# CONGRESSIONAL BUDGET OFFICE
# COST ESTIMATE

January 28, 2016

## H.R. 3700
### Housing Opportunity Through Modernization Act of 2015

*As ordered reported by the House Committee on Financial Services*
*on December 9, 2015*

## SUMMARY


H.R. 3700 would amend the United States Housing Act of 1937 to change certain aspects of the Department of Housing and Urban Development's (HUD’s) rental assistance programs. The bill would alter calculations of tenant income and rent; make households that exceed new income and asset limits ineligible for assistance; change requirements for adjusting payment standards; and expand eligibility for the Family Unification Program. The bill also would make changes to Federal Housing Administration (FHA) requirements that affect whether buyers of certain condominiums would be eligible to receive mortgage insurance from the agency.

CBO estimates that implementing this legislation would reduce spending subject to appropriation by $311 million over the 2017-2021 period, assuming appropriations are consistent with the estimate.

Enacting H.R. 3700 would not affect direct spending or revenues; therefore, pay-as-you-go procedures do not apply. CBO estimates that enacting H.R. 3700 would not increase net direct spending or on-budget deficits in any of the four consecutive 10-year periods beginning in 2026.

H.R. 3700 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).


## ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary effect of H.R. 3700 is shown in the following table. The costs of this legislation fall within budget functions 370 (housing) and 600 (income security).

| | By Fiscal Year, in Millions of Dollars | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | 2020 | 2021 | 2017-2021 |

**CHANGES IN SPENDING SUBJECT TO APPROPRIATION**

| | 2017 | 2018 | 2019 | 2020 | 2021 | 2017-2021 |
|---|---|---|---|---|---|---|
| **Changes to Allowances** | | | | | | |
| Medical Expense Allowance | | | | | | |
| Estimated Authorization Level | -144 | -201 | -211 | -223 | -236 | -1,015 |
| Estimated Outlays | -79 | -175 | -207 | -218 | -230 | -909 |
| Childcare Allowance | | | | | | |
| Estimated Authorization Level | -36 | -49 | -50 | -51 | -53 | -239 |
| Estimated Outlays | -20 | -43 | -49 | -51 | -52 | -215 |
| Elderly and Disabled Allowance | | | | | | |
| Estimated Authorization Level | 66 | 88 | 88 | 105 | 105 | 452 |
| Estimated Outlays | 36 | 78 | 88 | 97 | 105 | 404 |
| Dependent Allowance | | | | | | |
| Estimated Authorization Level | 34 | 46 | 46 | 71 | 71 | 268 |
| Estimated Outlays | 19 | 41 | 46 | 60 | 71 | 237 |
| **Eligibility Changes** | | | | | | |
| Asset Eligibility | | | | | | |
| Estimated Authorization Level | 10 | 13 | 14 | 14 | 14 | 65 |
| Estimated Outlays | 6 | 12 | 14 | 14 | 14 | 59 |
| Income Limit in Public Housing | | | | | | |
| Estimated Authorization Level | 8 | 10 | 11 | 11 | 12 | 52 |
| Estimated Outlays | 4 | 9 | 11 | 11 | 11 | 46 |
| **Income Determination Changes** | | | | | | |
| Aid and Attendance Exclusion | | | | | | |
| Estimated Authorization Level | 6 | 6 | 6 | 6 | 6 | 30 |
| Estimated Outlays | 3 | 6 | 6 | 6 | 6 | 27 |
| Imputed Return on Assets | | | | | | |
| Estimated Authorization Level | 2 | 3 | 3 | 3 | 3 | 14 |
| Estimated Outlays | 1 | 2 | 3 | 3 | 3 | 12 |
| **Other Housing Assistance Provisions** | | | | | | |
| Payment Standard for Rent | | | | | | |
| Estimated Authorization Level | 24 | 24 | 25 | 26 | 27 | 125 |
| Estimated Outlays | 13 | 24 | 25 | 25 | 26 | 113 |
| Expansion of the Family Unification Program | | | | | | |
| Estimated Authorization Level | 4 | 6 | 5 | 5 | 6 | 27 |
| Estimated Outlays | 2 | 5 | 6 | 5 | 6 | 24 |
| Moving Assistance | | | | | | |
| Estimated Authorization Level | 1 | 2 | 2 | 2 | 2 | 8 |
| Estimated Outlays | 1 | 1 | 2 | 2 | 2 | 7 |

