court to compel transfer of the funds to a receiver is not available. By analogy, if there is a remedy at law, a receiver should not be appointed to collect rents and make improvements; as to making improvements, public officials are authorized to order their effectualization, and this probably bars appointment under *Hartsook*.

It should be noted that there may be some authority to appoint a receiver under the general equity power, but the extent of such power is uncertain.

Foreclosure on Tax Delinquent Dwellings

(The county trustee is the collector of all State, municipal, and county taxes which are levied on property.) [146] Accrued taxes on all real property, plus all damages and costs accruing thereon, are and remain a first lien upon such property.[147] Thus, there is a lien upon the land for taxes against it in favor of the State, county, or city, *Pope* v. *Knoxville Indus. Bank*,[148] and it overrides all mortgages, encumbrances, and

[136] Id., § 53–2540 (1966).
[137] Id., § 53–2615.
[138] Id., § 53–2723.
[139] Id., § 13–1203(c) (1955).
[140] Id., § 13–203 (d) & (e).
[141] Id., § 13–203(f).

[142] T.C.A., § 16–1201 (1972 Supp.) on home rule municipalities.
[143] Id., §§ 13–1201—13–1209 (1955).
[144] 168 Tenn. 70, 73 S.W.2d 713 (1934).
[145] 224 Tenn. 36, 450 S.W.2d 7 (1969).
[146] T.C.A., § 67–1104 (1955).
[147] Id., § 67–1801.
[148] 173 Tenn. 461, 121 S.W.2d 530 (1938).

other liens of whatever kind there may be upon the property. *Dunn* v. *Dunn*.[149]

Chapter 20 of Title 67[150] deals with enforcement of tax liens. Preliminary notice is required; as a preliminary step toward enforcing the lien for uncollected land taxes charged to him, the county trustee must have a notice inserted in one or more newspapers of the county once a week for two consecutive weeks in the month of January.[151] As a second step, after the publication of notice and between February 1 and March 1, the trustee is directed to appoint an attorney, who shall bring suit after February 1 and before March 1 in the circuit or chancery courts of the county for the collection of land taxes due to the State, county, or municipality.[152]

When the amount due is ascertained, the court will order a sale of the land for cash, subject to the equity of redemption. The proceeds from the sale are applied first to the payment of a 10 percent penalty allowed as compensation for prosecuting the suit, second to the cost, and the remainder is applied to the State, the county, or the municipality (in that order).[153]

All the provisions of the chapter are to be construed liberally in favor of the validity of all official acts pursuant thereto.[154]

In addition to the basic foreclosure provisions above, officers charged with the duty of collecting state revenues are authorized to issue a distress warrant;[155] and if the officer cannot find personal property to satisfy the warrant, he may levy the same upon any real estate in his county belonging to the taxpayer.[156]

Municipal corporations having power under their charters to collect their own taxes may provide for the collection of their delinquent real property taxes by ordinance.[157]

Tax Officials Appear Barred from Maintaining Existing Levels of Assessment

According to §67–605 (1967), all property is to be assessed and taxed "according to its value, which shall be ascertained from the evidences of its sound, intrinsic and immediate value, for purposes of sale between a willing seller and a willing buyer without undue consideration of speculative values."

[149] 99 Tenn. 598, 42 S.W. 259 (1897).
[150] T.C.A., §§ 67–2001—67–2046 (1972 Supp.)
[151] Id., § 67–2001 (1955).
[152] Id., §§ 67–2002—67–2003.
[153] Id., § 67–2012 (1972 Supp.).
[154] Id., § 67–2043 (1955).
[155] Id., § 67–2201.
[156] Id., § 67–2204.
[157] Id., § 67–1319.

Prior to 1967, the section used the term "actual cash value," reflecting the position of the leading case of *Carroll* v. *Alsup*,[158] that the actual cash value is the only practicable basis upon which taxes can be made equally uniform and is clearly the constitutional requirement (see Article 2, §28 of the Tennessee constitution) and the legislative intent.

The *Alsup* case still seems to maintain considerable vitality, not only because the new wording is quite similar (albeit more sophisticated and elaborate), but also because the wording "actual cash value" was not changed in other sections. §67–101 (5) provides that it is the duty of the commissioner of finance to procure the assessment of all property in the State at the actual cash value thereof, and §67–103 (privilege taxes) states that the commissioner has the power to raise or lower any assessment fixed by the county court clerk on merchants, "in order to make said assessments conform to the standard of the actual cash value of the property."

It seems, therefore, that a refined actual cash value approach is used in State assessments, and that, as a result, property must be assigned such value.

Mortgage Financing

No provisions were found as to "flexible" mortgage financing. No provisions were found re: open-end mortgages.

The State does not require insurance companies doing business in Tennessee to write fire insurance in substandard areas; nothing of such requirement is contained in Chapter 25 of Title 56 (Fire Insurance), §§56–501—56–518.

Interjurisdictional Housing Authorities Are Provided by Statute

The Housing Authorities Law[159] specifically authorizes the establishment of housing authorities and spells out their extensive powers in §13–804 (in addition to the enumerated powers, "an authority may do all things necessary and convenient to carry out the purposes and provisions of the Housing Authorities Law."). Furthermore, housing authorities have specific powers as to blighted areas.[160]

The Tennessee court held in *Mink* v. *City of Memphis*[161] that the general law on housing in the State is not mandatorily applicable to any

[158] 107 Tenn. 257, 64 S.W. 193 (1901).
[159] T.C.A., §§ 13–801—13–831 (1972 Supp.).
[160] Id., §§ 13–813 & 13–814 (1955).
[161] 222 Tenn. 216, 435 S.W.2d 114 (1968).

municipality, but is merely authority for any municipality to establish a housing authority if it so desire.

All housing projects of an authority are subject to the planning, zoning, sanitary, and building laws, ordinances, and regulations applicable to the locality.[162]

City Housing Authorities: Any 25 residents of a city and of the area within 10 miles from the territorial boundaries thereof may file a petition with the city clerk setting forth that there is a need for an authority, and that the city council is to determine whether such a need exists.[163] If so, the authority is created as public body corporate and politic.[164]

It is interesting to note that the boundaries of such an authority embrace not only the city but the area within 10 miles from the territorial boundaries of the city (provided that the peripheral area does not lie within another city or within the boundaries of another housing authority).[165] Therefore, rural areas on the outskirts of a small town may be included in its housing authority.

"City" until 1965 was defined as a city or town having a population of over 2,000 inhabitants, but the numerical requirement was abolished in that year.[166]

County and Regional Authorities: Creation of and powers of such authorities are similar to those of city housing authorities.[167]

For our purposes, §13–1009 is the most important provision, since it deals specifically with rural housing projects. Basically, it provides that housing authorities created for counties, and regional housing authorities (explained under Interjurisdictional Housing Authorities, below), are specifically empowered to borrow money, accept grants, and exercise their other powers to provide housing for farmers of low income.

§13–1010 provides further that the owner of any farm operated or worked upon by "farmers of low income" [168] in need of safe and sanitary housing, may file an application with a housing authority of a county or regional housing authority, requesting that it provide for a safe and sanitary dwelling or dwellings for such farmers. This is a rather weak provision for several reasons. First, agricultural areas are exempted from the zoning regulations (see opening section on Tennessee). Second, the tenants or workers may not apply for such housing, and (at least in some cases) expecting the landlord or owner to seek better housing for them is unrealistic, especially in tenant farming situations. Third, and perhaps most crucially, the application of the owner is merely "received and examined" by the housing authorities in connection with the formulation of projects of programs. Thus, any and all effects of the application result from a discretionary choice on the part of the authority members.

Finally, in relation to rural housing, a regional or county housing authority has the power to sell or rent dwellings outside of cities and to make or accept such conveyances and leases as it deems necessary to carry out the rural housing purposes of the Housing Authorities Law.[169]

Interjurisdictional Housing Authorities: With regard to city housing authorities, if land within the 10-mile limits of any city is in another county and not covered by another housing authority, nothing would prevent the city from exercising jurisdiction in the adjoining county (under §13–1905).

A housing authority of City A may also exercise any and all of its powers within the territorial boundaries of another municipality (B), for the purpose of planning, undertaking, financing, constructing, and operating a housing project in B, if a resolution has been adopted by the governing body of B and by any housing authority theretofore established by B, declaring that there is a need for the housing authority of A to exercise its powers within B's territory.[170]

Consolidated housing authorities are also authorized, if the governing bodies of two or more municipalities by resolution declare that there is a need for one housing authority for all such municipalities.[171] The area of operation of a consolidated housing authority includes all of the territory within the boundaries of each municipality, together with the territory within 10 miles of the boundaries of each. Upon the creation of the consolidated housing authority, any housing authority theretofore created for the municipality ceases to exist.

Counties and Regional: Regional housing authorities may be created when the county court of each of two or more contiguous counties by resolution declare that there is a need for one housing authority to be created for all such counties; upon its creation, any county housing

[162] T.C.A., § 13–811 (1955).
[163] Id., §§ 13–901 & 13–902.
[164] Id., § 13–904.
[165] Id., § 13–905.
[166] Id., § 13–802 (1972 Supp.).
[167] Id., §§ 13–1001, 13–1008 (1955)
[168] Defined in § 13–802(19).
[169] Id., § 13–1011.
[170] Id., § 13–915.
[171] Id., § 13–918.

authority created for any of the counties involved ceases to exist.[172]

The area of operation of a regional housing authority includes all of the counties for which it is created, excluding the area within the boundaries of any city or municipality (unless a resolution has been adopted by the governing body of such city and also by any housing authority which was theretofore established, declaring that there is a need for the regional housing authority to exercise its powers within that city.)[173] The same holds true for county authorities and municipalities.[174]

Statewide housing corporations are not mentioned in the code, nor are specific rules relating to housing development corporations.

Home Rule in Tennessee

Tennessee has long been a jurisdiction wherein municipal corporations are considered creatures of the State legislature and dependent upon it. The early case of *Nichol* v. *Town of Nashville*[175] held that the legislature has the power to create corporations for the governing of towns, and to enlarge or diminish the powers of such corporations from time to time, at its discretion.

State v. *Frost*[176] reinforced this position, going further, if anything, by holding that the legislature has absolute power over the creation of municipal corporations and what their powers and duties are to be. For a recent (1965) articulation of this view, see *Town of Mount Carmel* v. *City of Kingsport*.[177]

Apparently, as of 1972, Tennessee has authorized municipalities to adopt home rule,[178] but aside from the election provisions in §6–509 and the city court provision in §16–201, there seems to be little statutory distinction between home rule and non-home rule municipalities in the Code.

Virginia Report on Legislation

Land Use Controls

The Commonwealth of Virginia has adopted three techniques of local land use control; planning commissions, subdivision ordinances, and zoning ordinances.

The first method to be considered is the local planning commission. Section 15.1–427 enables the governing body of any county or municipality to create by ordinance a local planning commission to promote the orderly development of such political subdivision. This planning commission serves primarily in an advisory capacity to the governing body. Planning commissions of one political subdivision may cooperate with planning commissions of other political subdivisions so as to coordinate the planning and development of the respective localities.[1] The sections providing for regional planning commission were repealed.

Among the major functions of the planning commission is to prepare and recommend a comprehensive plan for the physical development of the territory within its jurisdiction, including a land use plan, designation of a comprehensive system of transportation facilities, the designation of a system of community service facilities, and the designation of areas for urban renewal or other treatment.[2] After such a plan has been submitted by the commission and adopted by the governing body, it controls the general location, character, and extent of each feature shown on the plan. Thereafter, every street, park, or other public area, public building or public structure, public utility or public service corporation—before it may be constructed—must be approved by the commission as being substantially in accord with the adopted plan.[3] An official map may be adopted by the local planning commission,[4] and thereafter additions and modifications may be made to this map.[5]

The second means of land use control is by subdivision and development ordinances. Section 15.1–465 enables the governing body of any county or municipality to adopt ordinances assuring the orderly subdivision of land and its development. § 15.1–466 lists possible areas of regulation. In any county or municipality having a local planning commission, the subdivision ordinances are to be prepared and recommended by the commission.[6] After the adoption of a subdivision ordinance, certain provisions listed in §15.1–473 become effective. The local governing body is responsible for administering and enforcing the regulations[7] (§15.1–474). When the owner

[172] Id., § 13–1002.
[173] Id., § 13–1003.
[174] Id.
[175] 28 Tenn. 252 (1848).
[176] 103 Tenn. 685, 54 S.W. 986 (1900).
[177] 217 Tenn. 298, 397 S.W.2d 379 (1965).
[178] T.C.A., § 6–509 (1972 Supp.).

[1] Code of Virginia Ann., § 15.1–428 (1973).
[2] Id., § 15.1–446.
[3] Id., § 15.1–456.
[4] Id., § 15.1–458.
[5] Id., § 15.1–460.
[6] Id., § 15.1–470.
[7] Id., § 15.1–474.

of a tract of land subject to an ordinance wishes to subdivide his land, he must first submit a plot of the proposed subdivision to the local planning commission for approval.[8] When a plot for subdivision is accepted and recorded, it transfers to the local government such area on the plat that is set aside for streets, alleys, or other public use.[9] Under §15.1–480, if the owners of a subdivision wish to construct in or under any street in the subdivision any gas, water, sewer, or electric light or power works, pipes, wires, fixtures, or systems, they must present for approval plans or specifications to the governing body of the county or municipality in which the subdivision is located.

The third technique of land use control is zoning ordinances. Under §15.1–486, the governing body of any county or municipality may divide by ordinance into districts the territory or any substantial portion thereof. In each district, the governing body may regulate: (a) the use of land, buildings, structures, and other premises for specific uses, (b) the physical dimensions, construction, alteration, or removal of structures, (c) areas and dimensions of land, air, and water space to be used, (d) the excavation of soil or other natural resources, and (e) the sedimentation and soil erosion from nonagricultural lands. All zoning regulations within a district must be uniform for each class or kind of building or uses.[10] But regulations may vary among districts. The local planning commissions are to recommend regulations and boundaries. Where no planning commission exists, for a governing body to exercise its zoning power it must create a zoning commission until such time as a zoning commission exists.[11] §15.1–491 lists provisions that a zoning ordinance may include, such as provisions for variations in cases of unusual circumstances, for special exceptions, for the administration and enforcement of the ordinances, and for amendment and repeal of the regulations from time to time. The local planning commission at the request of the governing body is to prepare a proposed zoning ordinance. After the zoning ordinance has been adopted, it may not be amended unless the governing body submits the proposed amendment to the planning commission for recommendation. Also, the governing body may not adopt any ordinance or amendment without first holding a public hearing.[12]

[8] Id., § 15.1–475.
[9] Id., § 15.1–478.
[10] Id., § 15.1–488.
[11] Id., § 15.1–487.
[12] Id., § 15.1–493.

The enabling legislation also requires any governing body which has adopted zoning ordinances to create a board of zoning appeals.[13] This board has the power to hear appeals from decisions of the zoning administrator and to grant variances in special circumstances.[14] Any person aggrieved by a decision of the zoning administration has the right to appeal to the board.[15]

Any person aggrieved by a decision of the board, or any taxpayer, may petition the circuit or corporation court of the county or city to review a decision of the board.

The Commonwealth utilizes only local land use control and has no state wide control.

Regulations Governing the Use of Mobile Homes

There are three areas of regulation concerning mobile homes. These are: A statewide building code for mobile homes; health and sanitation laws affecting trailer parks; and highway restrictions on their movement.

The first area of regulation is the Industrialized Building Unit and Mobile Home Safety laws.[16] These laws apply both to mobile homes and industrialized building units (modular housing). Under § 36–73 the State Corporation Commission is to promulgate rules and regulations prescribing standards to be complied with in industrialized building units and mobile homes for protection against hazards to the safety of life, health, and prosperity. In formulating these standards, the commission is to have due regard for generally accepted safety standards by nationally recognized organizations. The statute specifically mentions—as examples of such codes in regard to industrialized building units—the Southern Building Codes Congress, the Building Officials Conference of America, the International Conferences of Building Officials, the National Fire Protection Association, and the National Bureau of Standards.

The statute specifically mentions—as regulations to be considered for mobile homes—the American National Standards Institute Standard A 119/1 and the National Fire Protection Association #501 B. Where practical, the regulations are to be in required levels of performance. Once the regulations are promulgated, any industrialized building unit or mobile home is

[13] Id., § 15.1–494.
[14] Id., § 15.1–495.
[15] Id., § 15.1–496.
[16] Id., § § 36–70–36—85 (1972 Supp.).

deemed to comply with the standards of the Commission when bearing the label, seal, or other evidence of listing by an approved testing facility,[17] (an approved testing facility is defined in § 36–71(5)). Industrialized building units or mobile homes bearing such evidence of listing are to be accepted as meeting any local ordinance concerning requirements of safety to life, health, and property, without further investigation or inspiration if the units are erected or installed in accordance with all conditions of the listing.

Local requirements including zoning, utility connections, and preparation of the site and maintenance of the units remain in effect. Unlabeled units are subject to full inspections for local requirements and for compliance with the regulations of the Commission. All local building officials are authorized to enforce the laws, rules, and regulations.[18] Representatives of the State Corporation Commission have the right to enter industrialized building units and mobile homes for examination as to compliance with rules and regulations of the commission upon the complaint of any person having an interest in any such unit or upon request of local officials having jurisdiction. Limitations to this right are that it not be occupied and used as a dwelling unit at the time, and that they may enter only during reasonable hours.[19]

The second area of regulation of mobile homes concerns the area in which they are parked—trailer camps. The legislation provides for both local and State regulations. Under §35–62, the governing body of any county may regulate the location and operation of trailer camps in the county. They may require the owners or operators of such camps to obtain a license. As a condition for obtaining a license or as a condition for operating such trailer camps, the local governing bodies may prescribe by ordinance the area and size of the lots to be used, the water supply, sewage, and garbage disposal facilities to be maintained (provided that such sanitary regulations are not in conflict with the regulations of the State board of health), safety measures for the heating facilities maintained in such trailers, and other measures that are reasonably necessary to protect the health, safety, and welfare of the people of the county and the occupants of such trailer camps. §35–64.1 to §35–64.4 enable local governments to license not only trailer camps but also individual lots not in trailer camps. Where a license is required, it is unlawful to park a trailer anywhere except in a licensed lot.

The State also regulates trailer camps. Under § 35–66 and § 35–73, the State Board of Health may issue rules and regulations governing cleanliness and general sanitation around trailer camps and provide for inspections of such camps. The State Board of Health also provides for the issuance and revocation of permits necessary to operate a trailer camp.[20] To carry out the provisions concerning health and sanitation, the State Health Commission or any agent of the State Board of Health is to have free access to any trailer camp during all reasonable hours.[21] The statutes also require that the camps provide adequate drainage[22] (§35–68), water supply[23] (§35–69), sewage disposal and toilet fixtures[24] (§35–70), and garbage disposal. Also, §35–67 requires that the owner of a trailer camp provide 1,000 square feet of ground, exclusive of the ground underneath the vehicles for each space rented.

The third area of regulation of mobile homes concerns restrictions on their movement on State highways. No vehicle, including the load thereon, traveling on State highways may exceed 96 inches in width.[25] No vehicle may exceed 13 feet, 6 inches in height.[26] Under § 46.1–331, the actual length of any combination of a towing vehicle and any mobile home coupled together may not exceed 55 feet. Statute § 46.1–330, which governs the length of coupled vehicles, generally permits the State Highway Commission to a special permit allowing movement of coupled vehicles exceeding 55 feet where the objects moved could not be moved otherwise. It is not clear whether the special permits authorized under §46.1–330 would be applied to mobile homes under § 46.1–331.

Usury

Virginia's general usury statute, § 6.1–319, provides that no contract may be made for a loan or forbearance of money at a greater rate of interest than 8 percent per annum. This rate includes points expressed as a percentage of the loan, divided by the number of years of the loan contract. The statute defines points as "the amount of money, or other consideration, re-

[17] Id., § 36–79.
[18] Id., § 36–81.
[19] Id., § 36–82.

[20] Id., § 35–74 (1970).
[21] Id., § 35–76.
[22] Id., § 35–68.
[23] Id., § 35–69.
[24] Id., § 35–70.
[25] Id., § 46.1–328.
[26] Id., § 46.1–329.

ceived by the lender, from whatever source, as a consideration for making the loan and not otherwise expressly permitted by statute." However, §6.1–319.1 excludes loans secured by first mortgages or first deeds of trust on real estate from the general usury statute. Such loans are enforcible at the interest rate stated therein on the principal amount loaned. There are several conditions attached to taking advantage of § 6.1–319.1. Every loan made under this provision, less than $75,000, must permit prepayment of the unpaid principal at any time, and no penalty in excess of 1 percent of the unpaid principal balance is allowed. Under this section, an "interest rate which varies in accordance with any exterior standard, or which cannot be ascertained from the contract without reference to any exterior circumstances or documents, shall not be an interest rate stated therein." An interest rate which varies with external circumstances may not be enforced beyond the legal rate of interest stated in § 6.1–319.