(Continued)

**TABLE CONTINUED**

| | By Fiscal Year, in Millions of Dollars | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | 2020 | 2021 | 2017-2021 |
| **Changes to FHA Insurance Requirements**[a] | | | | | | |
| Additional FHA Offsetting Collections | | | | | | |
| Estimated Authorization Level | -25 | -23 | -21 | -20 | -18 | -107 |
| Estimated Outlays | -25 | -23 | -21 | -20 | -18 | -107 |
| Additional GNMA Offsetting Collections | | | | | | |
| Estimated Authorization Level | -2 | -2 | -2 | -2 | -2 | -10 |
| Estimated Outlays | -2 | -2 | -2 | -2 | -2 | -10 |
| **Total Changes** | | | | | | |
| Estimated Authorization Level | **-52** | **-77** | **-84** | **-53** | **-65** | **-331** |
| Estimated Outlays | **-41** | **-64** | **-80** | **-68** | **-58** | **-311** |

Notes: FHA = Federal Housing Administration; GNMA = Government National Mortgage Association.

Components may not sum to totals because of rounding.

a. Using the fair-value approach, CBO estimates that implementing H.R. 3700 would decrease offsetting collections generated by FHA and GNMA by $117 million over the 2017-2021 period, assuming appropriation actions to allow FHA to increase the amount of mortgage guarantees it provides by an amount sufficient to meet the increased demand for mortgage guarantees under the bill. As shown in the table, using a FCRA approach, CBO estimates that implementing H.R. 3700 would increase offsetting collections generated by FHA and GNMA by $117 million over the 2017-2021 period.

## BASIS OF ESTIMATE

For this estimate, CBO assumes that H.R. 3700 will be enacted by the end of fiscal year 2016, spending will follow historical outlay patterns, and future appropriations will be consistent with the bill. The bill would require the changes to income determinations and allowances to take effect at the start of a calendar year; CBO expects that those changes would take effect beginning in January 2017. In cases where the tenant rent contribution would change, CBO assumes that appropriations will be adjusted to reflect the costs of such changes. In addition, CBO assumes that these changes would not affect the funding requirements for about 350,000 public housing or voucher units covered by Moving-to-Work agreements because those public housing authorities (PHA) are funded pursuant to their agreements, rather than the standard administrative formulas.

### Background

Almost 5 million households receive assistance through HUD's various rental assistance programs, including the Section 8 Housing Choice Voucher program, public housing, and other project-based subsidy programs. To be eligible for assistance, family income must be below either 50 percent or 80 percent of the area median income, depending on the program. Each program has a minimum percentage of families receiving assistance who must be below 30 percent of the area median income.

Tenants who receive assistance generally pay 30 percent of their adjusted monthly income towards rent. Funding from HUD covers the difference between what the tenant pays and the full rent for the unit (up to certain limits). In the case of public housing, HUD provides PHAs with operating and capital funding that allows them to subsidize rents.

Families participating in HUD's rental assistance programs have their incomes certified when they enter the program and at least annually thereafter in most cases. Current law allows various adjustments to income (called allowances) prior to calculating a family's rent payment. Families may deduct certain child care expenses and elderly and disabled households may deduct any medical expenses that exceed 3 percent of income. In addition, households may deduct $400 from gross income if they include an elderly or disabled member, and all households may deduct $480 for each dependent. As a result of these deductions, the average adjusted income is approximately 8 percent lower than the average gross income.

**Changes to Allowances**

This bill would change how allowances are used to lower income to determine housing assistance; on net, CBO estimates that implementing these provisions would reduce outlays by $483 million over the 2017-2021 period, assuming appropriation actions consistent with the bill.