Certain charges are not considered in computing the allowable rate of interest. Anyone engaged in the business of making real estate mortgage or deed of trust loans for resale may charge an initial service, investigation, or processing fee. Such fee shall not exceed 1 percent of the amount of the loan, and the loan must have a maturity date of 10 years or more.[27] Also, on loans for the construction and improvement of real estate, the lender may charge and collect in advance inspection and supervision fees not to exceed 2.5 percent of the amount of the loan. If a lender provides both construction and permanent financing, the total fees may not exceed 2.5 percent.[28] The fees in § 6.1–323 and § 6.1–324 are not considered in determining the legality of the interest rate.

If a lender brings a suit to enforce a loan which provides for a usurious interest rate, judgment will only be for the principal. He forfeits all interest.[29] However, corporations, partnerships, professional associations, real estate investment trusts, and joint ventures organized for the purpose of holding, developing, and managing real estate for a profit may not use the usury laws as a defense to avoid payment of interest it contracted to pay.[30] Also the usury laws do not apply to loans insured by FHA, loans guaranteed by the Veterans' Administration, or insured or guaranteed by any similar Federal Government agency or organization, including HUD, or made persuant to the requirements of the Federal Home Loan Mortgage Corporation.[31]

§ 6.1–330 regulates certain junior mortgages. No loan secured by a mortgage or deed of trust that is not a first mortgage or deed of trust, or residential real estate improved by the construction of four or fewer family dwelling units, may be for an interest rate in excess of that permitted by §6.1–234 and §6.1–234.1 (7 percent in advance). The borrower on such loan has the right to prepay at any time and to receive a rebate on unearned interest.

Regulation Affecting the Homebuilding Industry

The main area of regulation affecting the homebuilding industry is the registration and licensing of general contractors and subcontractors. The statute only applies to those falling within the definition of "general contractor" or "subcontractor." They are defined as essentially any person, firm, association, or corporation that bids upon or accepts contracts for the construction, removal, repair, or improvement of any building or structure permanently affixed to real property or any other improvements to real property when either (a) "the total value of all such construction, removal, repair, or improvements referred to in a single contract or project is $30,000 or more, or (b) the total value of all such construction, removal, repair or improvements undertaken by such persons within any 12-month period is $200,000 or more." [32] Under § 54–128, no contractor or subcontractor (as defined above) may do business in the State unless he is licensed and obtains a certificate of registration from the State Registration Board of Contractors (authorized by §54–114). The Board has the authority to promulgate bylaws, rules, and regulations necessary to promote the ethical practices of contracting and subcontracting.[33]

A person wishing to obtain a license from the board must offer proof of his ability, character, and financial responsibility and a statement of his current financial position. If the information offered is satisfactory, he must then take an examination to determine his qualifications. If he passes the examination he may be issued an unclassified registration or a limited certificate

[27] Id., § 6.1–323 (1973).
[28] Id., § 6.1–324.
[29] Id., § 6.1–325.
[30] Id., § 6.1–327.

[31] Id., § 6.1–328.
[32] Id., § 54–113(2) (1970).
[33] Id., § 54–119.

such as building contractor or specialty contractor.[34] No political subdivision may issue a building permit without proof that the person seeking the permit has the proper registration.[35]

The governing bodies of counties, cities, and towns may also by ordinance provide for licensing of builders. Under § 54–145.2, such governing bodies may require every person engaged in the business of "home improvement, electrical, plumbing or heating or air conditioning contracting or the business of constructing single or multifamily dwellings" to obtain a license, except that contractors examined and registered under § 54-129 are exempt from such licensing.[36]

Another regulation affecting the home building industry is the provisions for licensing of architects, engineers, and land surveyors. Any person practicing as a professional engineer, architect, or land surveyor must first register with the State Board for the Examination and Certification of Architects, Professional Engineers and Land Surveyors before practicing.[37] In order to obtain a registration, a person must meet qualifications determined by the board[38] and must pass an examination.[39] The board may issue certificates to holders of certificate of registration in other States and the District of Columbia where the board determines that the requirements for registration in the other States are sufficient and that State offers reciprocity to holders of certificates from Virginia.[40]

State Housing Corporations

There are no special laws enabling State housing corporations. Laws enabling housing authorities and creating the Housing Development Authority have been included below.

Banks and Savings and Loans

Banks: I did not find much legislation concerning the operation of banks in the home mortgage field. One area of legislation is a restriction on the amount of a loan secured by real estate. Under § 6.1–63, no bank may make any loan secured by real estate when such loan together with all prior liens and encumbrances on the real estate exceeds 50 percent of the appraised value of the real estate securing the loan unless certain conditions are met. First, either the loan is "amortized by level or substantially level payments of principal and interest due at least as regularly as annually in amounts which would pay the loan in full over a period of 30 years or less or amortized by payments of principal due at least as regularly as annually, which are not less than 3½ percent per annum of the original principal of the loan. . . ." In either event, the loan together with all prior liens and encumbrances may not exceed 90 percent of the appraised value of the real estate. This section also provides that banks shall not make loans secured by real estate in an aggregate sum in excess of the amount of its capital and its surplus, or in excess of 70 percent of its time and savings deposits, whichever is greater. Under §6.1–65, where the bank reasonably and prudently relies on other factors than, or in addition to, the real estate security and enters in its records the factors relied upon, the loan does not constitute a loan secured by real estate within the measuring of §6.1–63 and therefore is not bound by its restrictions. Likewise, loans made to homeowners for maintenance, repair, modernization, improvement, and equipment to their homes, whether or not secured, do not fall within §6.1–63 if they meet certain limitations. The limitations are that the loan be for not more than $5,000 for a term not to exceed 7 years, and it is to be payable in approximately equal monthly installments.[41] Also, certain construction loans do not fall within § 6.1–63 provided that they meet the conditions of § 6.1–64. Loans made to finance the construction of a building or the improvement of real estate, having a maturity not exceeding 60 months, are not loans secured by real estate (§6.1–63) if accompanied by a valid and binding agreement to advance an amount equal to or greater than the construction loan upon completion of the building. Instead, such loans are classified as ordinary commercial loans.

Savings and Loans: The Commonwealth laws affecting the participation of savings and loan associations in the home mortgage field consist of statutes limiting the investments proper for a savings and loan.

Under § 6.1–195.34(c), a savings and loan may invest in stock or obligations of the Federal Home Loan Banks, the Federal National Mortgage Association, the Federal Savings and Loan Insurance Corporation or the Government National Mortgage Association.

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[34] Id., § 54–129.
[35] Id., § 54–136.
[36] Id., § 54–145.2.
[37] Id., § 54–27.
[38] Id., § 54–28.
[39] Id., § 54–29.
[40] Id., § 54–35.

[41] Id., § 6.1–66 (1973).

A savings and loan may invest its assets in loans secured by first liens on improved real estate, with certain limitations.[42] No loan shall exceed $45,000 on each home securing the loan. No loan shall exceed 90 percent of the appraised value of the real estate. Loans guaranteed or insured by a Federal agency, however, may be made on such terms as are acceptable to the agency. Savings and loans may also fully participate in such other housing programs approved by Federal associations as permitted by the commissioner. No loan made under §6.1–195.34(b) may exceed 30 years, with the provision mentioned above that loans guaranteed or insured by a Federal agency may be made on terms acceptable to the agency.

Up to 20 percent of a savings and loans' assets may be invested in secured or unsecured loans for maintenance, repair, alteration, modernization, landscaping, improvement, furnishing, and equipment of improved real estate. There is a limit of $10,000 and an 8-year limit on the term of such loans. Any loan insured or guaranteed by certain specified Federal programs may be made for the amount and terms that are acceptable to the agency.[43]

A savings and loan association may invest up to 5 percent of its assets in loans on mobile homes. The loan must be secured by a first lien on the mobile home, and the mobile home must be the residence of the borrower or a relative of the borrower. The loans are payable monthly and the term cannot exceed 12 years on a new, or 8 years on a used, mobile home. An association may collect in advance the legal rate of interest upon the entire amount of such loans.[44]

Under § 6.1–195.34(k), up to 20 percent of the assets of an association may be invested in other loans secured by a first lien or improved real estate. Under this section, a loan may not exceed 75 percent of the value of the real estate unless the real estate is located, or will within a year be located, on one or more single family dwellings or dwelling units for not more than four families in the aggregate, then a loan may be for 80 percent of the value of the real estate. A loan may be made for more than $45,000 under §6.1–195.34(h), provided that the excess of $45,000 be included within the 20 percent of (k).

Statutes also regulate the participation of savings and loans in mortgage transactions with other savings and loans. State associations and Federal associations may purchase from or participate with each other, or with instrumentalities of the State or of the United States, or with banks insured by the Federal Deposit Insurance Corporation in loans on real estate. An associate may participate in the making of, or purchase a participation in, a loan or real estate made by a savings and loan association that is not authorized to do business in Virginia not to exceed 90 percent of the amount of the loan, irrespective of where the security is located. An association may sell a participation in a loan made by it on real estate to a savings and loan association that is not authorized to do business in Virginia, provided that the loan is collected and received by the Virginia association. An association may purchase a loan it may legally make. An association may not engage in the mortgage brokerage business; but an association may sell any loan made by it, provided that it is sold without recourse against the association.[45]

Health Laws and Regulations As They Affect Safe and Sanitary Housing

Virginia provides for health, water, and waste regulation on both the State and local level. Included within this section are several diverse regulations lumped together under the title of health.

The first area to consider is regulation by the State. The State Board of Health may regulate the disposition of sewage in the State.[46] Under the same statutory authority, the board may require anyone to obtain a septic tank permit before commencing the construction of any building for which a septic tank will be installed. Such a permit is issued only after the local office is assured that the safe, adequate, and proper sewerage treatment is or can be made available. Under § 32–9.1, the board of health may also regulate solid waste disposal.

The State Board of Health is also authorized to establish official standards and regulations dealing with plumbing and plumbing equipment. The standards adopted may not be above those required by the American Standard National Plumbing Codes.[47] These statewide standards are to be enforced by local authorities.[48]

The last area of statewide regulation is in fire safety. The Virginia Fire Hazards Law requires the State Corporation Commission to

[42] Id., § 6.1–195.34(h).
[43] Id., § 6.1–195.34(i).
[44] Id., § 6.1–195.34(j).
[45] Id., § 6.1–195.39.
[46] Id., § 32.9.
[47] Id., § 32–406.
[48] Id., § 32–408.

promulgate minimum standards in public buildings for protection from fire hazards.[49] A public building is defined in § 27–65 as any building or structure which is used or occupied by 10 or more persons who are ". . . lodged, housed . . . therein." This specifically includes apartment houses. The State's power to regulate health in trailer courts has been discussed in the section on mobile homes.

Far more regulation is done on the local level. The three instruments of regulation are counties, municipalities, and special districts and authorities. Local governments are empowered to adopt such measures as they may deem expedient to secure and promote the health, safety, and welfare of the inhabitants of the locality, not inconsistent with State laws.[50] There is also specific enabling legislation.

The governing bodies of cities, towns, and counties may adopt rules and regulations (not inconsistent with the laws of the State) to secure the sanitary construction, alteration, and inspection of plumbing and sewer connections and drains. They may appoint an inspector who will report defects to the local board of health, which will cause such defects to be remedied.[51] The local governments may also regulate plumbing in the same manner as State regulation under §32–406, provided that the local regulations are not below those adopted by the State Board of Health (§32–407).

In any city or incorporated town, and for a half-mile radius beyond the corporate limits and elsewhere in the State where the local board of health deems it necessary, it is unlawful for the owner of any house or other building used for human habitation to rent, lease, or occupy a building unless the building has a sanitary privy or closet of such form as to comply with the law. If any landlord fails to provide a sanitary privy or closet, the tenant shall have one installed and he may deduct the cost from his rent.[52]

Another area of local health regulation concerns the health aspects of construction and maintenance of buildings and their appurtenances. This material will be covered again in the area of building codes and landlord tenant. Any county[53] or municipality[54] may regulate the construction, maintenance, and repair of buildings and other structures. Both may regulate the "installation, maintenance, operation, and repair of plumbing, electrical, heating, elevator, boiler, unfired pressure vessel and air conditioning installations in or appurtenant to buildings and structures."[55] Counties and municipalities both may regulate the emission of smoke, the construction, installation and maintenance of fuel burning equipment, and the methods of firing and smoking furnaces and boilers.[56] Both may regulate the light, ventilation, sanitation, and use or occupancy of buildings.[57] Municipalities may compel the abatement of all nuisances, including the removal of unsanitary and unsafe substances from premises and the removal or repair of all unsafe, dangerous, or unsanitary housing. If the owners refuse to abate the nuisance upon notice, then the municipality may do so and collect the cost from the owner.[58]

Local governments are also empowered to issue fire safety regulations. Under § 27–5.1, the governing body of any county, city, or town may adopt by reference any building, plumbing, electrical, gas, fire protection or fire prevention code promulgated by an authoritative body. Any code adopted must meet the minimum standards prescribed by the Virginia fire hazards law.

The last areas of health regulation concern water and waste systems. I will first treat county regulation in these areas. Counties that have adopted land use and development ordinances pursuant to § 15.1–427 et seq., may also adopt regulations fixing requirements as to the extent to which and the manner in which water, sewer, and other utility remains, piping, conducts, connections, pumping stations and other facilities will be installed as a condition necessary for approval of a subdivision plan or alteration of such a plan pursuant to § 15–491.[59] These regulations are subject to the provisions of State control under § 62.1–44.2 et seq.

The counties also have the power to establish public sewers and public water mains along the streets, alleys, and public highways in any incorporated town, village, or suburb of any city whether title to such streets, alleys, or highways is vested in the governing body or not. The owners of adjacent lands have the right to connect their land with such sewers and water mains on such terms as the governing body describes.[60]

[49] Id., § 27–72.
[50] Id., §§ 15.1–510 (counties) and 15.1–683 (municipalities).
[51] Id., § 32–61.
[52] Id., § 32–64.
[53] Id., § 15.1–510.2.
[54] Id., § 15.1–863.
[55] Id., §§ 15.1–510.3, 15.1–864.
[56] Id., §§ 15.1–510.5, 15.1–868.
[57] Id., §§ 15.1–510.5, 15.1–869.
[58] Id., § 15.1–867.
[59] Id., § 15.1–299.
[60] Id., § 15.1–300.

The list of general powers of counties also gives them authority to regulate in this area. Under §15.1–520, counties may regulate the installation of septic tanks, including requiring a septic tank permit. The board of supervisors of a county may adopt land use regulations requiring a subdivision or land developer to pay his pro rata share of the cost of providing reasonable and necessary sewage and drainage facilities located outside the property limits of the developer but necessitated at least in part by the construction or improvement of his development.[61] Any person constructing a sewage system [62] or a water supply system [63] having three or more connections must first get the approval of the governing body of the county.

The municipalities also have general powers in water and waste. A municipal corporation may regulate and inspect public and private supplies and the production, preparation, transmission, and distribution of water.[64] It may regulate and inspect public and private sewers.[65] A municipal corporation may require the installation, maintenance, and operation of septic tanks or other means of disposing of sewage when public sewers or sewage disposal facilities are not available.[66] Where the municipality provides water facilities [67] and sewage disposal service,[68] the municipality can require the connection of premises with such facilities.

Aside from health regulation by municipalities and counties, there is also regulation by special districts. Under the Virginia Water and Sewer Authorities Act, one or more political subdivisions may create water or sewage authorities.[69] These have several effects on homeowners. The authority may, subject to local restrictions, enter, use, occupy, or dig up private lands necessary for the acquisition, constructing, or improvement of water or sewage systems [70] (§15.1–1250(m)). Also, §15.1–1261 provides that where such authorities have been created, the authority—with the approval of the local government—may require the owner, tenant, or occupant of each lot or parcel of land which abuts upon a street or public way that contains a water or sewage system to cease using any other source of water supply for domestic use or any other method for the disposal of sewage, waste, or other polluting matter.

Another form of district is a sanitary district created under the provisions of §21–113. Where such sanitary districts have been created, the board of supervisors has the power to require the owners or tenants of any property in the district to connect up with sanitation systems [71] (§21–118.4(d)).

Environmental Laws Affecting Housing

The area of environmental protection is in a state of flux in Virginia. The 1973 legislature abolished many existing programs and instituted new ones which will go into effect on July 1, 1974, and will expire on July 1, 1975 unless continued by legislation prior to that time.[72] I will try to treat generally the areas of regulation. It is difficult to access the impact of these laws on housing because they are not yet operative.

The new environmental legislation is the Environmental Coordination Act of 1973. As mentioned above, the act becomes effective July 1, 1974. The act provides for a unified program of environmental protection. Under §10–17.34, a Department of Conservation, Development and Natural Resources is created. Also created within the new department are five divisions, including the Division of Air Pollution and Solid Waste, the Division of Water Resources, and the Division of Natural Resources. In each of the divisions mentioned a board is created.[73] Among the powers of the Commissioner of the Department is the power to issue, deny, revoke, or modify all permits, licenses, and certificates required by law.[74] He is also empowered to coordinate the application and processing requisites for State permits with those required by any provision of Federal law.[75] §10–17.65 provides that any rules or regulations promulgated prior to July 1, 1974, concerning matters covered by the act remain in force until specifically revoked or until they expire.

§10–17.66 to §10–17.84 provides the air quality control section of the Environmental Coordination Act. Prior to July 1, 1974, the power to adopt rules and regulations concerning abating, controlling, and prohibiting air pollution resided with the State Air Pollution Board.[76] This board,

[61] Id., § 15.1–510.7.
[62] Id., § 15.1–326.
[63] Id., § 15.1–341.
[64] Id., § 15.1–854.
[65] Id., § 15.1–855.
[66] Id., § 15.1–856.
[67] Id., § 15.1–875.
[68] Id., § 15.1–876.
[69] Id., § 15.1–1241.
[70] Id., § 15.1–1250(m).

[71] Id., § 21–118.4(d).
[72] Acts 1973, Ch. 471, cl. 5.
[73] Code of Virginia Ann., § 10–17.40 (1973 Supp.).
[74] Id., § 10–17.36.
[75] Id., § 10–17.55.
[76] Id., § 10–17.18.

until its expiration, had the power to issue orders to enforce its rules and regulations, to hear complaints of violations, and to initiate court action to enforce its regulations and orders.[77] On July 1, 1974, the State Air Pollution Control Board ceased to exist and its powers and duties were vested in the Department of Conservation, Development and Natural Resources.[78]

Certain duties are assigned to the Air Pollution and Solid Waste Board. Among the duties and powers of the board are to establish air quality standards [79] and to adopt rules and regulations to enforce the general air quality management program in the State.[80] The statute specifically provides that the standards, rules, and regulations should not encourage any degradation of air quality in any air basin or region at present superior to that stipulated in the standards, policies, rules, and regulations.[81] Among the powers of the Commissioner of the Department of Conservation, Development and Natural Resources, are the powers to enforce all rules and regulations promulgated, to administer a State permit system, and to issue any permits or licenses required by the Federal Clean Air Act.[82] The board may create local air pollution control districts to aid in enforcement.[83] Local ordinances in existence prior to July 1, 1972, continue in force, but in any conflict between the ordinance and the rules and regulation of the board, the board's rules govern unless the local ordinance is stricter, in which case the latter governs. Any ordinance passed after July 1, 1972, must be approved by the board.[84] As I mentioned above and will point out again, it is impossible to determine how the rules and regulations issuing from this legislation will affect housing. However, it is certainly conceivable that they will affect housing.

The environmental act also provides for regulation for solid waste disposal.[85] Powers to regulate in this area, previously exercised by the State board of health under §32–9.1, are vested on July 1, 1974, in the Department of Conservation, Development and Natural Resources.[86] This chapter, like the one dealing with air pollution, vests certain powers and duties to regulation in the hands of the Commissioner and the Air Pollution and Solid Waste Board. Although the regulation deals directly with cities, towns, and counties, it will indirectly involve the solid waste disposal requirements for dwellings.

The environmental act also provides for water resources regulation. It repeals the present State Water Control Law [87] and replaces it with the State Water Resources Law.[88] Again, power is transferred from the State Water Control Board to the Department of Conservation, Development, and Natural Resources. Among the powers of the new Water Resources Board are to establish standards of water quality, to establish programs for areawide water quality control and management, and to establish requirements for the treatment of sewerage.[89] Among the duties of the commissioner are to enforce the standards and the statutes and to issue certificates for discharge of sewerage.[90] Again, as with the other areas, regulation could affect housing, but it might not. It is impossible to tell without the regulations.

The last area of regulation is the Critical Environmental Areas Law.[91] Under this plan, the Division of State Planning and Community Affairs is to designate certain areas as critical environmental areas.[92] After the areas have been delineated, the division is to develop standards for protective land use and development of the areas.[93]

Welfare Lien Law

§63.1–133.1 specifically provides that no lien or other interest in favor of the State or any political subdivision may be claimed against the personal or real property of any welfare recipient as a condition of eligibility.

Taxation

Virginia has a sales tax. There is a State sales tax of 3 percent on each item of personal property sold at retail or distributed in the State.[94] There is also a 3 percent use tax upon the use or consumption of tangible personal property within the State or the storage of such property outside the State for use in the State.[95] Mobile homes, however, are excluded from the application of the sales and use tax by

[77] Id., § 10–17.18(O).
[78] Id., § 10.17.68.
[79] Id., § 10–17.69(1)(9).
[80] Id., § 10–17.69(2).
[81] Id., § 10–17.69(3).
[82] Id., § 10–17.71.
[83] Id., § 10–17.82.
[84] Id., § 10–17.83.
[85] Id., §§ 10–17.85—10–17.99.
[86] Id., § 10–17.85 (1973).

[87] Id., §§ 62.1–44.2—62.1–44.34 (repealed in 1973 Supp.).
[88] Id., §§ 62.1–44.45—62.1–44.82 (1973 Supp.).
[89] Id., § 62.1–44.51.
[90] Id., § 62.1–44.52.
[91] Id., §§ 10–187—10–196.
[92] Id., §§ 10–190 + 10–191.
[93] Id., §§ 10–192 + 10–193.
[94] Id., §§ 58–441.5.
[95] Id., §§ 58–441.5.

§58–441.6(e). I have not been able to determine if modular housing is taxed as real or personal property, so I cannot tell if it is subject to the sales tax. The cities and counties may impose a 1 percent sales or use tax in addition to the sales tax.[96] The local tax is subject to all the provisions of the State tax, however, so the local tax does not apply to mobile homes.

Under §58–441.15(a), a person who contracts to perform construction, reconstruction, installation, repair, or other services with respect to real property, and in connection with this service to provide tangible personal property, must pay the use tax on the personal property. Also under §58.441.15(d), "tangible personal property incorporated in real property contracts which loses its identity as tangible personal property shall be deemed to be tangible personal property used or consumed within the meaning of this section." This section might apply to the components of modular housing, but, again, I have been unable to ascertain how modular housing is classified. I have not found a case interpreting §58–441.15(d).

Although mobile homes are not subject to the sales tax, they are subject to the Virginia motor vehicles sales and use tax. Under §58–685.12, the Commonwealth levies a tax of 2 percent of the sales price on every motor vehicle sold in the State, and a 2 percent tax on every motor vehicle not sold in the State but used or stored in the State more than 6 months after their acquisition, the 2 percent tax is on their current market value. This tax apparently applies to mobile homes because a mobile home fits the definition of motor vehicles given in §58–685.11(3). The tax must be paid by the purchaser or user at the time he applies for and obtains a certificate of title. No tax is required of a motor vehicle for which no certificate of title is required. However, §46.1–41 requires a certificate of title for mobile homes. Any transfer of any mobile housing, where permanently attached to the real estate and included in the sale of the real estate, is not a sale of a motor vehicle and therefore is not taxable.[97]

Personal Property Tax

Under Article X, §4, real estate and tangible personal property are segregated as subjects of local taxation. §58–829 is the statutory basis for local taxation of tangible personal property.

[96] Id., §§ 58–441.49 + 58–441.49.1.
[97] Id., § 58–685.11(5).

However, §58–829.3 makes mobile homes a classification for local taxation separate from other classifications of personal property, provided that the rate of assessment and the rate of tax do not exceed that applicable to other classes of personal property.

I found no statute providing for taxation of mobile homes as real property under any circumstances. I found no authority determining that modular housing is taxed one way or the other.

Uniform Statewide Building Code

Virginia has recently passed legislation to create a statewide building code. By §36–98, the State Board of Housing was empowered to promulgate a Uniform Statewide Code. This code supersedes any building codes or regulations of the counties, municipalities, and State agencies. Prior to this, under §27–5.1, local governments could adopt building codes by reference. The building code is to prescribe standards to be complied with in the construction of buildings. Where practical the provisions are to be stated in terms of required levels of performance. In formulating the standards, the board should "have due regard for generally accepted standards as recommended by nationally recognized organizations, including, but not limited to, the standards of the Southern Building Code Congress, the Building Officials Conference of America, and the National Fire Protection Association.[98] I do not know whether the code has been issued yet, since it was not to become effective before January 1, 1973, or later than September 1, 1973. The local building department is entrusted with the duty to enforce the code. Any building may be inspected before completion and is not deemed in compliance until approved by the inspecting authority.[99] The statutes also provide for the creation of a Board of State Building Code Review.[100] The board is empowered to hear appeals from decisions concerning the building code, and even to interpret the code and to make recommendations concerning amendments to the code.

Minimum Housing Code and Landlord and Tenant Relations

There is no State minimum housing code. However, §27–72 requires the State Corporation

[98] Id., § 36–99 (1972 Supp.).
[99] Id., § 36–105.
[100] Id., §§ 36–108—36–119.

Commission to prescribe minimum standards in all public buildings for the protection of life and property from hazards incident to fire. Public buildings, including apartment buildings, are those occupied by 10 or more persons. This assures at least some minimum safety standards.

There is no explicit provision stating that localities may institute minimum housing codes. There are several provisions, however, from which such a power may be inferred. Under the general powers of local governments, §15.1–11.2 enables the governing body of any county, city, or town by ordinance to provide that owners of property remove, repair, or secure any building which might endanger the public health. Under §15.1–510 (counties) and §15.1–839 (municipalities), local governments may adopt such measures as it may deem expedient to secure and promote the health, safety, and welfare of the inhabitants of the locality, not inconsistent with State laws. §15.1–510.2 (counties) and 15.1–683 (municipalities) enable local governing bodies to regulate the construction, maintenance, and repair of buildings, providing such regulations are uniform through the district. The local governing bodies may also regulate the installation and maintenance of plumbing, electrical, heating, elevator, and boiler installations in buildings.[101] Lastly, §27–5.1 enables the governing body of any county, city, or town to adopt by reference any building, plumbing, electrical, gas, fire protection, or fire prevention code promulgated by an authoritative body, provided such codes meet the minimum standards prescribed by the Virginia fire hazards law.

There is no provision for tenant suits for damages in cases of a landlord's not meeting a minimum housing code.

There is no statute giving the tenant the right to withhold payment for failure to comply with a minimum housing code.

Local government is empowered to make repairs on substandard dwellings and to make the cost a lien on the dwelling. Under §15.1–867, a municipal corporation may compel the abatement or removal of all nuisances. Included in the action specified was the razing or repair of all "unsafe, dangerous or unsanitary public or private building" which constitute a menace to the health and safety of the occupants or the public. If after reasonable notice the owners or occupants fail to remedy the condition, the municipal corporation may do so and collect the costs from the owners or occupants of the property in any manner provided by law for the collection of State or local taxes. In the general powers of local government, §15.1–11.2 provides that the governing body of any county, city, or town may by ordinance require the owners of property to remove, repair, or service any building that might endanger the public health or safety. The governing body, through its agents or employees, may make the repairs where the owner fails to do so after reasonable notice and a reasonable time to do so. If the governing body makes such repairs, the costs are chargeable to the owners and may be collected as taxes and levies are collected. Every charge levied against an owner but unpaid constitutes a lien against such property.

The statutes which provide authority to repair substandard buildings also gives local governing bodies the right to close, vacate, and demolish substandard housing. §15.1–11.2 permits the governing bodies of counties, cities, and town by ordinance to require owners to remove any building that might endanger the public safety or health. If, after reasonable notice, the owner fails to act, the agents or employees of the governing body may remove the building. Costs are to be charged to the owner as described above concerning repairs. §15.1–867 enables municipal corporations to compel the removal of nuisances. It may require the razing of all unsafe, dangerous, or unsanitary public or private buildings that constitute a menace to the health and safety of the occupants thereof or to the public. If, after notice, the owner refuses to act, the municipality may raze the building and provide for charging the cost to the owner as described above.

In addition to the powers of counties and municipalities to repair or demolish substandard dwellings, housing authorities have some power in this field. Under §36.6, counties, cities, and towns may enter into agreements with housing authorities to exercise their power to repair, eliminate, or close unsafe, unsanitary, or unfit dwellings. When an authority undertakes a redevelopment project, it may acquire by eminent domain dwellings within the blighted area to be redeveloped.[102] Also, where an authority undertakes a conservation plan, it may acquire and demolish dwellings which do not meet requirements for the plan and have not been rehabilitated within 1 year of notice.[103]

[101] Id., §§ 15.1–510.3, 15.1–864 (1973 Supp.).

[102] Id., §§ 36–48 + 36–49 (1970).

[103] Id., § 36–50.1.

Housing Court and Appointment of a Receiver

I found no special provision for a housing court or similar court.

I found no legal authority for the court appointment of a receiver to collect rent and to make improvements.

Foreclosure of Tax Delinquent Housing

Virginia in 1973 repealed its comprehensive statute on foreclosure of tax-delinquent housing and replaced it with a far less comprehensive one.[104] The newer method provides a slower means of foreclosure.

Under § 58–762, there is a lien on real estate for taxes and levies assessed on the real estate. This tax lien is prior to any other lien on the property. Prior to August 1 of each year, the treasurer of the county or city compiles a list of real estate which is delinquent for the nonpayment of taxes as of June 30 of that year.[105] The treasurer presents this list at the first meeting of the governing body occurring after the list's compilation. The governing body publishes the list once, and if the taxes remain unpaid on the third anniversary of the due date, a lien is recorded in the clerk's office.[106]

Under the law just repealed, the real estate could be sold in December of the year following the presentation of the delinquent list. Under the present law, the delinquent real estate may be sold on December 31 following the third anniversary of the due date, after proper notice.[107] The procedure for foreclosure is a suit in equity brought by an attorney appointed by the local government. All necessary parties must be defendants, and the purchaser takes possession free of all claims of beneficiaries under any deed of trust or mortgage.[108] The title of the purchaser is governed by the laws applying to purchases at judicial sales generally. The former owner is entitled to any surplus in excess of the tax, penalties, interests, costs, and any liens chargeable thereon.[109] The county or city may be a purchaser at a tax sale [110] (§58–1117.6). It is interesting to note that the statute makes no special provisions concerning equity of redemption.

[104] Id., §§ 58–1117.1—58–1117.11 (1973 Supp.).
[105] Id., §§ 58–978(2) + 58–979.
[106] Id., § 58–983.
[107] Id., § 58–1117.1.
[108] Id., § 58–1117.3.
[109] Id.
[110] Id., § 58–1117.6.

Fire Insurance

Virginia does have a program to provide fire insurance in substandard areas. This plan is the Basic Property Insurance Inspection and Placement Plan and Joint-Underwriting Association. One important limitation is that the plan does not include property used for farm purposes. Qualified property in its definition excludes farm property and specifies that the property be in an urban area. The property, which may include real and tangible personal property, must comply with applicable State laws and local building codes and ordinances.[111]

Under the plan, a person meeting the qualifications above would have his property inspected by an inspection bureau created for the purpose. The authorized insurers in Virginia are to formulate and administer a program for the equitable distribution and placement of applications for fire and extended coverage insurance for qualified property that has been inspected.[112] If the State Corporation Commission finds that the program devised by the insurers under § 38.1–748 is failing to provide adequate insurance for qualified property, the commission may order the creation of a joint underwriting association. All insurers authorized to write fire and extended coverage in the State must be members of the association as a condition precedent to doing business in the State. The association is to formulate a program to carry out the purpose of this statute. The association has the power to cause its members to issue policies to applicants to assure reinsurance from members and to cede reinsurance.[113]

The degree of participation in the association by members of the associations is in the proportion of each member's total yearly premiums to the total yearly premiums of all members of the association.[114]

Improvements and Existing Levels of Assessment

I found no legal authority authorizing tax officials to maintain existing levels of assessment following improvement of substandard housing. Under Article X, §2 of the Virginia Constitution, assessment of real property must be for its fair market value. This would seem to be a barrier to such a law.

[111] Id., § 38.1–747(3) (1970).
[112] Id., § 38.1–748.
[113] Id., § 38.1–750.
[114] Id., § 38.1–751.

Mortgages

I did not find legislation permitting interest abatement during the early years of mortgage payments on low and middle income housing.

I also did not find State legislation permitting or forbidding open-end mortgages.

Housing Authorities Law

§36.4 creates Redevelopment and Housing Authorities in each city and county in the Commonwealth. Where no housing authority presently exists, it can only come into existence by a vote of the people of the city or county. The municipality may exercise certain of its powers to aid the authority in the development and operation of housing projects.[115] Examples of the cooperation enabled are aid in zoning or rezoning (d) and entering into agreements with respect to the municipality's powers relating to the repair, elimination, or closing of unsafe, unsanitary, or unfit dwellings. §36.19 lists an enumeration of the powers granted the authority along with the other specified powers. The housing projects operated by the authority are not to be operated for a profit.[116] Under Article X, §6(1) of the Virginia Constitution, the property owned by the authority is exempt from all State and local tax. §36–22 provides that the authority shall rent only to persons of low income and that the authority should create guidelines to determine low income status. A housing authority may exercise its powers in a municipality, but not within its territorial boundaries, to operate a housing project, provided that the project is approved by resolution by the municipality.[117] Two or more housing authorities may cooperate in planning, constructing, and managing a housing project or projects within the territory of one of the authorities. The authorities are empowered under §36–26 to cooperate with the Federal Government. The authority has the power of eminent domain to acquire real property necessary for the purposes of the authority.[118] All housing projects of an authority are subject to the planning, zoning, sanitary, and building laws, ordinances, and regulations of the locality. Sections 36–29 through 36–35 describe the financial powers of the authority.

[115] Id., § 36–6.
[116] Id., § 36–21.
[117] Id., § 36–23.
[118] Id., § 36–27.

Rural Housing

There is a special article (5) concerning rural housing projects. Under §36–36, county and regional housing authorities are specifically empowered to exercise their powers to provide housing for farmers of low income. The authorities may rent or sell dwellings forming part of such projects to farmers of low income. Rural housing is exempted by §36–37 from the tenant selection limitations provided in §36–22(c). The owner of any farm operated or worked on by farmers of low income in need of safe and sanitary farming may file an application with a county or regional authority requesting the authority to provide such housing. The authorities are to receive and consider such applications in formulating programs to provide housing for farmers of low income.

Regional and Consolidated Housing Authorities

The board of supervisors of two or more contiguous counties may create a regional housing authority.[119] When such regional authorities exist, the individual authorities of the counties cease to operate. The regional housing authorities have within their territory the same powers as the municipal and county authorities have in theirs.[120] There are also provisions for uniting municipal housing authorities. Under §36–47, the governing bodies of two or more municipalities may create consolidated housing authorities. When such consolidated authorities are created, the individual authorities cease to function. The consolidated authorities have the same powers and duties as the individual authorities. A municipality having two or more housing authorities may cause such authorities to be consolidated.[121]

There are no provisions for a statewide housing authority other than the Virginia Housing Development Authority, discussed elsewhere.

The Housing Authorities Law also empowers authorities to undertake redevelopment projects [122] and conservation plans [123] in blighted areas. The powers of authorities in redevelopment projects are listed in Code of Virginia Ann., §36.49 (1973 Supp.). It is interesting to note that in the redevelopment of blighted areas, the authority may condemn property which is not blighted but which exists in the blighted area.[124] Also under his power

[119] Id., § 36–40.
[120] Id., § 36–46.
[121] Id., § 36–47.2.
[122] Id., § 36–49.
[123] Id., § 36–49.1.
[124] *Hunter v. Norfolk Redevelopment + Housing Authority*, 195 Va. 326.

to redevelop, an authority may make lands available to private enterprises or public agencies in accordance with the redevelopment or conservation plan.[125]

Virginia Housing Development Authority Act

Virginia does not have laws enabling the establishment of State housing corporations. Nor does it regulate the operation and development of housing development corporations. It did create the Virginia Housing Development Authority Act. The Housing Development Authority (HDA), created by §36–55.27 as a political subdivision of the Commonwealth, has as its general purpose the creation of needed safe and sanitary low income housing through technical and financial assistance to public and private efforts. A statement of purpose and a list of powers can be found in §36–55.26 and §36–55.30.

Since much of the legislation is detailed financial powers and restrictions, it is difficult to summarize. I shall try to point out some of the general features, however. Under certain conditions specified in §36–55.31, HDA may make mortgage loans and temporary funding for construction and rehabilitation of housing developments to housing sponsors. Where long term mortgages on similar terms are not available, HDA may make first mortgage loans to low and moderate income persons and families to purchase residential housing. The loans to sponsors, and mortgages to low income persons and families, are limited by the terms and conditions in §36–55.34.

§36–55.32 lists HDA's powers in relation to purchasing and selling mortgage loans and the making of loans to mortgage lenders. Among the powers are the powers to invest in, purchase, and take, on assignment from mortgage lenders, notes and mortgages evidencing loans for the construction, rehabilitation, purchase, leasing, or refinancing of residential housing for persons of low and moderate income. The rest of the powers can be found in §36–55.31 through §36–55.33. The exercise of all these powers in §36–55.32 is subject to the terms and conditions of §36–55.25 and §36–55.36.

HDA has the power to supervise housing sponsors in a list of areas specified in §36–55.33. Among the areas of supervision is the power of HDA to set rent rates and to control tenant selection. HDA may also supervise the operation and maintenance of housing developments, including repairs.

§36–55.40 to §36–55.49 give details as to the powers and obligations of HDA in regard to issuing bonds.

Areas in Which No Laws Were Found

There were no special laws enabling the establishment of State housing corporations.

There was no State legislation permitting tenant suits for damages in cases of a landlord's failure to meet minimum housing codes.

I found no legislation giving the tenant the right to withhold payment of rent if the unit does not comply with the minimum housing code.

There is no provision for a special housing court or similar court.

I found no legal authority for court appointment of a receiver to collect rent and make improvements.

I found no legal authority authorizing tax officials to maintain existing levels of assessment following improvement of substandard housing.

I did not find State legislation permitting flexible mortgage finance or open-ended mortgage financing.

West Virginia Report on Legislation

In the State of West Virginia, the primary responsibility for community planning is delegated to local units of government.[1] Because planning involves the rural areas of the State, it is the county government that bears the primary responsibility. The county body is a three-man commission, called the county court.[2] The county courts are authorized to appoint county planning commissions to carry the primary responsibility for planning. The county planning commissions are authorized to develop comprehensive plans concerning a wide range of variables including streets, waterways, playgrounds, public facilities, forests, agricultural areas, and the distribution of the population.[3]

After the appropriate hearings and the adoption of a comprehensive plan by the planning commission, the plan is submitted to the county court which must accept the plan to give it effect. Once the plan is accepted by the county court it is incorporated by reference in the ordinances of the county.[4]

[125] Code of Virginia Ann., § 36-53 (1970).

[1] West Va. Code Ann., § 8-24-1 (1969).
[2] W. Va. Constitution, Art. 8, § 22.
[3] W. Va. Code Ann., §§ 8-24-16 (1969), 8-24-17 (1969).
[4] Id., § 8-24-21 (1969).

The county courts are expressly authorized to cooperate with the Federal Government regarding the exchange of planning information, as well as cooperating to integrate planning on a broader scale.[5] They are also authorized to participate in Federal planning assistance programs.[6]

Once a comprehensive plan concerning the development of housing subdivisions has been promulgated by the planning commission and enacted into ordinance by the county court, no plan or subdivision may be recorded within the jurisdiction of the planning commission without the permission of the commission.[7] The local planning commission has exclusive jurisdiction over subdivision and plan control.[8]

With respect to zoning authority, each county court is empowered to act on the recommendation of the planning commission to enact local zoning ordinances.[9] To the extent that any conflict arises between State enactments concerning zoning and local ordinances governing the same situation, the stricter of the two applicable laws is to be applied.[10] But this provision seems to be of little consequence since at this juncture there appears to be no State law directly controlling zoning.