**Medical Expense Allowance.** Elderly and disabled families can currently deduct the amount of unreimbursed medical expenses that exceed 3 percent of the family's income. Based on data provided by HUD, CBO estimates that 16 percent of families claim an average allowance of $1,900 each (for a total of $1.3 billion). The bill would decrease the amount of medical expenses that can be deducted to the amount that exceeds 10 percent of the family's income. CBO estimates that this change would cut the number of families claiming medical expenses by 40 percent and the total amount claimed by about 45 percent. CBO estimates that implementing that provision would reduce discretionary spending by $909 million over the 2017-2021 period.

**Child Care Allowance.** Families may deduct any child care expenses necessary to enable a member of the family to be employed or attend school. Section 102 would only allow families to deduct child care expenses that exceed 5 percent of their annual family income. Based on data provided by HUD, CBO estimates that about 4 percent of families (about 160,000) claim child care allowances of about $3,300 each. CBO estimates that implementing the new child care allowance would reduce outlays by $215 million over the 2017-2021 period.

**Elderly and Disabled Allowance.** Section 102 would increase the amount that can be deducted by elderly and disabled households from $400 to $525, and would inflate that amount each year, rounded down to the nearest multiple of $25. Based on data provided by HUD, CBO estimates that this deduction is claimed by just over half of households receiving assistance. About 1 percent of families claiming the allowance would not see any additional benefit from the increase because their adjusted incomes are already at zero. CBO estimates that increasing the elderly and disabled allowance would cost $404 million over the 2017-2021 period.

**Dependent Allowance.** The bill also would increase the amount that can be deducted for dependents from $480 to $525, and would inflate that amount each year, rounded down to the nearest multiple of $25. Based on data provided by HUD, CBO estimates that this allowance is currently claimed for about 3.7 million dependents. About 9 percent of families claiming the allowance would not see any additional benefit from the increase because their adjusted incomes are already at zero. CBO estimates that increasing the dependent allowance would cost $237 million over the 2017-2021 period.

**Eligibility Changes**

H.R. 3700 would affect how household income and assets are used to target assistance. On net, CBO estimates that implementing these provisions would increase outlays by $105 million over the 2017-2021 period, assuming appropriation actions consistent with those provisions.

**Asset Eligibility.** Section 104 would make households with more than $100,000 in assets ineligible for assistance, but would leave the enforcement of this provision up to the discretion of the PHAs and property owners. Assets in retirement accounts would be not be subject to the asset limit. Based on data provided by HUD, CBO estimates that about 9,000 families would become ineligible for assistance under the bill. Because there is unmet demand for participation in HUD's rental assistance programs, CBO expects that families made ineligible would be replaced by families on housing authority waiting lists. Replacing those newly ineligible families (who have higher than average incomes) with families with average income would cost the government an additional $1,500 per family in 2017. CBO estimates that implementing that provision would cost $59 million over the 2017-2021 period.

**Income Eligibility.** Under current law, families with income over 80 percent of the area median income at their initial certification are not eligible for assistance. Eligibility tests are not done after the initial certification (most incomes are certified each year to determine a tenant's rent contribution); therefore, a family's income can rise above 80 percent of the area median and the family can continue to receive assistance. Section 103 would require PHAs to terminate assistance for households in public housing whose income exceeds

120 percent of the median for two consecutive years. Alternatively, the PHA could charge the household the market rent for their unit.

Based on data provided by HUD, CBO estimates that approximately 2,100 households that reside in public housing would lose their subsidy. Because there is unmet demand for participation in HUD's rental assistance programs, CBO expects that families made ineligible would be replaced by families on waiting lists maintained by housing authorities. Replacing those newly ineligible families with families with average income would cost the government an additional $4,900 per family in 2017. CBO estimates that implementing that provision would cost $46 million over the 2017-2021 period.