It is important to note that public housing projects under the administration of the local housing authorities are subject to the county or municipal zoning ordinances as well as other locally promulgated regulations.[11]

A recent development in West Virginia law that has important implications for any Federal effort in the rural housing field is the recently enacted section 8–24–50a. Component and factory-type housing is freed from any local or State building code or other regulation if the housing is approved as meeting the standards for such housing set by the Federal Department of Housing and Urban Development. Certification by the State director of the Federal Housing Administration is evidence that the applicable HUD standards have been complied with. It is important to note that preemption of State and local regulation does not extend to local zoning and land use planning laws. It is quite conceivable that modular housing may still face substantial legal barriers in some communities. The possibility of preemptive or highly restrictive zoning may exist as an impediment to expanded use of modular housing.

Although there is no statewide planning commission, regional planning is authorized and encouraged by State legislation.[12] Regional planning commissions are established in designated regions. The commissions are composed of a representative of every municipality and county in the designated region. The representatives are to be selected on the county level by the county court, and at the municipal level by the mayor or his designate.[13] The regions for which regional planning commissions are established are to be approved and determined by the Governor after the effective date of this legislation. The factors to be considered in determining these regions include community interest and homogeneity, geographic features, communication, and transportation, as well as such things as existing governmental services and municipal boundaries.[14]

Each commission is empowered to prepare plans for the development of various community services, land development, etc.; to prepare and recommend ordinances to implement the commission planning; to provide technical assistance to the local communities; and to exercise its powers jointly with other agencies or political subdivisions of the State of West Virginia, any other State, or the United States.[15]

Building and Housing Codes

West Virginia has not enacted a statewide building code nor has it set any standards for the adoption of a national building code by the local units of government. Counties are only authorized to adopt or promulgate building codes if the population of the county is in excess of 200,000.[16] This leaves rural counties with small populations powerless to establish minimum standards. And it leaves them completely without any regulation of construction without State action. Where counties are authorized to promulgate or adopt a code, there are no statutory guidelines for inspection procedures or enforcement of the code. Thus, it would appear that inspection and enforcement are subject to the determination of the county courts under the general grant of administrative power given by the State legislature to the county courts.[17] As

[5] Id., § 8–24–27 (1969).
[6] Id., § 8–24–6 (1969).
[7] Id., §§ 8–24–28 (1969), 8–24–30 (1969).
[8] Id., § 8–24–35 (1969).
[9] Id., § 8–24–40 (1969).
[10] Id., § 8–24–70 (1969).
[11] Id., § 16–15–9 (1972).

[12] Id., § 8–25–1 (1969).
[13] Id., § 8–25–5 (1969).
[14] Id., § 8–25–4 (1969).
[15] Id., § 8–25–8 (1969).
[16] Id., § 7–1–3n (1969).
[17] Id., § 7–1–3 (1969).

has been noted earlier, the effect of section 8–24–50a of the West Virginia Code is to preempt the application of county building codes where component housing is HUD-approved.

The State legislature has not established a statewide minimum housing code, but as is the case with building codes, counties of over 200,000 people are authorized to promulgate or adopt such codes to promote public health and welfare.[18]

Because there is no statewide building or housing code, a body of State law has not developed to enforce minimum standards of either State or local origin. For example, a tenant does not have the right to withhold rent if minimum standards created by the local government are not met, absent the appropriate local ordinance. Indeed, the landlord has no common law duty to repair property unless there is an express contractual obligation.[19] Likewise, there appears to be no statutory or case authority for the appointment of a receiver to collect rents and make improvements on substandard housing, or for local agencies, such as the county housing authority, to make repairs on substandard housing, retaining a lien on the property in the amount of the cost of repairs. Also, there is no specialized adjudicatory body which handles only housing matters.

There does appear to be power in local agencies—primarily slum clearance and redevelopment authorities and housing authorities—to vacate and clear away slum and substandard housing. Under the Urban Renewal Authority Act, counties are authorized to establish a slum clearance and redevelopment authority.[20] This agency is granted broad power to deal with the problem of slum and substandard housing, including, importantly, the power of eminent domain.[21]

Under the authority of the State Housing Law, each county and municipality is empowered to establish a housing authority. The authority has broad powers to plan and effect housing within its jurisdiction, including the power of eminent domain, which may be exercised in the furtherance of its policy objectives.[22]

To assist in the repair, closing, and demolition of substandard housing, county courts may cooperate with other agencies to accomplish the goal of safe and sanitary housing.[23] And county courts are charged within their general grant of power to make and keep surveys of substandard and slum housing within their jurisdiction.[24]

Although there is no statewide building code, State regulation does affect the construction industry in two areas, the materials used in doors and panels around doors, and the regulations promulgated by the State fire marshal. Section 46–5–1 et seq., of the West Virginia Code regulates the types of glazed materials that may be used in and around doors. The purpose of the regulation is to minimize injury by allowing only materials that do not cut and pierce. Only materials that meet the test requirements of the American National Standards Institute Standard Z–97.1–1966 may be used in what the commissioner of the State department of labor determines to be a hazardous location in any residential, commercial, or public building. All such doors or panels that are installed must be labeled as meeting standards. A knowing violation of the statute is punishable as a misdemeanor.

The State fire marshal is charged with the responsibility of promulgating regulations necessary as a precaution against fire.[25] Among the areas within the ambit of the fire marshal's rule-making power are the installation of electrical wiring and the installation and maintenance of fire escapes on certain types of buildings.[26] Orders of the fire marshal pursuant to the rules and regulations are enforceable by injunction against violators or action brought by the appropriate prosecuting attorney.[27]

Environmental and Health Regulations

The State department of health is given broad powers to set standards for all drainage, water supply, excretia disposal, and refuse or garbage disposal insofar as public health is affected.[28] According to the State attorney general, this provision of State law is to be read expansively.[29] The State board of health, part of the State department of health, also regulates the chemical and bacteriological content of water systems serving more than 200 people.[30] Further, the State board of health is authorized to establish rules and regulations to control the

[18] Id., § 7–1–3n (1969).

[19] See *Lennox* v. *White*, 133 W. Va. 1, 54 S.E.2d 8, *Clifton* v. *Montague*, 40 W. Va. 207, 21 S.E. 858, W. Va. Code Ann, §16–18–1, et seq. (1972).

[20] W. Va. Code Ann, § 16–18–4 (1972).

[21] Id., §§ 16–18–5 (1972), 16–18–8 (1972).

[22] Id., §§ 16–15–1 (1972), 16–15–8 (1972).

[23] Id., § 16–16–4 (1972).

[24] Id., § 7–1–5 (1969).

[25] Id., § 29–3–4a (1971).

[26] Id., § 29–3–4a (1971).

[27] Id., §§ 29–3–4–(b)(c) (1971).

[28] Id., § 16–1–9 (1972).

[29] 50 Op. Att'y Gen. 342 (1963).

[30] Id., § 6–1–3 (1971).

design of public water systems, plumbing systems, sewage systems and excretia disposal methods, whether publicly or privately owned.[31]

The rules and regulations of the department of health and the State board of health are enforced by local health officers.[32] But the department of health is given the explicit right to preempt local enforcement if local officers neglect to enforce State regulation.[33]

To further a comprehensive health program, the department of health is permitted to receive Federal assistance subject to any accompanying restrictions and regulations.[34]

The State water resources board is responsible for the effectiveness of sewage and water disposal as they affect the quality of ground and surface waters.[35] The board has promulgated regulations to effectuate its policy goals. Sewage treatment processes that lead to such things as objectionable odor, color, floating solids, or foam, concentrations of materials poisonous to animals or man, and depleted oxygen content of water, are prohibited.[36]

Violation of the regulations is a misdemeanor punishable by fine from $100 to $1,000 or imprisonment of up to 6 months, or both. Wilful violation is a misdemeanor punishable by fine of $1,000 to $10,000 or imprisonment not exceeding 6 months or both. Each day of failure to comply creates a separate offense.[37]

Mobile Homes and Modular Housing

Although mobile homes are not specifically mentioned in the traffic safety statutes, it appears clear that the restrictions on the permissible dimensions of motor vehicles are applicable to mobile homes. The maximum height permitted is 12 feet 6 inches, unless specific exemption is obtained from the commissioner of highways.[38] The maximum length of any motor vehicle is 40 feet where the truck has three axles.[39] The greatest permissible width of any vehicle or load is 8 feet unless the load is excepted by the commissioner of highways.[40]

A great deal of discretion is vested in the State highway commissioner. He is empowered to permit oversized vehicles not in continous highway use to use the State highways. This discretionary power is crucial to the free movement of mobile homes within the State, since a large majority of mobile homes are wider than the 8 feet permitted by statute. But since special stickers are authorized to be issued to mobile homes on the highways in lieu of a motor vehicle license, it would appear that there is no significant impediment to highway movement imposed by size regulations.[41]

In the 1971 amendments to the motor vehicle statutes, a new provision was added affecting mobile homes. It is now clear that a pilot car is no longer required to follow mobile homes while they are transported on the highways.

Of course, mobile homes are subject to regulations through local building codes, but the effective application of local codes is highly problematic. Because the plumbing and electrical components are enclosed in the body of the mobile home, it is difficult to make adequate inspection of the mobile home at the point of completion. On the local level as well, county courts may require all mobile homes in a county for more than 30 days to obtain permits. The purpose of this authority is basically informational, and the cost of the permit is only $2.[42]

Finance

In the area of mortgage financing, there seem to be no particular restrictions on banks outside of the usury laws. The commissioner of banking has some discretionary regulatory power to order any bank to cease engaging in any unsound procedure detrimental to the bank and its depositors.[43]

Banks are expressly authorized to make loans secured by real property or leasehold if the loan is guaranteed or insured by the Federal Government or a Federal agency.[44] Banks are also permitted to take mortgages from the State housing development fund or related fund projects.[45]

Savings and loan associations may take mortgages under the conditions set forth in Section 31–6–21 of the West Virginia Code. The conditions: 1) A complete application must be made following guidelines specified in the statute, and the property must be appraised; 2) the loan is not to exceed 95 percent of the appraised valuation unless insured or guaranteed by the Federal Government; and 3) the transactions must be ap-

[31] Id., § 6–1–3 (1971).
[32] Id., § 16–2–1 (1972).
[33] Id., § 16–2–4 (1972).
[34] Id., § 16–1–15 (1972).
[35] Id., §§ 20–5A–3(b)(2) (1970), 20–5A–a (1970).
[36] West Va. Admin. Regs., State Water Resources Board § 3.
[37] Id., § 20–5A–19 (1970).
[38] Id., §§ 17C–17–11, 17C–17–4 (1966).
[39] Id., §§ 17C–17–11, 17C–17–4 (1966).
[40] Id., § 17C–17–3 (1966).
[41] Id., § 17A–7–2 (1966), 17A–17–3 (1966).
[42] Id., §§ 16–18–5 (1972), 16–18–8 (1972).
[43] Id., § 31A–2–4(14)(B) (1972).
[44] Id., § 31A–4–27 (1972).
[45] Id., § 37–18–12 (1966).

proved by the attorney retained by the association. Banks and building and loan associations may have freedom to adopt a flexible mortgage approach. Section 38–1–5 seems to be permissive of such an approach. The open-end concept in mortgage financing is not mentioned in the statutory or case law, but it appears that section 38–1–5 may also be permissive of this device.

The legal rate of interest in West Virginia is 6 percent, and the permissible rate of interest for agreements in writing is 8 percent per annum.[46] Loans payable in installments are limited to the permissible rate of 6 percent per *annum, but the* interest charge may be added on or deducted from the amount of the loan. Thus the effective rate of interest is somewhat higher than 6 percent.[47]

"Points" are included as interest under section 47–6–5, setting forth the maximum rate of interest in written agreements. There is no specific reference in the section dealing with installment loans. "Points" are defined as any charge received by the lender from any source in consideration of the loan and not otherwise permitted by statute.[48] The same section of the code authorizes only the simple amortization of points over the life of the loan.

Although no reference is made to "points" where installment loans are concerned, it should be observed that it is likely that such charges are included within the permissible 6 percent rate.[49]

Although "points" are included within the confines of the usury statutes, both case law and statutory authorization permit charges above the permissible rate of interest that are not includable in that interest rate. A lender is permitted to charge just and reasonable expenses for making the loan to the borrower, and the expenses are not considered interest.[50] The boundaries of this proposition are unclear from both the case and the statutory law. Banks are allowed to charge the borrower for the expenses of reports and information concerning the loan, and these charges are outside of the usury constraints.[51]

Building and loan associations may charge interest rates which are higher than those permitted by the usury statutes if the loan is made to one of its shareholders and the rate is fixed in the bylaws of the association.[52]

[46] Id., § 47–6–5 (1966).
[47] Id., § 47–6–5a (1966).
[48] Id., § 47–6–5 (1966).
[49] *James* v. *Felton*, 99 W. Va. 407, 415, 129 S.E. 482, 481 (1925).
[50] *Liskey* v. *Snyder*, 56 W. Va. 610, 49 S.E. 515 (1904).
[51] W. Va. Code Ann., § 31A–4–20 (1972).
[52] Ibid., § 3–6–17 (1971).

In the context of the installment loan, the applicable statute makes it mandatory that discounted or added-on interest be refunded at the contract rate of interest; thus the lender need not refund at the effective rate of interest, which —because of the discount or add-on characteristic—may be greater than 6 percent.[53]

Veterans' Administration and Federal Housing Administration-insured loans are specifically exempted from the usury laws under section 31A–4–29 of the West Virginia code.

There are regulations encompassing the area of secondary mortgages. These regulations are not applicable to banks, building and loan associations, or where Federal agencies are involved as the lender or guarantor of a loan.[54] The restrictions imposed on other lenders are, after licensing, that the lender may not extend a loan beyond 60 months at 6 percent interest, with total charges not to exceed 10 percent. Late payment charges of up to 5 percent are not included in the 10 percent figure. Hazard insurance may also be required and is not considered within the 10 percent limitation.[55]

Housing Authorities and Housing Law

In West Virginia, the local units of government are authorized to establish five-member housing authorities.[56] The purpose of these county and municipal housing authorities is to establish low cost housing and engage in slum clearance projects, in the interest of promoting public health and welfare.[57] The housing authorities are empowered to make investigations and studies of existing conditions and the present and future needs for low cost housing as well as the power to purchase, sell, lease, and rent in connection with the goal of providing needed low cost housing.[58] Included among the powers granted to the housing authority is the power of eminent domain, to be exercised in conjunction with slum clearance or the construction of new low cost housing.[59] If interjurisdictional cooperation is required to accomplish the goal of the State housing law, housing authorities are permitted to cooperate with other authorities for the purpose of planning, financing, constructing, or operating housing projects.[60] The local authori-

[53] Ibid., § 47–6–5a (1966).
[54] Ibid., § 31–17–2 (1972).
[55] Ibid., § 31–17–8 (1972).
[56] Ibid., § 16–15–3 (1972).
[57] Ibid., § 16–15–2 (1972).
[58] Ibid., § 16–15–7 (1972).
[59] Ibid., § 16–15–8 (1972).
[60] Ibid., § 16–15–7b (1972).

ties, in the furtherance of their goal, are empowered to incur any indebtedness, issue any obligation, or give any security to finance low cost housing. Statutory limitations on municipal financing are specifically designated as inapplicable to housing authorities.[61]

All authorities are charged with the responsibility of fixing rents at rates that will meet the demands of the underlying financing incurred in the construction of the housing project.[62] Further, authorities are restricted from accepting persons into any housing project whose aggregate income is greater than 5 times the annual rent unless the person has three or more minor dependents.[63]

Housing authorities are exempted from all other otherwise applicable State and local taxation but are subject to all other local regulation.[64]

An added feature of the State housing law is that an individual owner of farms may apply for low cost housing for those of low income who operate or maintain his farm. (The owner would seem to fall within this group.) To achieve this purpose, the county authority is empowered to borrow or otherwise finance the rental or purchase of the appropriate housing.[65]

The Housing Development Act provides for the establishment of a State housing fund, which is to finance and provide assistance to public and private builders constructing residences for low and moderate income people.[66] The fund has a broad range of powers, including the power to buy and sell real property in conjunction with its power to provide appropriate financing. The fund may borrow money and enter into mortgage agreements that are modifiable consonent with the goal of providing low cost housing. The fund and the property that it owns is exempt from all State and local taxes.[67]

Taxes, Welfare Liens, and Insurance Regulation

There is no authority for the practice of maintaining existing levels of real property assessment following the improvement of substandard housing. In fact, it is expressly provided that all property is to be assessed at its true or actual value. Actual value is defined as the fair market value on the open market.[68]

The tax foreclosure procedure is a relatively long and complex process. Ad valorem property taxes are collectible in two installments payable September 1, or the following March 1.[69] Taxes due on these dates are delinquent on October 1 and the following April 1.[70] The compilation and recording of the first delinquent tax list take place on July 1 of the year of assessment.[71]

Among the remedies available to the sheriff whose duty it is to enforce delinquent taxes is the power to sell the land on which the taxes are due.[72] After a second publication of the list of taxes which are still delinquent as of September 1, the property involved may be sold, at the earliest, on October 14 following the year of assessment. The minimum price for which the land may be sold is the amount of delinquent taxes plus the cost of publication. The owner of the property sold in the tax sale may redeem that property by March 31 of the second year following the tax sale at a price not less than the amount of the tax sale purchase price plus 12 percent per annum and all additional taxes and expenses incurred while the property remains unredeemed.[73]

Welfare liens no longer exist in West Virginia, and all prior liens have been released by statute.[74]

As a part of its insurance law and regulation, the State of West Virginia does not require insurance companies to write fire insurance policies on substandard housing.

Comparative Analyses of the Seven Southeastern States

Statewide Housing Corporations

Kentucky is one of the three States studied that has established a statewide housing corporation. The legislation seems sound and might well serve as a model for other States.

In 1972, the Kentucky legislature created the Kentucky Housing Corporation, codified in § 198A of the Kentucky Revised Statutes. The purpose is to create safe and sanitary housing, in rural and urban areas, that have deteriorated in recent years through the spread of slum conditions.

[61] Ibid., § 16–15–10; but see §§ 16–15–19, 16–15–20, 16–15–21 concerning bonds.
[62] Ibid., § 16–15–18 (1972).
[63] Ibid., § 16–15–19 (1972).
[64] Ibid., §§ 16–15–14, 16–15–9 (1972).
[65] Ibid., §§ 16–15–24, 16–15–25 (1972).
[66] Ibid., § 31–18–1 et seq. (1972).
[67] Ibid., § 31–18–18 (1972).

[68] Ibid., § 11–3–1 (1966).
[69] Ibid., § 11A–1–3 (1966).
[70] Ibid., § 11A–1–3 (1966).
[71] Ibid., § 11A–2–14 (1966).
[72] Ibid., § 11A–2–10 (1966).
[73] Ibid., § 11A–3–17 (1966).
[74] Ibid., § 9–5–26 (1969).

The corporation is governed by a board of directors and has the necessary powers to effectuate the legislation. Among the powers are: To make insured construction and mortgage loans to sponsors of land developments or residential housing; to purchase insured mortgage loans made to such sponsors; to acquire real property by purchase, foreclosure, or otherwise; to sell all or any part of a mortgage or any document securing a construction, land development, or loan; to insure against loss; to consent to a modification of the usury rates; and to acquire, establish, and operate residential housing for persons of low income.

The housing corporation does more than finance the construction of low cost housing. § 198A.050 authorizes the director of the corporation to provide that training and employment arising in connection with the planning, construction, rehabilitation, and operation of housing assisted under such programs be given to persons of low income residing in the area of such housing, wherever feasible. It provides further that contracts for work be awarded to individuals and business firms doing business in the fields of design, architecture, building construction, rehabilitation, maintenance, and repair located in, or owned in substantial part by persons residing in the area of such housing. Thus the act encourages active participation by those it is created to help, by providing employment and stimulating business.

Kentucky is not responsible in any way for any debts, liabilities or obligations issued under the act.[1] These are payable solely from the revenues or assets of the corporation.

The act also created a housing loan fund, known as the Housing Development Fund, to be administered by the corporation as a trust fund separate and distinct from any other moneys or funds administered by the corporation. It is comprised of funds and contributions and of fund notes issued by the corporation.[2] The purpose of the fund is to provide a source from which the corporation may make temporary loans at such interest rates as may be determined by the corporation for the purposes of: Defraying development costs of sponsors, developers, and builders of residential housing; or providing, to low income families applying for mortgages, funds to make downpayments and pay closing costs; or participating in construction loans which are not federally insured to sponsors, builders, and developers. Construction loans, however, will only be made from the fund when such loans are not otherwise available from private lenders upon reasonably equivalent terms.

The corporation is authorized to issue $200 million in bonds to carry out its purposes, and may issue bond anticipation notes, interim receipts, or temporary bonds.[3]

In the discretion of the corporation, any obligations it undertakes may be secured by a trust agreement by and between the corporation and a corporate trustee, which may be any trust company or bank and trust company within or outside the State.[4]

The West Virginia legislature recently passed a Housing Development Act establishing a development fund to finance and provide assistance to public and private builders constructing residences for low and moderate income families.[5] The fund is a tax-exempt public body corporation, run by a board of directors. The fund is empowered to buy and sell real property, borrow money, and enter into mortgage agreements to achieve its ends.

Virginia has established a Housing Development Authority, which is a State political subdivision, to provide safe and sanitary housing for people of low income.[6] The authority may make mortgage loans and those necessary for housing rehabilitation for housing sponsors.[7] It can also make first mortgage loans to low and moderate income families.[8] The authority is also empowered to supervise housing sponsors through the setting of rental rates, tenant selection, and supervision of the operation and maintenance of the developments.[9]

Housing Authorities

The seven States have nearly uniform provisions regarding housing authorities.[10] No State has a statewide housing authority, but all have provisions enabling the establishment of county and regional authorities. Most require a finding of unsafe and unsanitary conditions before any

[1] Kentucky Revised Statutes, § 198A.070 (1972 Supp.).
[2] Id., § 198A.080.

[3] Id., § 198A.090.
[4] Id., § 198A.100.
[5] West Virginia Code, § 31–18–1 et seq. (1972).
[6] Code of Virgina, § 36–55.27 (1973 Supp.).
[7] Id., § 36–55.3.
[8] Id., § 36–55.34.
[9] Id., § 36–55.33
[10] Code of Alabama, Title 25, §§ 33 et seq. (1960); Arkansas Statutes Annotated, §§ 19–3001 et seq. (1968); Kentucky Revised Statutes, 80.000 et seq. (1969); Mississippi Code Annotated, §§ 43–33–1 et seq. (1972); Tennessee Code Annotated, §§ 13–804 et seq. (1955); Code of Virginia, §§ 36–1 et seq. (1970); West Virginia Code, §§ 16–15–1 et seq. (1972).

authority may be set up. All provide that two or more counties with similar housing problems may combine to create a regional authority with the same powers as the county authority, which then ceases to exist.

The powers granted to county and regional authorities are wide. All are empowered to build, operate, maintain, and lease housing projects, acquire real property, issue bonds, borrow money, contract with the Federal Government, insure their property, and perform other functions necessary for the construction and operation of housing projects.

Certain regulations are placed on all the authorities. All their projects are to comply with local building codes, zoning, sanitary, and safety ordinances. The operations are to be nonprofit, so the States require special procedures for determining rental rates and tenant selection. The projects are to be operated so that the lowest rental possible, consistent with safe and sanitary housing, will be charged. Tenants are to be people with incomes so low that they are otherwise unable to procure sanitary housing. No absolute schedules for rates are listed, nor are maximum incomes for tenants (except that some States limit net aggregate income of a renting group to 5 times the rental rate). The States provide flexible guidelines so that individual counties or areas may meet their own needs.

All seven States have included special provisions for low income rural landowners.[11] The statutes were enacted in 1941 or 1942, and they appear to come from a common model. The language is identical in all except Alabama and Kentucky, and the intent in these is identical.

An owner of a farm operated or worked upon by farmers of low income in need of safe and sanitary housing may file an application requesting the housing authority to provide a dwelling or dwellings for occupancy by such persons. In all States, the authorities are empowered to use their funds to build such housing upon determination of real need. The housing may be either leased or sold to the farmer. It remains the tax-exempt property of the authority until full payment is made, except that the landowner may usually claim homestead exemption for it.

[11] Code of Alabama, Title 25, § 55 (1960); Arkansas Statutes Annotated, § 19-3054 (1968); Kentucky Revised Statutes, 80.510 (1969): Mississippi Code Annotated, § 43-33-121 (1972); Tennessee Code Annotated, § 13-1010 (1955); Code of Virginia, § 36-38 (1970); West Virginia Code, § 16-15-25 (1972).

Building Code

Virginia is the only State with *provisions for* the implementation of a statewide building code. The Uniform Statewide Building Code[12] empowers the State Board of Housing to adopt and promulgate a uniform building code for the entire State.

The building code is to prescribe standards to be complied with in the construction of buildings, with due regard to the health, safety, and welfare of the residents of the State. The board should consult the standards set forth by nationally recognized organizations, such as the Southern Building Code Congress, the Building Officials Conference of America, and the National Fire Protection Association, when making the code. Also, the provisions of the code are to be stated in terms of a required level of performance, whenever practical.[13]

Before any code provisions are adopted, the State board is required to hold at least one public hearing giving persons an opportunity to present their views. Notice of the hearing is to be published in at least four newspapers of general circulation in the State.[14]

No code provisions may be made effective prior to January 1, 1973, or later than September 1, 1973.[15] Enforcement of the code is the responsibility of the local building department.[16] Any violation of the code is deemed a misdemeanor and the person, firm, or corporation convicted of such violation will be punished not more than $500.[17]

Alabama has passed an enabling statute for a statewide building code, but none has been promulgated.[18] Kentucky, Arkansas, and Mississippi give local authorities power to adopt a building code,[19] and West Virginia counties may adopt one also if the county has a population greater than 200,000.[20]

Finally, West Virginia does have a progressive element in its statutes in the building code

[12] Code of Virginia, §§ 36-97 to 36-119 (1970).
[13] Id., § 36-99.
[14] Id., § 36-100.
[15] Id., § 36-101.
[16] Id., § 36-105.
[17] Id., § 36-106.
[18] Code of Alabama, Tit. 55, § 367(1),(7)—(9) 1960). The code would be primarily applicable to State buildings and construction; municipalities and counties could adopt and apply it to all buildings within their jurisdiction.
[19] Kentucky Revised Statutes, §§ 67.380 (counties) & 82.080 municipalities) (1969); Ark. Stat. Ann., §§ 19-2801 et seq. (1968) (municipalities); Miss. Code Ann., §§ 19-5-9 (counties) & 21-19-25 (municipalities) (1972).
[20] West Virginia Code, § 7-1-3n (1969). Tennessee has a similar provision. Tenn. Code Ann., §53-2549 (1972 Supp.)

area. Under West Virginia law, glazed materials used around doors must meet the standards promulgated by American National Standards Institute Standard Z–97.1–1966.[21] Also, where component housing is HUD-approved in West Virginia, county building codes are preempted.[22]

It is interesting to note that Mississippi has a provision to the effect that county governments may not adopt standards exceeding those building regulations of construction codes published by nationally recognized code groups.[23]

Land Use Controls

The seven States utilize various means of land use control. Generally, the laws provide for some form of planning commission and for zoning regulations. Land use control power is usually delegated to the local governments, with the State often serving in an advisory capacity. Because of the various structures in the States, I will treat each State separately, giving a general view of their land use controls and commenting on any unique or interesting feature.

Kentucky follows the general pattern of land use controls. The main area of emphasis is local control. Before land use planning may begin, a "planning unit" must be formed or designated. Such unit may be a joint planning unit composed of a county and the municipalities within it,[24] or a city or county separately if they fail to form a joint unit,[25] or two or more planning units may form a regional planning unit.[26]

To exercise its planning powers, a planning unit must appoint a planning commission.[27] The planning commission is required to prepare a comprehensive plan of the region including a land use plan to guide the development of the unit.[28] It is not clear what legal effect the comprehensive plan has.

Zoning, perhaps the principal method of land use control, is left to local government. Cities and counties which are members of a planning unit may create zones and issue zoning ordinances as to certain specified features.[29] An important feature of Kentucky's zoning law is that land used for farming is exempt from many of the zoning restrictions.[30]

Kentucky also provides for area planning commissions. Two or more adjacent counties, one of which has a city of more than 50,000 and less than 200,000, may form such an area planning commission.[31] The area commissions within their territory exercise powers similar to those exercised by the other planning units.

Statewide land use control is exercised by the Kentucky Progress Commission[32] and the Governor's cabinet.[33] Both bodies have principally a study, advisory, and a planning function.

Mississippi has a less developed system of land use control, but it utilizes the same two tools: Zoning ordinances and planning commissions. The State has delegated its land use powers to the local governments. Municipalities and counties for the unincorporated portions of the county may exercise the power to issue zoning ordinances pertaining to various specified factors. Land and buildings used for agriculture, however, are exempt from county regulation.[34] To facilitate the exercise of their zoning powers, local governments may act jointly to attain uniformity and conformity in zoning regulations in the area.[35]

The local governments may also regulate the development of subdivisions. They may make dedication of such subdivisions conditional upon such terms as the local government shall feel necessary to implement their zoning and planning powers.[36]

To aid in the development of local land use and to create and implement an official plan, counties and municipalities may create local planning commissions.[37] In order to aid development on a broader scale, two or more counties and municipalities may form regional planning commissions. Local governments are also empowered to participate in interstate planning commissions.[38]

Tennessee has a State planning commission, but it serves primarily in an advisory capacity.[39] Its most important function is the creation of planning regions and planning commissions.[40] These regional planning commissions also serve primarily in an advisory capacity.[41] These commissions are to adopt a plan for the general re-

[21] Id., § 47–5–1 (1972 Supp.)
[22] Id., § 8–24–50a.
[23] Miss. Code Ann., § 2890.7 (1972 Supp.).
[24] K.R.S., § 100.121 (1969).
[25] K.R.S., § 100.117 (1969).
[26] Ibid., § 100.123 (1969).
[27] Ibid., § 100.133(1) (1969).
[28] Ibid., § 100.183 and § 100.187 (1969).
[29] Ibid., § 100.201 and § 100.203 (1969).
[30] Ibid., § 100.203(4) (1969).
[31] Ibid., § 147.010 (1969).
[32] Ibid., § 147.010 (1969).
[33] Ibid., § 147.070 (1969).
[34] Miss. Code Ann., § 17-1-3 (1972).
[35] Ibid., § 17-1-5 (1972).
[36] Ibid., § 17-1-23 (1972).
[37] Ibid., 17-1-11 (1972).
[38] Ibid., § 17-1-29 (1972).
[39] Tenn. Code Ann., § 13-108 (1955).
[40] Ibid., 13-107 (1955).
[41] Ibid., § 13-108 (1955).

gion for physical development of the region. The commission's major authoritative action is that once a plan has been created for a county, a plat for subdivision may not be recorded by the county unless it is first approved by the regional commission.[42]

The counties, while having no planning function per se, do have the power to enact zoning ordinances.[43] Where a regional planning commission has been established, the ordinances must be submitted to that commission, but they may be enacted by the counties over their disapproval.[44] Under § 13–414, buildings and lands used for agricultural purposes are generally exempted from regulation.

The municipalities exercise both a planning and a zoning function. Under §13–501, the chief legislative bodies of the municipalities are authorized to create municipal planning commissions. The commission is authorized to make a plan for the physical development of the municipality, including a zoning plan. Once a plan is adopted, no street or other public way, public building, or public utility may be constructed without first submitting it to the planning commission for approval.[45] The municipal planning commission has the same power in regard to subdivision platting as the regional planning commission.[46] The municipalities have the power to enact zoning ordinances upon the recommendation of the planning commission.[47]

Arkansas does not have a highly developed land use control system. On the State level there is the State planning commission.[48] Its main functions are the development of an ongoing State plan and coordinating and furnishing advice to local officials.[49] Another State mechanism is the creation of regional multicounty planning and development organizations. The State planning commission advises them but has no authority to set standards as guidelines for them.[50]

First- and second-class cities have the power to establish zoning ordinances. However, they may classify land use in only three ways: Manufacturing use, business other than manufacturing, and residential only.[51] First- and second-class cities and incorporated towns are given additional power if they establish a municipal planning commission.[52] The commission's two main functions are to control and administer the development and subdivision of land and to recommend zoning ordinances.[53] A city creating a planning commission may adopt far more comprehensive zoning ordinances.

The counties may appoint county planning boards.[54] Among the powers and duties of the board are the development of an official county plan and the creation of land use zones.[55] Under § 17-1106, the county planning board has the same power over subdivision of unincorporated land as a municipality has within incorporated land.

Arkansas permits cities, towns, and counties to create joint or metropolitan planning commissions.[56] They exercise basically a coordinating function, since the power to zone and plan remains in the participating local governments.[57]

In West Virginia, control of land use is generally in the hands of local government. Counties and municipalities may create local planning commissions.[58] The planning commissions are to create comprehensive plans of land development.[59] After a plan has been accepted by the local government, a plan for subdivision may not be recorded unless it is approved by the planning commission.[60]

Both counties and cities may adopt zoning ordinances,[61] subject to certain qualifications specified in § 8–24–40. Such zoning regulations are to be proposed by the planning commission.[62]

In 1971, the statutes providing for regional cooperation were revised. Now the State has provided for statewide cooperation.[63] The Governor is given broad powers to coordinate State and local development. This development includes more than just land use control. The Governor is required to create regional boundaries throughout the State and to provide for the formation of regional councils. These regional

[42] Ibid., § 13-302 (1955).
[43] Ibid., § 13-401 (1955).
[44] Ibid., § 13-507 (1955).
[45] Ibid., § 13-507 (1955).
[46] Ibid., § 13-602 (1955).
[47] Ibid., § 13-701 and § 702 (1955).
[48] Ark. Stat. Ann., § 9–306 (1971 Supp.).
[49] Ibid., § 9-316 to § 9-318 (1971 Supp.).
[50] Ibid., § 9-324 to § 9-328 (1971 Supp.).
[51] Ibid., & 19-2805 (1968).
[52] Ibid., § 19-2825 (1971 Supp.).
[53] Ibid., § 19-2828 and § 19-2829 (1971 Supp.).
[54] Ibid., § 17-1101 (1968).
[55] Ibid., § 17-1103 (1968).
[56] Ibid., & 19-2820 (1968).
[57] Ibid., § 19-2824 (1968).
[58] W. Va. Code Ann., 8-24-1 (1969).
[59] Ibid., § 8-24-16 (1969).
[60] Ibid., § 8-24-28 and § 8-24-31 (1969).
[61] Ibid., § 8-24-39 (1969).
[62] Ibid., § 8-24-42 (1969).
[63] Ibid., § 8-25-1 to 8-25-15 (1972 Supp.).

councils are to provide planning and technical assistance for the development of the region.

Local governments are also empowered to cooperate with local governments in other States regarding the development of regions.[64]

Alabama has both State and local land use controls. There is the Alabama State Planning Board.[65] The board is entrusted with the duty of developing a master plan for the development of the State.[66] It may also propose to the legislature legislation including zoning and land use regulations to carry out the master plan.[67]

Local regulation is entrusted to municipalities and regional planning commissions, but almost no provisions are made for county control. Perhaps Alabama considers land use planning as primarily an urban problem.

Municipal corporations have the power to zone according to land use in regard to business, industrial, and residential use.[68] The cities are given additional powers to provide more comprehensive zoning according to a comprehensive plan.[69] There is no provision for zoning by the counties.

Municipalities also have the power to create planning commissions.[70] Under § 791, the primary duty of the commission is to make and adopt a master plan for the physical development of the area, including areas outside the municipality that affect the planning for the municipality. Once a plan has been adopted, no improvement may be made in the area without first submitting it to the commission for approval.[71] Where a municipality has created a commission, the commission has all the powers formerly held by the zoning commission,[72] and also has the power to regulate subdivision development within the municipality and 5 miles beyond.[73]

Alabama has had several different programs dealing with regional planning commissions. The original one[74] provided that the planning commission of any municipality or the county commissioners of any county could petition for the creation of a regional planning commission. The legislation was clearly aimed at areas of urban spillover that made municipal planning difficult. The commission's primary purpose was the development of a master plan of the region. The second attempt at regional planning called for the creation of advisory regional planning commissions.[75] These commissions served primarily an advisory planning and research role. They had no specific control over zoning on land use. The latest program for regional development was enacted in 1969.[76] It provides for the creation of regional planning and development commissions. These commissions have a far broader grant of power than do the commissions created by the first two plans. The earlier commissions were to cease to exist 2 years after this plan was enacted.

As can be seen, most of Alabama's land use legislation is aimed at urban area and areas of urban spillover. One area where counties have substantial power to regulate land use is in flood-prone areas.[77] Flood-prone areas are those with a frequency of inundation of once every 100 years. Where this happens, the county has the full range of land use control devices available, including planning, zoning, and subdivision control.

Virginia uses three techniques of land use control: Planning commissions, subdivision ordinances, and zoning ordinances. Control is entirely by local government.

Under § 15.1–427, any county or city may create a local planning commission. There is no provision for a regional commission. The local commission serves primarily in an advisory capacity. Its chief function is the development of a comprehensive plan for the physical development of the territory, including a land use plan.[78] After the plan has been adopted, it controls the general location of every feature on the plan.

Local county and city governments are also empowered to adopt subdivision and development ordinances.[79] When the local government has created a planning commission, the subdivision ordinances are to be prepared and recommended by the commission.[80] After the plan has been adopted, before anyone may subdivide his land he must first submit a plan of the proposed subdivision to the commission.[81]

The local governments also have zoning power.[82] The local government may divide up

[64] Ibid., § 8-26-1 to 8-26-5 (1969).
[65] Code of Ala., Tit. 55, § 373(1) (1960).
[66] Ibid., Tit. 55, § 373(4) (1960).
[67] Ibid., Tit. 55 § 373(5) (1960).
[68] Ibid., Tit. 37, § 772 (1960).
[69] Ibid., Tit. 37 § 774-785 (1960).
[70] Ibid., Tit. 37, § 786 (1960).
[71] Ibid., Tit. 37, § 794 (1960).
[72] Ibid., Tit. 37, § 796 (1960).
[73] Ibid., Tit. 37, § 797-803 (1960).
[74] Code of Ala., Tit. 37, § 809-814 (1960).
[75] Ibid., Tit. 37, § 814(1)-814(4) (1971 Supp.).
[76] Ibid., Tit. 37, § 814(4)-814(14) (1971 Supp.).
[77] Ibid., Tit. 12, § 341-364 (1971 Supp.).
[78] Code of Va., § 15.1-446 (1973).
[79] Ibid., § 15.1-465 (1973).
[80] Ibid., § 15.1-470 (1973).
[81] Ibid., § 15.1-475 (1973).
[82] Ibid., § 15.1-486 (1973).

the land into districts, and regulations must be uniform within a district. Where the planning commission exists, it is to recommend regulations and boundaries. When no planning commission exists, a local government may only exercise its zoning power by creating a zoning commission.[83]

Virginia's system of comprehensive enabling acts for local government, has both its advantages and disadvantages. Because it is left purely to local option, there is no State law assuring at least minimum control where local governments through inertia or shortsightedness have not sought to assure the orderly development of their land. But where a local government does act, the statutes provide a comprehensive array of tools.

Mobile Homes

Uniform Standards: Virginia is the only State which has a statewide building code for mobile homes and modular housing.[84] This statute was passed in 1972 and was based primarily on the North Carolina Uniform Standards Code for Mobile Homes Act of 1971.[85]

The Virginia Industrialized Building Unit and Mobile Home Safety Law requires that every mobile home and modular house sold in Virginia, as defined in § 36–71, be inspected by an "approved testing facility" and obtain a seal of approval.[86] An "approved testing facility" is an architect or professional engineer, registered in Virginia, or a testing organization, determined by the State Corporation Commission to be specially qualified to investigate and test modular housing and mobile homes and to provide followup services at the point of manufacture to assure that production units are in full compliance with the State regulations.[87]

Whether a mobile home or modular housing unit receives a seal of approval from the testing facility will depend on whether it meets the rules, regulations, and qualifications promulgated by the State Corporation Commission. The commission will adopt rules and regulations having due regard for generally accepted safety standards as recommended by such nationally recognized organizations as the American National Standards Institute Standard A 119/1 and the National Fire Protection Association #501B as they are applied to mobile homes. The commission will also consider the standards of the Southern Building Codes Congress, the Building Officials Conference of America, the International Conference of Building Officials, and the National Bureau of Standards applying to industrialized building units.[88]

It is noteworthy that the Virginia statute requires that, where practical, the rules and regulations shall be stated in terms of required levels of performance, so as to facilitate the prompt acceptance of new building materials and methods.[89]

All industrialized building units or mobile homes bearing a seal of approval are acceptable in all localities of the State as meeting the requirements of the Virginia Industralized Building Unit and Mobile Home Safety Law, and are exempt from internal inspection by local governing bodies of Virginia provided they are erected properly. Any such structure not containing a seal of approval is subject to full inspection by local officials.[90] Any unit constructed before June 26, 1971, is subject to the ordinances, laws, and regulations in effect at the time such unit was constructed, but additional necessary requirements may be enacted.[91]

The commission has the right to enter into any building unit or mobile home, not occupied as a dwelling unit at the time, upon the complaint of any person having an interest in any such unit or upon request of local officials having jurisdiction, for examination as to compliance with the rules and regulations of the commission. If the officer finds a violation of the rules of the commission, the manufacturer will be ordered to bring the unit into compliance with such rules.[92]

Anyone violating the provisions of the Virginia Industrialized Building Unit and Mobile Home Safety Law will be found guilty of a misdemeanor and fined not more than $500.[93]

The Virginia statute takes a long step towards providing a uniform system of safe mobile homes and modular housing units. One provision of the North Carolina statute which was not adopted by Virginia, and which would provide for even greater assurance that the regulations were being followed, is that which declares it unlawful

[83] Ibid., § 15.1-487 (1973).
[84] Code of Virginia, §§36-70 to 36-85 (1970).
[85] G.S.N.C., §§ 143–144 to 143–151.1 (1971 Supp.).
[86] Code of Virginia § 36-71(5), § 36-79 (1970).
[87] Id. § 36-71(5).
[88] Id. § 36-73.
[89] Id.
[90] Id. § 36-81.
[91] Id. § 36-78.
[92] Id. § 36-82.
[93] Id. § 36-83.

to turn on and furnish electricity to units without the appropriate certificate or label.[94] This provision would make it even more difficult for units not built in conformance with the State building codes to function properly, by making it a misdemeanor for a supplier of electrical current to furnish electricity to such structures.

The only other States which have any national standards for the building of mobile homes are Alabama and Mississippi.[95] Alabama has adopted the American National Standards Institute Code for minimum standards of plumbing, heat production, and electrical systems.[96] Factory-built housing must be approved by the Alabama Development Office or by the local government at the place of manufacture to see that it meets local building requirements in conformity with the Southern Building Codes Congress, the National Fire Protection Association, and HUD.[97] Approval will be given to housing from out of State which had to comply with standards reasonably consistent with those of Alabama.[98]

Miscellaneous: In Tennessee, no certificate of title need be obtained for any vehicle of a type subject to registration if it is owned by the Government of the United States.[99] In all the other States, federally owned mobile homes are subject to the registration provisions, carried out through the local governments (except in Virginia, which has a desirable statewide uniform standard). Each State also has certain limitations on the size of mobile homes that can be transported on State highways. These dimensions are approximately 8 feet in width, 13 feet in height, and 55 feet in length. However, larger units can be transported with special permission from the State highway commission.[100]

Mobile Home Taxation

Sales Tax: Most of the States studied have a sales tax that is applicable to the sale of mobile homes, at a rate ranging from 3 to 5 percent, either explicitly—Alabama[101] and Arkansas[102]—or implicitly by virtue of the fact that mobile homes are considered personal property—Kentucky[103] and Tennessee.[104] Mississippi would also seem to consider them subject to the sales tax.[105] While Virginia excludes mobile homes from the application of the regular 3 percent sales and use tax,[106] they are subject to the Virginia motor vehicles sales and use tax of 2 percent.[107] As to West Virginia, the State Tax Department has informed us that all mobile homes and modular units are subject to the State sales tax as they leave the factory.

A number of States involved also have use taxes that appear applicable to mobile homes: Arkansas,[108] Kentucky,[109] Mississippi,[110] and Virginia.[111] Tennessee has a limited use tax applicable only to tangible personal property imported from other States.[112]

Mobile Homes as Personal Property: Most of the State statutes appear to treat mobile homes as personal property, either generally—Alabama,[113] Arkansas,[114] and Virginia[115]—or at least when the wheels have been removed—Kentucky[116] and Tennessee.[117] West Virginia and Mississippi take a different approach. In the former, when the mobile home is owner-occupied and the owner also owns the land on which it rests, the mobile home is classified as real estate (whether or not the wheels have been removed). However, if the mobile home is

[94] Gen. Stat. N.C., § 143-150 (1971 Supp.).
[95] Uniform Standards Code for Factory Manufactured Movable Homes Act., Miss. Code Ann. §§ 5131-101 et seq. (1972 Supp.).
[96] Code of Alabama, Title 25, § 126 (1971 Supp.).
[97] Id. § 116(a)(2) and (3).
[98] Id. § 118.
[99] Tenn. Code Ann. § 59-301 (1972 Supp.).
[100] E.g., W. Va. Code §§ 17C-17-3 to 17C-17-11 (1966).
[101] Code of Alabama, Title 51, §§ 786(3)(d), 786(25) (Supp. 1971).
[102] Ark. Stat. Ann. § 84-1903(e) (1960).
[103] See note 16 infra. Furthermore, Kentucky Revised Statutes § 139.160 (1972) [hereinafter cited as KRS] defines "tangible personal property" subject to the sales tax as "personal property which may be seen, weighed, measured, felt or touched, or which is in any other manner perceptible to the senses. . . ."
[104] See note 17, infra.
[105] See note 19, infra. If the owner of a mobile home does not own the land on which it rests, the mobile home is treated as personal property.
[106] Code of Virginia § 58-441.6(e) (1970).
[107] Id. at § 58-685.11(3). Any transfer of any mobile housing whenever permanently attached to the real estate and included in the sale of real estate is not a sale of a motor vehicle subject to the Motor Vehicles Sales Tax, § 58-685.11(5).
[108] Ark. Stat. Ann. § 84-3101 (1960).
[109] KRS § 139.310 (1972).
[110] Miss. Code Ann. § 27-67-3(j) (1972).
[111] Code of Virginia § 58-685.11(13) (1970).
[112] Tenn. Code Ann. § 67-3005 (Supp. 1972) [hereinafter cited as TCA].
[113] Code of Alabama, Title 51, § 704(2) (Supp. 1971).
[114] Bartke, Gage, *Mobile Homes: Zoning and Taxation*, 55 *Corn. L. Rev.* 491, 521 (1970); Note, *Taxation—Property Tax on House Trailers—Real Property*, 8 *Ark. L. Rev.* 188 (1954). This conclusion is reached from the general framework of mobile home regulation, and particularly a 1965 amendment to the taxation code which strongly suggests it. See Ark. Stat. Ann. § 84-1934 (Supp. 1971).
[115] See notes 6 & 7, supra.
[116] KRS § 139.200 (1969). If the wheels or mobile parts have been removed from a house trailer or mobile home, and the unit rests on a fixed permanent foundation, it is classified as real estate. Id. at § 132.750. However, house trailers generally are termed as personal property.
[117] TCA § 67-612 (1955). Enumerating wheeled vehicles as a type of personal property apart from automobiles lends itself to the conclusion that mobile homes, at least with wheels, are considered personal property.

owner-occupied and its owner does not own the land on which it rests, the home is considered personal property.[118] Mississippi follows a similar approach, except that the mobile home owner who owns the land has a choice of treating his mobile home as either personal or real property.[119]

Treatment of Modular Housing: Modular housing is not mentioned in the tax statutes of any of the seven States.

Maintaining Existing Levels of Assessment

None of the States apparently allows the maintenance of existing levels of assessment after improvements, all using some form of the "fair market value" approach which, by implication, bars it: Alabama,[120] Arkansas,[121] Kentucky,[122] Mississippi,[123] Tennessee,[124] Virginia,[125] and West Virginia.[126]

Welfare Lien Laws

The only State that has a general welfare lien law is Kentucky. First-class cities that have paid general assistance to any person through the department of public welfare of that city have a claim against the estate of any such deceased person.[127] The claim has priority over all unsecured claims against such estate except the burial expenses of the decedent, the cost of administration of his estate, the cost of his last illness, and claims by the Commonwealth of Kentucky for assistance rendered by it to the decedent. The lien will be enforceable against all real estate and rights to real estate belonging to or thereafter acquired by any recipient of general assistance through the city's department of public welfare, and will continue until it is satisfied. The lien is not effectual against any mortgagee, purchaser, or judgment creditor without actual notice until notice has been filed by the director of public welfare in the office of the clerk of the county court of the county in which the property is located.[128]

The West Virginia and Virginia statutes specifically state that there are no liens on the property of those receiving welfare assistance.[129] There are no welfare lien laws in Arkansas, Alabama, or Tennessee.

Repair, Closing & Demolition of Unfit Structures

Most of the States have statutes that contain rather broad provisions giving power to local authorities to repair and clear away substandard housing in slum areas. Kentucky and Tennessee have the most extensive legislation.

Kentucky and Tennessee have virtually identical legislation authorizing city and county governing officials to adopt ordinances relating to structures in their jurisdiction that are unfit for human habitation. After a petition is filed with the appropriate public officer by a public authority or by at least five residents of the city or county, the public officer will issue a complaint to be served on the owner of the structure. The complaint notifies the owner that a hearing will take place based on the charges that the structure is unfit for human habitation. Following the hearing, the public officer will state his findings of fact and will issue an order requiring the owner to repair, improve, or alter the structure to make it fit for human habitation; to vacate and close the structure if the repair of the structure can be made at a cost that is less than 50 percent of the value thereof in Kentucky (or is a "reasonable cost" in Tennessee); or to remove or demolish the structure if the repair, alteration, or improvement of it cannot be made at a cost less than 50 percent of the value of the structure (or at a "reasonable cost" in Tennessee). If the owner refuses to comply with the order, the public officer may cause the structure to be repaired, altered, vacated, closed, or demolished, and the cost of such improvements will be a lien upon the real property upon which cost was incurred. If the structure is removed or demolished, the public officer will sell the materials of the structure and credit the proceeds of the sale against the cost of the removal or demolition, and any balance remaining will be deposited in the circuit court and disbursed to the persons entitled thereto. Standards to guide the public officer in his determination of whether the structure is unfit for human habitation are defects increasing hazards of fire or accident; lack of ade-

[118] Letter from Donald P. Shafer, Assistant Director, Local Government Relations Division, State Tax Department of West Virginia.
[119] Miss. Code Ann. §§ 27-15-13 & 27-53-15 (1972).
[120] Code of Alabama Tit. 51 § 17(1) (1971 Supp.)
[121] Ark. Stat. Ann. § 84-428 (1960).
[122] Kentucky Constitution §§ 172, 174.
[123] Miss. Code Ann. § 27-3-5 (1972).
[124] Tenn. Code Ann. § 67-605 (1972 Supp.).
[125] Virginia Constitution Article 10, § 2.
[126] West Virginia Code Ann., § 11-3-1 (1966).
[127] Kentucky Revised Statutes § 98.012 (1972).
[128] Id. § 98.013.

[129] West Virginia Code § 9-5-26 (1969), Code of Virginia § 63.1-133.1 (1973).

quate ventilation, light, or sanitary facilities; dilapidation; disrepair; structural defects, uncleanliness, and any additional standards promulgated by local ordinances.[130]

Arkansas provides that first-class cities have the power to order the removal or razing of buildings that have become dilapidated, unsightly, unsafe, unsanitary, or detrimental to the public welfare.[131]

In Alabama, the incorporated municipalities are specifically authorized to adopt and enforce ordinances regulating the repair and maintenance of all buildings used for human occupancy, the number of occupants, and the mode and manner of occupancy for the purpose of insuring the safe and sanitary environment of the occupants of such structures; and to compel the owners or persons in charge of such buildings to alter or modify them for the purpose of insuring the safe and sanitary environment of the occupants thereof; and to prohibit the use and occupancy of such buildings used for human occupancy until such rules, regulations, and provisions imposed by ordinance shall have been complied with.[132]

In West Virginia, local agencies, primarily the urban renewal authority and the county housing authority, are empowered to vacate and clear away slum and substandard housing. Under the Urban Renewal Authority Act, counties are authorized to establish a slum clearance and redevelopment authority. This agency is granted broad powers to deal with the problem of slum and substandard housing including the power of eminent domain.[133] County courts may cooperate with other agencies to accomplish the goal of safe and sanitary housing by assisting in the repair, closing, and demolition of substandard housing and by making and keeping surveys of substandard and slum housing within its jurisdiction.[134]

In Virginia, the local government can make improvements in slum areas and make the cost thereof a lien on the property. Local authorities also have the right to close, vacate, and demolish the buildings if the owner does not comply with the order from local authorities to take appropriate action on the buildings in question.[135] Where the housing authority undertakes a conservation plan it may demolish dwellings under certain circumstances, and where it undertakes a redevelopment plan it may acquire dwellings within the area by eminent domain.[136]

Minimum Housing Code and Landlord Tenant Relations

None of the seven States provides for a statewide minimum housing code. To a varying degree, however, the States allow for local regulation in the area. The enabling statutes differ on the specificity of the delegation and on the localities and buildings subject to regulation.

West Virginia, for instance, only authorizes counties having a population of more than 200,000 persons to adopt minimum building and housing standards. This clearly is aimed at urban rather than rural housing.[137] Likewise, Alabama only authorizes incorporated municipalities to adopt minimum housing standards.[138] Mississippi enables both counties[139] and municipalities[140] to adopt building codes and other codes dealing with the general public health, safety, or welfare. Mississippi specifically exempts farm buildings and structures from the regulation of counties, thus diminishing its effect on rural housing. The other States do not make specific reference to minimum housing codes but give general grants to power to regulate construction, maintenance, and repair of housing.[141]

As can be seen by the dearth of specific legislation, legislation in this area should not significantly affect the present supply of housing. Even where there is legislation, it is merely enabling rather than mandatory and seems aimed at urban rather than rural problems.

Because the States have left regulation of minimum standards of housing to local governments, the States have not enacted legislation providing for suits for damages by aggrieved tenants. Likewise, the State legislation does not authorize an aggrieved tenant to withhold rent where the landlord has violated minimum housing codes. None of the States has provided for special housing courts to deal with landlord-tenant and other housing-related problems. Although none of the States had enacted legislation permitting the appointment of a receiver to

[130] Kentucky Revised Statutes §§ 80.620—80.720 (1969).
[131] Arkansas Statutes Annotated § 19-2803 (1968).
[132] Code of Alabama Title 37, § 785(2). (1971 Supp.).
[133] W. Va. Code Annotated §§ 16-18-4, 16-18-5, 16-18-8 (1972).
[134] Ibid., §§ 16-16-9, 7-1-5.
[135] Code of Virginia, §§ 15.1—11.2 (1970).
[136] Ibid., §§ 36-48, 36.50.1.
[137] W. Va. Code. Ann. § 7-1-3n (1969).
[138] Code of Ala. Tit. 37. § 785(2) (1971 Supp.).
[139] Miss. Code Ann. § 19-5-9 (1972).
[140] Id. § 21-19-25.
[141] Code of Va. Ann. § 15.1-510, § 15.1-510.2 (counties), 15.1-839, 15.1-683 (municipalities); K.R.S. § 67.380, § 67.390, § 67.400, § 67.410 (1972). Kentucky excludes buildings for agricultural purposes on land solely used for agriculture from these provisions. Ark. Stat. Ann. § 19-2802 (1968). This applies only to first-class cities.

collect rents and make improvements, the attorney general of Tennessee has advised us that a Tennessee court may be able to do so under its general equity power.

Perhaps the most noticeable feature of landlord-tenant relations in the seven States is the relative dearth of legislation protecting the tenant, possibly due to the fact that concepts of tenants' rights are largely of recent vintage. The statutes governing landlord-tenant relations have remained relatively unchanged in recent years.

Three of the States—Kentucky,[142] Virginia,[143] and West Virginia [144]—do have legislation prohibiting discrimination in the leasing of publicly owned, operated, or assisted housing on grounds of race or color; and they also forbid such discrimination in the leasing of private property, with certain exceptions.[145]

Fire Insurance

Of the seven States, apparently only Virginia has a program to provide fire insurance in substandard areas. But since Virginia's program is limited to urban areas [146] and specifically excludes property used for farming,[147] it is of no consequence to rural housing. I will briefly discuss the program, however, merely as a guide to a possible program to include rural housing.

Under the Virginia plan,[148] the property—which may include both real and tangible personal property—must meet certain qualifications, such as those mentioned above, that it be urban and not farm and that it be in compliance with State laws and local building codes and ordinances.[149] Under the plan, a person meeting the qualifications above would have his property inspected by an inspection bureau created for the purpose. The authorized insurers in Virginia are to formulate and administer a program for the equitable distribution and placement of applications for fire and extended coverage insurance for qualified property which has been inspected.[150] To carry out this program, the insurers are authorized to form a direct insurance association.[151] If the State Corporation Commission finds that the program devised by the insurers under §38.1–748 and §38.1–748.1 is failing to provide adequate insurance for qualified property, the commission may order the creation of a joint underwriting association.[152] If the commission orders the association created, all insurers authorized to write fire and extended coverage in the State must be members of the association as a condition precedent to doing business in the State. The association is to formulate a program to carry out the purposes of the statute. The association will have the power to cause its members to issue policies to applicants, to assume reinsurance from members, and to cede reinsurance.[153] Members' degree of participation in the association will be in the proportion of each member's total yearly premiums of all members of the association.[154]

The Virginia program has the advantage of first giving the insurers the chance to work out their own program. This makes the plan more palatable to the insurers, who can best allocate cost and plans. But the threat of State control checks any inclination of the insurers to thwart the aims of the legislation.

Interest and Usury

Of the seven States surveyed, four—Virginia, West Virginia, Alabama, and Mississippi—have restricted the permissible rate of interest to 8 percent in written agreements.[155] Beyond this point, the similarity between State statutory schemes ends. (See the appended State legislative reports for the basic provisions in each State.)

Of particular note is a provision of the Virginia code that is somewhat unique. Under section 6.1–319.1, loans secured by primary real estate mortgages and first deeds of trust are

[142] Kentucky Revised Stat. § 344.360 (1972 Supp.).
[143] Virginia Constitution Art. 1, § 11.
[144] W. Va. Code Ann. § 5-11-9 (1971).
[145] Kentucky Revised Stat. § 344.360 (1972 Supp.) (exemptions include the rental of housing accommodations in buildings for less than two families living independently of one another, if the owner resides in one of the accommodations);
W. Va. Code Ann. § 5-11-9 (1971) (rentals of rooms or rooms in rooming housing occupied by the owner and containing no more than four rented rooms are excluded from the term "housing accommodations" as covered by § 5-11-9, § 5-11-3(k).);
Code of Virginia § 36-88 (1973 Supp.) (nothing in the Virginia Fair Housing Law applies to single-family houses sold or rented by an owner or to rooms or units in dwellings occupied or intended to be occupied by no more than four families living independently of each other, if the owner occupies one of such units as his residence. § 36-87 (1973 Supp.).
[146] Code of Va. § 38.1–747(3)(1970).
[147] Id. § 38.1–747(3)(a).
[148] The Basic Property Insurance Inspection And Placement Plan And Joint Underwriting Association. Id. §§ 38.1–746 to 38.1–755.1(1970).
[149] Id. § 38.1–747.
[150] Id. § 38.1–748.
[151] Id. § 38.1–748.1(1973 Supp).
[152] Id. § 38.1–749(1970).
[153] Id. § 38.1–750.
[154] Id. § 38.1–751.
[155] Code of Ala., Tit. 9 § 60 (1958); Miss. Code Ann. § 36 (1966 Amended 1972); Code of Va. Ann. § 6.1–319n (1968); W. Va. Code Ann. § 47–6–5 (1968).

exempted from the general usury statutes. The permissible rate of interest allowed in this situation is that rate agreed upon and included in the written loan contract. But the statute forbids the exemption of floating interest rates in first mortgages and first deed of trust situations.[156]

An interesting feature of both Kentucky and Alabama law is the existence of an upward threshold at which the usury limitations are eased or eliminated. Kentucky law permits any specified rate of interest where the extent of the obligation is in excess of $25,000, but an 8.5 percent interest ceiling is enforced where the loan agreement is secured by a single-unit family residence or where the obligation secured is less than $25,000.[157] In Alabama, where corporate borrowers are involved, the maximum permissible interest rate is 15 percent on any loan greater than $10,000, but less than $100,000. For a loan of greater than $100,000, the rate of interest is unregulated.[158] Where other borrowers are involved and the loan is in excess of $100,000, the lender may charge as much as 15 percent.[159]

For purposes of the permissible rate of interest, all of the seven States surveyed include discount points in the definition of interest.[160] In at least six of the seven States, simple amortization is used to determine whether the inclusion of discount points makes the interest rate usurious.[161] The major difference among these seven States is the way each defines "points" for purposes of the usury statutes. In West Virginia, Virginia, Tennessee, Kentucky, and Mississippi it is clear that whatever points the lender receives are counted as interest for usury purposes.[162] In Arkansas, it is unclear from the latest court decision in the area whether points received from sources other than the borrower are includable in interest for usury purposes.[163] In Alabama, it is clear that points must be paid by the borrower to be includable in interest for usury purposes.[164]

In five of the seven States surveyed, loans insured through the Federal Housing Administration and the Veterans' Administration are exempted from the State usury restriction.[165] In two of the States, Tennessee and Arkansas, there is no provision for exemption, and it appears that such loans are subject to the normal State usury prohibitions. Tennessee has passed no legislation in this area, and Arkansas is prohibited by the constitutional nature of the usury provisions from statutorily making a distinction between VA or FHA loans, or any other type of loan.[166]

Of the States exempting VA and FHA loans, Virginia has perhaps the broadest statute.[167] It not only exempts VA- and FHA-insured loans but also loans insured by any other Federal agency or organization and loans made pursuant to the requirements of the Federal Home Loan Mortgage Corporation.

The time-price differential is recognized as an exemption to the usury laws in Virginia, West Virginia, Kentucky, Tennessee, and Mississippi.[168] In Alabama, the time-price differential is subject to the consumer finance law, which limits the permissible rate of finance charges.[169]

The time-price differential has long been recognized in Arkansas.[170] But under a 1952 Arkansas court decision, the extent to which this method of financing can be utilized in that State may be somewhat limited.[171] In the *Hare* decision, doubt was cast upon what had theretofore been considered a "sale." The key test now seems to be whether the seller increased his cash price with the reasonable assurance that the paper could be discounted; if such assurance existed, the transaction is essentially a loan and may be attacked as usurious.[172]

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[156] Code of Va. Ann. § 61–319.1 (1968).
[157] Ky. Rev. Stat. Ann. § 360.010 (1970).
[158] Code of Ala. Tit. 9 § 67(1) (1958).
[159] Code of Ala. Tit. 9 § 67(1) (1958).
[160] Code of Ala., Tit. 5 § 316(9) (1958); W. Va. Code Ann. § 47–6–5 (1968); *Smith* v. *Easton* 223 Ark 747, 749, 268 S.W.2d 389 (1950); 70 Op. Att'y Gen. of Ky. 284; *Silver Homes* v. *Marx and Bensdorf Ins.* 206 Tenn 361, 333 S.W.2d 810 (1960); *Hyde* v. *Finley,* 26 Miss. 468 (1853); *accord Palkinghorn* v. *Hendricks* 61 Miss. 366 (1883); *Hillen* v. *Ellis* 72 Miss. 701, 18 So. 95 (1895); Code of Va. Ann. § 6.1–319 (1968).
[161] Code of Ala., Tit 5 § 316(a) (1958); Code of Va. Ann. § 6.1–319 (1968); W. Va. Code Ann. 47–6–5 (1968); 70 Op. Att'y Gen. of Ky. 284; T.C.A. § 47–14–104 (1969); *Smith* v. *Easton* 223 Ark. 747, 749, 268 S.W.2d 389 (1950).
[162] Miss. Code Ann. §§ 36, 37 (1966); Code of Va. Ann. § 6.1–319 (1968); W. Va. Code Ann. § 47–6–5 (1968); *Silver Homes* v. *Marx and Bensdorf Ins.* 206 Tenn. 361, 333 S.W.2d 810 (1960).
[163] *Smith* v. *Easton* 223 Ark 747, 749, 268 S.W.2d 389, 390 (1950).
[164] Code of Ala., Tit. 5 § 316(a) (1958).
[165] Code of Ala., Tit. 9 § 67(3) (1958); Miss. Code Ann. 43–33–307 (1972); Code of Va. Ann. § 6.1–328 (1972); W. Va. Code Ann. § 319–4–29 (1972).
[166] *Winston* v. *Personal Finance Co. of Pine Bluff,* 220 Ark. 580, 249 S.W.2d 315 (1952).
[167] Code of Va. Ann. § 6.1–328 (1972).
[168] *Roger* v. *O'Neal* 33 W. Va. 159, 10 S.E.375 (1889), *First Nat. Bank* v. *Mann* 94 Tenn. 17, 27 S.W. 1015, 27 LRA 565 (1894); Ky. Rev. Stat. Ann. 371.260(1); *Kidd* v. *Brottors* 212 Va. 197, 183 S.E.2d 140 (1971); See *Bryant* v. *Securities Investment Co.* 233 Miss. 740, 102 So.2d 701(1958).
[169] Code of Ala. Tit. 5 §§ 317, 316(a) (1958) (see Appended statute).
[170] *Smith* v. *Kaufman* 145 Ark. 548, 224 S.W. 978 (1920).
[171] *Hare* v. *General Contract Purchase Corp.* 220 Ark. 601, 249 S.W.2d 973 (1952).
[172] Id., at 978.

Banks and Savings and Loan Associations

Branch Banking: In terms of branch banking, the seven States can be divided into three main categories: 1) not allowed, 2) allowed only if certain requirements are met and there is approval by the appropriate State official(s), and 3) allowed automatically if certain conditions are met.

In the first category is West Virginia, the only State studied that prohibits all types of branch banks and engagement in business at any other place besides the principal office; [173] it follows that extra-county branches of banks are prohibited.

The second and largest category includes Kentucky, Mississippi, Tennessee, and Virginia. Virginia provides that the State corporation commission, when satisfied that the public convenience and necessity will be served, may authorize banks having unimpaired capital of a certain amount to establish branches within the limits of the city or county in which the parent bank is located, or to establish branches elsewhere by merger with banks located in any other city or county [174] (this appears to be unique to Virginia). Kentucky's statutory provision is similar, except that: 1) The commissioner of banking must find that there is a reasonable probability of successful operation of the branch, as well as that it would be and is in the public interest to establish it; 2) there must not be another existing bank in the area; and 3) there is no merger provision allowing extra-city or extra-county branches.[175]

The approach of Mississippi is a bit different; the parent bank must first obtain from the State comptroller, the attorney general, and the Governor, or a majority thereof, a certificate that the public convenience and necessity will be promoted by the establishment of such a bank. Mississippi is unique in that a noncounty radial measurement is used—a branch may be authorized within 100 miles of the parent bank—and in that there is an express statutory maximum (15) on the number of branch banks that can be set up.[176]

While Tennessee law provides that the superintendent of banking may approve branch offices, no branch may be set up outside the county wherein the principal office is located.[177]

The last category includes Arkansas and Alabama. If several requirements are met (i.e., the branch office is within the county where the main office is located, no other chartered bank is in existence within a certain distance from the branch, and a surplus capital requirement is met), a bank in Arkansas can establish a branch, further official approval not being necessary.[178] In Alabama, the prohibition against branch banking does not apply if branch banking has been authorized in the county, or if that county has a population of 200,000 or more according to the last national census.[179] This section was held not to authorize branch banking across county lines in *Security Trust Sav. Bank* v. *Marion County Banking Co.*[180]

In short, five States do not allow cross-county branch banks: Alabama, Arkansas, Kentucky, Tennessee, and West Virginia.

Loans-Banks: A discussion of two types of loan banks follows.

Percentage-of-capital limitations on loans: All of the seven States have some limitation on the percentage of capital assets that can be lent to any one person or entity, and all provide for exceptions.

The majority of the States have strict limitations (i.e., if the loan does not fit within an exception, there is no special procedure whereby it may exceed the maximum percentage): Alabama,[181] Arkansas,[182] Mississippi,[183] Virginia,[184] and West Virginia.[185] On the other hand, Kentucky provides that the 20 percent capital limitation is not binding if such a borrower pledges with the bank good collateral security or executes a mortgage upon real estate (in which case the limit is 30 percent).[186] Tennessee also allows a borrower to get more than the normal maximum of 15 percent of the bank's capital (up to 25 percent), on the condition that each specific loan of a higher amount be approved in advance by the board of directors or by the finance committee of the bank.[187]

[173] West Virginia Code Ann., § 31A-8-12 (1972).

[174] Code of Virginia, § 6.1-39 (1973 Supp.) On the contrary, savings and loan associations may not establish a branch unless the commission is satisfied that the public convenience and necessity will be served. §6.1-195.48 (1973).

[175] Kentucky Revised Statutes 287.180 (1972). [Hereinafter cited as KRS].

[176] Miss. Code Ann. § 5226 (1957). [The relevant 1972 Mississippi Code Ann. was not available at the time this appendix was written.]

[177] Tenn. Code Ann., § 45-443 (1972 Supp.). [Hereinafter cited as TCA].

[178] Ark. Stat. Ann., §§ 67-340, 67-348 (1971 Supp.).

[179] Code of Alabama Tit. 5, §§ 125 & 125(1) (1960).

[180] 253 So.2d 17 (Ala. 1971).

[181] Code of Alabama Tit. 5, § 82 (1960)—20 percent.

[182] Ark. Stat. Ann., § 67-507 (1971 supp.)—20 percent.

[183] Miss Code Ann., § 5211 (1957)—15 percent.

[184] Code of Virginia, § 6.1-61 (1973)—15 percent.

[185] West Virginia Code Ann., § 31A-4-26 (1972)—10 percent.

[186] KRS, 287.280 (1972).

[187] TCA § 45-426 (1964).

The limitation does not apply to the indebtedness of certain governmental units in all of the States: Alabama (United States, State, counties, and municipalities),[188] Arkansas (United States, State, counties, and municipalities),[189] Kentucky (United States, State, counties),[190] Mississippi (United States, State),[191] Tennessee (United States),[192] Virginia (United States, State, counties, and municipalities),[193] and West Virginia (United States, State, counties, and municipalities).[194] Arkansas, it might be noted, specifically lists housing authorities as government entities to which the limitation does not apply.[195]

Real Estate Loans: In a couple of States, Alabama [196] and Arkansas,[197] a bank may make loans on real estate secured by a mortgage with no statutory limitations or directions as to such loans, other than those relating to loans in general.

Most of the States studied, however, do have more specific limitations on real estate loans, the most common being some type of maximum length during which property may be held. The following States have a time limitation when real estate is conveyed to the bank in satisfaction of its debts or purchased at a judgment sale: Kentucky—10 years maximum; [198] Mississippi—5 years, unless the consent of the comptroller is obtained; [199] Tennessee—5 years, unless the superintendent of banking allows a greater period; [200] Virginia—10 years, except with the consent of the State corporation commission; [201] and West Virginia—5 years, unless an extension of time is given by the commissioner of banking.[202] Most of these States thus allow the maximum period to be extended.

Savings and Loan Associations: All but one of the States have requirements that every real estate loan of a savings and loan (or building and loan) association be secured by a mortgage or other instrument constituting a first lien (or its equivalent, e.g., the association itself owns any other prior liens) upon the real estate securing the loan: Alabama,[203] Arkansas,[204] Kentucky,[205] Mississippi,[206] Tennessee,[207] and Virginia.[208] The lone exception is apparently West Virginia.

In addition, several States provide that a real estate loan by a savings and loan association is not to exceed a certain proportion of the value of the real estate. Tennessee provides that the loan is not to exceed in amount two-thirds of the value of such real estate, as determined by the board of directors of the savings and loan association; this limitation does not apply to mortgage loans insured by the Federal Housing Administration.[209] West Virginia also has a percentage requirement on the amount of the real estate loan—the loan is not to exceed 95 percent of such value unless it is insured or guaranteed by the Federal Government.[210]

Virginia has a slightly different ceiling limitation, based not only on percentage but on actual monetary value; except as otherwise provided in the statutes, no real estate loan can exceed $45,000 on each home or exceed 90 percent of the value of the real estate up to $50,000. This, as in the case of Tennessee and West Virginia, is not applicable to loans insured or guaranteed by a Federal agency.[211]

Mortgages: None of the State statutes involved expressly prohibits or permits "flexible" or "open-end" mortgages. However, Alabama does permit open-end credit plans and, by analogy, this might give support to the proposition that authority exists in the State for open-end mortgages as well.[212]

Health Laws and Regulations

In summarizing the laws of the seven States in these three areas, perhaps the most meaningful statement that can be made is that they are generally not very significant in terms of affecting the current supply of housing nor in terms of the future development of low income housing. The key point to keep in mind is that in every

[188] Code of Alabama, supra note 9.
[189] Ark Stat. Ann., supra note 10, subsection (g) and (h).
[190] KRS, supra note 14, at 287.290 (1–3).
[191] Miss. Code Ann., supra note 11.
[192] TCA, supra note 15, subsection (b).
[193] Code of Virginia, supra note 12, subsection (A)(5).
[194] West Virginia Code Ann., supra note 13, subsection (a)(6).
[195] Ark. Stat. Ann., supra note 10, subsection (i).
[196] See Code of Alabama, Tit. 5, § 82 (1960).
[197] See Ark. Stat. Ann., § 67–501 (1966). In Arkansas, only building and loan associations having assets in excess of $500,000 may acquire real estate in satisfaction of debts owing to it or by a foreclosure sale, § 67–834 (1966).
[198] KRS, 287.100(3) (1972).
[199] Miss. Code Ann. § 5216(5) (1972 Supp.). The extension may not exceed five years, meaning that the absolute maximum is 10.
[200] TCA § 45–436(2) (1972 Supp.)
[201] Code of Virginia § 6.1–59 (1973).
[202] West Virginia Code Ann. § 31A–4–13 (1972).
[203] Code of Alabama Tit. 5 § 231 (1960).
[204] Ark. Stat. Ann. § 67–830 (1966).
[205] KRS, § 289.441(3) (1972).
[206] Miss. Code Ann., § 5288–15(a) (1972 Supp.).
[207] TCA § 45–1402 (1964).
[208] Code of Virginia § 6.1–195.34(h) (1973).
[209] TCA, supra note 35.
[210] West Virginia Code Ann., § 31–6–21 (1972).
[211] Code of Virginia, supra note 36.
[212] Code of Alabama Tit. 5 § 317 (1971 Supp.). The Consumer Finance Law does mention that open-end credit plans are specifically exempt from its control.

State a great deal of regulatory and rule making authority is granted to local government—particularly county and municipal boards of health.

This horizontal report makes no attempt to summarize each State's legislation in each of these three areas (the reader is referred to the appropriate State appendix for such individual attention); rather, it will briefly outline the general scope of the laws and regulations as they exist in most, if not all, of the States. Attention will be called to those specific laws which appear to be unique or unusual, and therefore, worthy of special mention.

Health Laws and Regulations as They Affect Safe and Sanitary Housing: All seven States attempt in some manner to regulate the building industry for the general purpose of public health and welfare. These regulations may be found in the health and welfare statutes of some States, and special building or professional and occupational statutes in others. For the most part, the States have delegated to municipal and often to county government the authority to establish building codes and regulate contractors, plumbers, and electricians. No State except Tennessee has seriously attempted to implement a statewide health code,[213] although at least one State has a uniform plumbing code administered by the State health department.[214] Typically, all regulation of these building trades and industries is left up to local government.

None of the seven States in this study has enacted a minimum housing code, although the authority to do so is frequently vested in municipalities.[215] It is quite likely, therefore, that each of these States could have dozens of separate and unrelated minimum housing codes.

Five of the seven States have promulgated some type of statewide fire code, or have established a State fire marshal to do so. Arkansas [216] and Mississippi [217] have no statewide guidelines but clearly authorize muncipalities to enact and enforce their own codes.

Very little of significance can be said about State health laws and their effect upon the supply of housing in these seven States. It is submitted that no unusual or troublesome State laws exist with regard to the purposes of this study. While Tennessee has perhaps the most detailed health and safety regulations,[218] most State legislation, in substance, just provides that any county or municipality can promulgate regulations or codes reasonably related to public health and welfare.[219] Clearly, such legislation defies any meaningful analysis; every county and municipality within all seven States would have to be individually examined and their regulations complied with.

Requirements for Installation of Water and Waste Systems: All seven States have legislation concerning the installation of water and waste systems, but with the exception of Tennessee none of these statutes has a measurable effect on lot size. As with health laws and regulations, the great majority of actual regulation in the water and waste system area is in the hands of local health boards and sanitation districts subject only to the general regulations of State health departments and performance standards imposed by State environmental and natural resources commissions.

In Tennessee, lot size requirements and their relationship to public water supplies are expressly dealt with by statute.[220] When such supplies are available, the minimum lot size is 7,500 square feet; when not available, 15,000 square feet. Moreover, minimum distances from a water well or other source may be specified, additional lot size may be required as indicated by percolation tests, or the particular lot or lots may be disapproved when it is determined that the soil will not absorb the sewage. Significantly, this section does not apply within any corporate limits. Although such detail is not present in the statutes of the other six States, it is reasonable to assume that similar or analogous regulations and local ordinances do exist.

In Alabama, the regulations are, typically, left largely in the hands of county health boards.[221] The county health boards may require the installation of plumbing facilities conforming to the rules and requirements of the State board of health, and require connections to sanitary sewers where necessary.[222] The issuance of permits for the installation of plumbing in structures outside the jurisdiction of a municipality depends on meeting statewide requirements and inspection is to be done by the county health boards.[223] Municipalities may establish their own regulations [224] and generally

[213] Tenn. Code Ann. Tit. 53 Ch. 25 (1966).
[214] Ark. Stat. Ann. §§ 71-1205—71-1217 (1957).
[215] See e.g., Code of Ala. Tit. 37 § 785(2) (1971 Supp.).
[216] Ark. Stat. Ann. § 19-2801 (1968).
[217] Miss. Code Ann. § 21-19-21 (1972).
[218] See Tennessee Appendix, § VII, infra.
[219] E.g., Miss. Code Ann. §§ 21-19-25 and 19-5-9 (1972).
[220] Tenn. Code Ann. §53-2012 (1966).
[221] Code of Ala. Tit. 22 § 140(14) (1971 Supp.).
[222] Id.
[223] Id. at Tit. 22 § 140(18).
[224] Id. at Tit. 37 § 601 (1958).

have greater power to promulgate more detailed regulations.[225] Also, water authorities in Alabama are operated on a countywide basis, and therefore are often the water suppliers of rural dwellings.[226]

In Kentucky, the Department of Environmental Protection is chiefly responsible for water and waste system control, but responsibility is shared locally with sanitation districts. Once a sanitation district is established in Kentucky, no person or public corporation is permitted to install within the district any laterals, trunk lines, interceptors for the collection or discharge of sewage or other liquid waste, or treatment or disposal works, until such plans have been submitted and approved by the board of directors of the sanitation district and by the Department of Environmental Protection.[227] Similarly, in Tennessee, no person may install, permit to be installed, or maintain any cross-connection, auxiliary intake, bypass, or interconnection, unless the source and quality of water from the auxiliary supply, the method of connection, auxiliary intake, bypass, or interconnection has been approved by the State department of public health.[228]

In Virginia, any person constructing a sewage system[229] or a water supply system[230] having three or more connections must first obtain the approval of the governing body of the county. Similarly, septic tank permits may be required from county authorities in Virginia.

At least two States, Tennessee and Virginia, specifically deal with subdivision problems in their water and sewer legislation. In Virginia, the county board of supervisors may require a subdivision or land developer to pay his pro rata share of the cost of providing reasonable and necessary sewage and drainage located outside the property limits of the developer but necessitated at least in part by the construction or improvement of his development.[231] This sort of provision is not unusual, and it should be reemphasized that similar regulations may exist in a large portion of all of the seven States in the form of subdivision and zoning ordinances.[232]

Tennessee has particularly detailed and somewhat confusing provisions regarding water and sewerage facilities for subdivisions. The State department of public health is authorized to exercise general supervision over the planning, construction, and operation of individual sewage disposal systems for proposed subdivisions, where public sewerage systems are not available, except within the corporate limits of municipalities, and to establish standards for individual sewage disposal systems.[233] The owner of a proposed subdivision is required to submit detailed information, including a map of the surrounding area and of the area to be subdivided, showing (inter alia) proposed lot sizes and location of supply lines.[234] He must also furnish additional data as required by the local health officers as a basis for determining the suitability of individual lots.[235] The confusion in the Tennessee law is caused by the statutory definition of a subdivision. A subdivision is defined as any tract or parcel of land divided or proposed for division into five or more lots, sites, or other divisions, for the purpose of immediate or future building of houses or other developments, requiring a maximum lot size in any subdivision be 40,000 square feet or less, to a minimum of 15,000 square feet.[236] Apparently, lots in excess of 40,000 square feet and less than 15,000 square feet are not subject to the act.

In conclusion, it is submitted that the legislation of the seven States studied does not yield a particularly informative or relevant body of law with respect either to the current supply of housing or with respect to future low income housing development. In the final analysis, each county and municipality, not to mention each State, will have to be examined to discover exactly what substantive regulations must be complied with. However, it is submitted that there are essentially no water and waste system laws that would present inordinate or unusual obstacles to new housing development—low income or otherwise.

Environmental Protection Laws: All seven States studied have enacted some sort of envi-

[225] Id. at Tit. 37 §§ 603–606.
[226] Id. at Tit. 50 §101 (1971 Supp.).
[227] Ky. Rev. Stat. § 220.260 (1969).
[228] Tenn. Code Ann. § 53–2004 (1966).
[229] Va. Code Ann. § 15.1–326.
[230] Id. at § 15.1–341.
[231] Id. at § 15.1–510.7.
[232] See e.g., Ark. Stat. Ann., §19–2829(c) (1968), which clearly authorizes this power for local planning and zoning commissions.

[233] Tenn. Code Ann., § 53–2010 (1966). (Sections 53–2009 through 53–2016 of the Tennessee Code Annotated were repealed by House Bill No. 224, Chapter No. 188, Public Acts 1973, effective July 1, 1973.)
[234] Id. at § 53–2011(1)(a) (1972 Supp.). (Sections 53–2009 through 53–2016 of the Tennessee Code Annotated were repealed by House Bill No. 224, Chapter No. 188, Public Acts 1973, effective July 1, 1973.)
[235] Id. at § 53–2011(1)(c). (Sections 53–2009 through 53–2016 of the Tennessee Code Annotated were repealed by House Bill No. 224, Chapter No. 188, Public Acts 1973, effective July 1, 1973.)
[236] Id. at § 53–2009. (Sections 53–2009 through 53–2016 of the Tennessee Code Annotated were repealed by House Bill No. 224, Chapter No. 188, Public Acts 1973, effective July 1, 1973.)

ronmental protection laws, usually establishing a single umbrella agency or, in some cases, several separate commissions to deal independently with air and water pollution. In terms of effect upon housing supply, the most significant provisions relate to water pollution and have been included in the previous discussion of water and waste systems legislation.

The primary thrust of both the water and air pollution control statutes is to establish minimum standards for the purity of the State's air and water resources. These standards have little effect upon the housing market other than the indirect influence achieved by the pressure of the regulations upon water and sanitation services. Most of the acts are aimed at discharges either directly or indirectly into the State's water supplies—this is not a meaningful hurdle to the supply of housing, in this writer's opinion. To the extent that new environmental protection regulations force improved methods of waste treatment, then perhaps the homeowner will be financially affected.

The most important statement that can be made about the environmental protection laws of these seven States with respect to their effect upon the supply of housing is that none of them has any requirement for environmental impact statements even remotely comparable to the new California Environmental Quality Act,[237] which has drastically affected the entire construction industry in that State.

Federal Laws that Regulate Real Estate Loans by National Banks

National banks are specifically authorized to make loans secured by real estate as long as the real estate is improved, the loan is secured by a mortgage or deed or trust, and the security is a first lien upon the property.[238]

Conventional Real Estate Loans: The requirements for conventional real estate loans are summarized in the following chart:

Max. maturity	% of appraised value	Amortization required
5 years	50	None
10 years	66⅔	At least annual installments sufficient to amortize 40% of the loan principal at maturity
20 years	66⅔	At least annual installments sufficient to amortize loan in full within a period of 20 years
20 years	75	At least annual installments sufficient to amortize loan in full at maturity
30 years	90	At least annual installments sufficient to amortize loan in full at maturity

Insured and Guaranteed Loans: The above limits do not apply to loans insured by the State or under provisions of the following acts: National Housing Act: Title II, VI, VIII, IX, section 8 of I (see Exhibit 2); Housing Act of 1949: title V (see Exhibit 3) Urban Growth and New Community Development Act of 1970: Part B; Home improvement loans insured under 12 U.S.C. 1709(k) or 1715(h).

Interest Rate:[239] A summary of interest rate laws follows.

A. Applicable interest rate

1. The rate allowed by the laws of the State where the bank is located, or

2. At rate of 1 percent in excess of the discount rate on 90-day commercial paper in effect at the Federal Reserve Bank in the Federal Reserve District where the bank is located.

3. Whichever may be greater.

4. If there are no State laws fixing interest rate, the rate shall be either 7 percent or 1 percent above the discount rate.

B. Applicable law

1. State usury laws are not applicable to national banks.[240]

2. The interest rate of the State where the loan is made is applicable, not the State where the bank is located.[241]

3. The penalty for usury fixed by Federal law [242] is twice the amount of the interest paid, with a 2-year statute of limitations.

Federal Laws that Regulate Real Estate Loans by Federally Chartered Savings and Loan Associations

A Federal savings and loan association is a financial institution which is chartered by the

[237] Cal. Pub. Res. Code § 21060 et seq. (Est. Supp. 1973.)
[238] 12 U.S.C. 371.

[239] 12 U.S.C. 85.
[240] 102 F.Supp. 542.
[241] 302 F.Supp. 62.
[242] 12 U.S.C. 86.

EXHIBIT 2

National Housing Act.
- Title II: FHA Loans
- Title VI: War Housing Insurance (for W.W. II veterans; loans made before 1950; rarely used today).
- Title VIII: Armed Services Housing Mortgage Insurance
- Title IX: Housing for Educational Institutions
- Title I: Sec. 8; Housing Renovation and Modernization

EXHIBIT 3

Housing Act of 1949: Title V: Farm Housing

This act provides for loans administered through the Farmer's Home Administration for the improvement, construction, alteration, or repair of dwellings or related facilities for farmers, rural residents, and elderly persons in rural areas.

Federal Home Loan Bank Board under the Home Owners' Loan Act of 1933, as amended. Its primary purposes are to promote thrift and to provide for the financing of homeownership.[243]

Rules and regulations regarding real estate loans are issued from time to time by the board pursuant to 12 U.S.C. 1464(c). The following is an outline of the current rules and regulations most relevant to the field of housing financing. These rules will vary somewhat depending upon the particular charter of the savings and loan association involved. Since 1933 there have been four different charters: E, N, K, and K (revised). Today, most associations operate under either charter N or K(rev.), which are virtually the same in actual practice. This outline is based on the provisions of charter N and K(rev.).

Generally, these savings and loan associations are limited in their lending to an area within a 100-mile radius of the home office or of a branch office approved by the local home loan bank board. However, if the association is a converted State institution, its lending area remains the same as it was under the State charter.

Loans are offered on various terms depending on the type of housing to be financed, with the primary emphasis on loans to individual homeowners.

Homes[244]**:** The following terms apply to loans secured by homes (dwelling units for up to four families) or a combination of homes and business property (used in part for home and part for business). Generally, these loans are limited to $45,000 per single family dwelling, they must be a first lien upon the property, and must be within the association's regular lending area. (Loans over $45,000 or beyond the regular lending area may be made on the security of homes, but these are limited to 20 percent of the association's assets.)

Also, loans which are insured or guaranteed under the National Housing Act, Servicemen's Readjustment Act of 1944, or chapter 37 of title 38, U.S.C., are generally not subject to the following terms, but rather are subject to terms acceptable to the insuring or guaranteeing agency.

A. Monthly Installment Loans
- Loans may be made up to 75 percent of the value of the real estate security (and up to 80 percent with the authorization of the association's members).
- Loans are repayable monthly within 30 years.

B. Other Installment Loans
- Loans with less than monthly payments are limited to a 15-year term.
- Interest payments must be made at least semiannually and principal payments at least annually.

C. Loans Without Full Amortization (Noninstallment)
- Loans may not be made in excess of 50 percent of the value of the security and are limited to a term of 5 years.
- With member's authorization, loans of up to 60 percent of value with a maximum term of 3 years may be made.
- Interest is payable semiannually. (Principal due at maturity).
- Construction loans may be made up to 80 percent of value and for a term of not more than 18 months.
- Trade-in loans may be made up to 80 percent of value and for a term of not more than 18 months. (Such loans are limited at any one time to 5 percent of the association's assets and must be in the regular lending area.)

D. Loans in Excess of 80 percent of Value
- Loans up to 90 percent and 95 percent of the value of the security may be made under certain conditions (but are limited in the aggregate to 30 percent of assets).
  - a. 90 percent loans: Monthly installment loans on one family completed residences may be made up to the least of:
    - i. 90 percent of value of real estate
    - ii. 90 percent of certified purchase price

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[243] 12 U.S.C. 1464.
[244] 12 U.S.C. 1464(c); 12 C.F.R. 545.6–1(a).

iii. $45,000;
for a maximum term of 30 years; and limited to 30 percent of assets

b. 95 percent loans: Monthly installment loans on one family completed residences may be made up to the least of:

i. 95 percent of value of real estate

ii. 95 percent of purchase price

iii. $36,000

iv. BUT, the balance over 90 percent must be privately guaranteed or insured;
for a maximum term of 30 years; and limited to 10 percent of assets (included in 30 percent limit category)

c. Both 90 percent and 95 percent loans require advance monthly payments of half the estimated taxes + insurance premiums:
d. Construction loans up to 90–95 percent may be made to owner-borrowers or vendors, BUT payouts over 80 percent of value are barred until completion, or sale (if vendor).

• Once an individual loan balance has been reduced to not more than 80 percent of value, it falls out of the 30 percent of assets category.

• Loans up to 100 percent of the value may be made on the security of:

a. a single family dwelling under the regulations for the Housing Opportunity Allowance Program [245] [for middle and low income] families (see Exhibit 4)
b. a home where that portion of the loan which exceeds 80 percent is insured or guaranteed.

Other Dwelling Units [246]**:** The following terms apply to apartment complexes for more than four families and real estate upon which are located apartments or homes combined with business property involving only minor or incidental business use (the value of the property attributable to business use must not exceed 20 percent of the total value). Insured and guaranteed loans, again, are subject to terms acceptable to the insuring or guaranteeing agency.

A. Monthly Installment Loans
1. Loans may be made up to 50 percent of value (or up to 80 percent if authorized by the association's members).
2. Loans are repayable monthly within 30 years.
3. Such loans may be combined with a construction loan and monthly installments will begin at the end of the term allowed for construction.

B. Fully Amortized Loans
1. Loans with less than monthly payments are limited to a 15-year term.
2. Interest is payable at least semi-annually and principal at least annually.

C. Partially Amortized Loans
1. Loans may be made up to 80 percent of value.
2. Monthly payments must be fixed at an amount which would be required to fully amortize the loan within 30 years.
3. The outstanding amount is payable at the end of the term, which must not be less than 10 years nor more than 30 years.

D. Loans Without Full Amortization (Noninstallment)
1. Loans up to 50 percent of value may be made and are limited to a term of 5 years.
2. With members' authorization, loans of up to 60 percent may be made with a term of not more than 3 years.
3. Interest is payable semiannually.
4. Construction loans may be made up to 75 percent of value for a term of not more than 36 months.

E. Limitation [247]
1. If the amount of any loan in this section exceeds, for any dwelling unit (apartment), an amount prescribed in/or under section 207(c)(3) of the National Housing Act (see Exhibit 5), or
2. is located beyond the regular lending area,
3. then, such loans are limited in the aggregate to 20 percent of the association's assets.

Other Improved Real Estate [248]**:** The following terms apply primarily to developed building lots or sites which by reason of installations and improvements are ready for the construction of single family homes on each site or lot.

[245] 12 C.F.R. 527.
[246] 12 C.F.R. 545.6–1(b).
[247] 12 C.F.R. 545.6–7(c).
[248] 12 C.F.R. 545.6–1(c); 12 C.F.R. 545.6–3(c).

A. Monthly Installment Loans

1. Loans may be made up to 75 percent of value.

2. The maximum term is 25 years.

B. Construction Loans to Builders (of one-family homes on developed building sites)

1. Loans may be made up to 75 percent of value of the real estate security.

2. Loans are limited to a 3-year term with interest payable semi-annually (term may be extended 3 years).

3. Construction of one-family homes must begin within 3 years of loan.

4. These types of loans are limited to 5 percent of the assets of the association and must be within the regular lending area.

C. Construction Loans to Individuals (holding developed building sites)

1. Loans may be made up to 75 percent of value.

2. Loans are limited to a 5-year term, with substantially equal payments of principal and interest sufficient to amortize at least 40 percent of the original principal amount by the end of the term.

3. The individual must certify that there is no other lien on the property and that the lot will be the site of his permanent home (not a vacation or seasonal home).

4. These loans are also limited to the regular lending area, and to 5 persent of assets.

Acquisition and Development of Land[249]: The following terms apply to financing the acquisition and development of land for primarily residential use and for the construction of homes inclusive of acquisition and development of land. However, such loans may be made only when 1) the aggregate amount of the association's general reserves, surplus, and undivided profits is equal to more than 5 percent of its savings accounts, 2) the total amount of such loans does not exceed 5 percent of the association's savings accounts, for the acquisition and development portion of the loan, 3) the loans are on the security of first liens, and 4) the loans are within the regular lending area.

A. Loans to Finance the Acquisition and Development of Land

1. Loans may not exceed 75 percent of the value of the land when completed into building lots and sites ready for construction.

2. Loans are repayable within 5 years with interest due semi-annually. (Term may be extended 1 to 2 years.)

B. Loans to Finance Construction of Homes, Inclusive of Acquisition and Development of Land

1. Loans may be made up to 80 percent of the value of the real estate when the construction of the homes is completed.

2. Loans are repayable within 6 years with interest payable semi-annually. (Term may be extended 1 to 2 years.)

C. These loans are limited to 2 percent of the amount of the association's savings accounts per borrower.

Housing Facilities for the Aging[250]: The following terms apply to loans secured by improved real estate designed for purposes of housing the aging (over 55 years of age).

A. Basic Limitations

1. Loans may be made only within the regular lending area.

2. Loans may be made only on a monthly installment basis.

3. Loans are limited to 5 percent of the assets.

B. Limitations on Specific Loans

1. Loans may not exceed 90 percent of value.

2. Loans are limited to a term of 30 years.

Development of New Communities[251]: Federal savings and loan associations may invest (without percentage limitations) in loans guaranteed in whole or in part: The New Communities Act of 1968 (82 Stat. 513) or Part B of The Urban Growth and New Communities Development Act of 1970 (84 Stat. 1791) (see Exhibit 6). The only limitations on these loans are terms acceptable to the Secretary of HUD.

Low Rent Housing[252]: The following terms apply to loans on real estate which is being constructed, remodeled, rehabilitated, modernized,

[249] 12 C.F.R. 545.6–14.

[250] 12 C.F.R. 545.6–16.

[251] 12 C.F.R. 545.6–22.

[252] 12 C.F.R. 545.6–23.

or renovated as the subject of an annual contribution contract for low rent housing under the provisions of the U.S. Housing Act of 1937, as amended.

A. There is no limitation as to maximum loan terms.

B. Loans may not exceed 90 percent of the amount of appraisal, or, in lieu of such appraisal, 90 percent of the purchase price if the real estate is to be purchased by a local public housing authority.

C. Must be within regular lending area.

Mobile Home Financing[253]: The following regulations apply to mobile home financing, but only after adoption of mobile home financing plan by the association's Board of Directors. Generally, loans secured by mobile homes are limited to 10 percent of the association's assets.

A. Inventory Financing (mobile home dealers)

1. The mobile home must be held for sale within the association's regular lending area.
2. Loans may be made up to 100 percent of the invoice price on new mobile homes and equipment, exclusive of freight.
3. Loans may be made up to 90 percent of wholesale price on used mobile homes.

B. Retail Financing (individual purchasers)

1. If the loan is not insured or guaranteed, the mobile home must:
   a. be maintained as a residence of the owner or a relative of the owner, and
   b. within 90 days of the loan, it must be located in a trailer park or other semipermanent site within the regular lending area.
2. The loan must not exceed an amount equal to the total of the following:
   a. the cost of appropriate insurance to protect lender and owner,
   b. sales tax, and
   c. in the case of a new home, 100 percent of the invoice price of the home, plus 100 percent of the invoice price of new equipment, plus 10 percent of the total of such invoice prices, exclusive of freight, or
   d. in the case of a used home, 100 percent of the wholesale value.
3. The debt must be paid in substantially equal monthly installments over a 12-year period for new homes, and over an 8-year period for used homes.
4. If the mobile home is shipped outside of the continental United States for sale, 80 percent of the freight cost may be included in the loan.

Loans Without Security (home improvement loans)[254]: Federal savings and loan associations may invest in loans without security up to 20 percent of their assets, subject to the following regulations:

A. Loans for Property Alteration, Repair, or Improvement

1. Loans may not exceed $5,000 per property.
2. They must be within the regular lending area.
3. The loan is repayable in equal weekly, biweekly, monthly, bimonthly, or quarterly installments with the first payment due no later than 120 days from the making of the loan.
4. The maximum loan term is 10 years and 32 days.

B. Any loan insured under title I of the National Housing Act or a home improvement loan insured under title II of the National Housing Act, may be made if it is within the regular lending area.

Realty in Urban Renewal Areas[255]:

A. These loans may be made on the same terms as outlined in Sections I, II and III except

1. Loans on "other dwelling units" and "other improved real estate" may be made up to 80 percent of value and for a term of 30 years (instead of 75 percent and 24 years)
2. The term of construction loans is increased to a 60-month maximum (from 36 months)

Exhibit 4: Housing Opportunity Allowance Program (12 C.F.R. 527)

Introduction: The Housing Opportunity Allowance Program as formulated by the Home Loan Bank Board is based on Title I of the *Emergency Home Finance Act of 1970* (Public Law 91–351), which provides funds to be dispersed to Federal home loan banks for the purpose of adjusting the effective interest charged

[253] 12 C.F.R. 545.7.

[254] 12 C.F.R. 545.8.

[255] 12 C.F.R. 545.6–18.

by such banks on borrowing to promote the flow of funds into residential construction. It is especially designed to assist in the provision of housing for low and middle income families: i.e., to help them purchase their own homes.

Middle Income Families: An eligible borrower will receive $20 per month to be credited toward interest to be charged on each of the first 60 monthly installments paid on a qualifying loan. An eligible borrower is:

- either or both spouses of a married couple living together, or head of household with dependent children;
- current adjusted annual income is not in excess of applicable maximum limits prescribed by the Home Loan Bank Board from time to time;
- has need of a housing opportunity allowance to warrant the making of a qualifying loan by a member institution.

A qualifying loan is:

- for a single family dwelling which is the primary residence;
- secured by a first lien on the property;
- is not an insured or guaranteed loan;
- the principal must be between 70 percent and 100 percent of the value of the property or the purchase price, whichever is smaller; and in any case not more than $25,000;
- the effective interest rate must be as approved by the Board;
- a monthly installment loan of 25-30 years;
- borrower must pay monthly to lender half of the established annual taxes, assessments, and insurance premiums on the secured property.

Low Income Families:

- A qualifying loan has the same characteristics as for middle income families.
- An eligible borrower has the same characteristics as for middle income families.
- An eligible borrower receives interest payments based upon his current adjusted annual income expressed as a percentage of the applicable Home Opportunity Allowance Program limits as prescribed by the board, and as determined at the time of approval of such borrower's application or at the time of recertification, pursuant to the following table;

Adj. annual income as percent of HOAP limits	Allowance for ea of 1st 60 paymts.	Allowance for ea of 2nd 60 paymts.	Total allowance
65 to 65.7	$25	0	$1500
63 to 64.9	30	0	1800
61 to 62.9	35	0	2100
59 to 60.9	40	20	3000
57 to 58.9	45	25	4200
54 to 56.9	50	30	4800
52 to 53.9	55	35	5400
50 to 51.9	60	40	6000
40 to 49.9	65	45	6600
39.9 and under	70	50	7700

- After the first 60 payments, the borrower must be recertified to determine whether he is still eligible and which income category he is in.

Exhibit 5: Mortgage Insurance (207(c)(3)

Introduction: Following are the amounts prescribed under Section 207(c)(3) of the National Housing Act (12 U.S.C. 1713(c)(3)) which, if exceeded, limit Federal savings and loan associations to 20 percent of their assets in making loans secured by apartments.

Regular Structures

$9,900	per family unit w/o bedroom
13,750	one bedroom
16,500	two bedrooms
20,350	three bedrooms
23,100	four or more

Elevator Type Structure

$11,550
16,500
19,800
24,750
28,050

Trailer Courts or Parks

$2,500 per space
$1,000,000 per mortgage

The Secretary of HUD may increase these amounts up to 45 percent in any geographical area where he finds the cost level so requires.

Exhibit 6: The New Communities Act of 1968 (82 Stat. 513); The Urban Growth and New Communities Development Act of 1970 (84 Stat. 1791)

These Acts are intended to encourage the development of newly built communities or major additions to existing communities by providing up to $500,000,000 in total for guaranteeing loans with a limit of $50 million per development program.

To be eligible for such assistance, the new community development program must meet such criteria as: 1) Provide an alternative to disorderly urban growth by so improving general and economic conditions in existing communities as to help reverse migration from existing cities or rural areas; and 2) make substantial provision for housing within the means of persons of low and moderate income and that such housing will constitute an appropriate proportion of the community housing supply.

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