**Income Determination Changes**

Section 102 would require PHAs and property owners to change the way they calculate income for determining housing assistance. In total, those changes would increase spending subject to appropriation by $39 million over the 2017-2021 period, assuming appropriation of the necessary amounts.

**Aid and Attendance Exclusion.** Section 102 would exclude federal pensions of veterans who receive Aid and Attendance (A&A) from the calculations of adjusted income. Doing so would reduce affected veterans’ rent contributions, thereby increasing the cost of HUD’s assistance payments. Based on data from the Government Accountability Office, CBO estimates that about 6 percent of households receiving assistance include a veteran. Based on information from the Department of Veterans Affairs, CBO estimates that less than 1 percent (about 1,600) of those households include a veteran receiving A&A and that those payments average about $16,000 per year. Excluding those amounts from calculations of adjusted income would lower tenants’ rent contributions by about $6 million per year (once fully phased in). CBO estimates that implementing that provision would cost $27 million over the 2017-2021 period.

**Imputed Return on Assets**. Under current law, housing authorities and property owners calculate a tenant's imputed rate of return on any assets over $5,000 by using an interest rate determined by HUD. If the imputed return on assets is greater than actual income from assets, the imputed return is included in the family's income. Section 102 would increase the threshold for calculating imputed returns to $50,000. Based on data provided by HUD, CBO estimates that about 1 percent of families (about 40,000) have imputed income from assets that would be excluded from their total income under the bill; asset income counted for determining housing assistance would decrease by about $8 million per year. CBO estimates that excluding the imputed return on assets with a value of less than $50,000 would cost $12 million over the 2017-2021 period.

## Other Housing Assistance Provisions

**Payment Standard for Rent.** Under current law, PHAs generally must set a payment standard that is between 90 and 110 percent of the fair market rent. The standard, in combination with a household's income, determines the amount of the housing assistance payment (HAP) that the PHA pays to the landlord. If the fair market rent in an area decreases, a PHA that has set its payment standard at 110 percent would have to decrease the HAP. Section 107 would allow a PHA to maintain the HAP at the prior year's amount when the fair market rent in an area decreases. Based on data from HUD, CBO estimates that implementing this provision would cost $113 million over the 2017-2021 period.

**Expansion of the Family Unification Program.** Section 110 would make adults ages 22 to 24 who left foster care after age 16 eligible for Family Unification Program vouchers. Under current law, only adults ages 18 to 21 who left foster care after age 16 are eligible for those vouchers. In 2015, the Congress appropriated about $6 million for that program. Based on information from HUD, the department of Health and Human Services, and studies on outcomes of adults that were previously in foster care, CBO estimates that the Family Unification Program served about 0.4 percent of eligible adults in 2015. Assuming that the program serves the same proportion of eligible adults ages 22 to 24 and adjusting for anticipated inflation, CBO estimates that implementing that section would cost $24 million over the 2017-2021 period.

**Moving Assistance.** Under current law, voucher payments that are withheld because a unit failed inspection are retained by the PHA; HUD's future payments to the PHA are then reduced by the amount withheld. Section 101 would allow PHAs to use voucher payments that are withheld because a unit failed inspection to pay for the relocation costs of the tenant that occupies the unit. Based on data provided by HUD and information provided by PHAs, CBO expects that about 1,000 households would receive assistance to move each year and that PHAs would provide about $1,500 per household. Thus, CBO estimates that implementing this provision would cost $7 million over the 2017-2021 period.

## Changes to FHA Insurance Requirements[1]

H.R. 3700 would change certain requirements that determine whether buyers of condominiums are eligible for FHA mortgage guarantees. The bill would reduce the amount of units in a condominium complex that must be owner occupied to qualify for an

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1. The budgetary effects of guarantees by FHA and the Government National Mortgage Association (GNMA) are classified as discretionary because new guarantees under those programs are subject to annual appropriation actions. Under current law, the budgetary effects of these activities are calculated under the Federal Credit Reform Act (FCRA). As required in S. Con. Res. 11, the Concurrent Resolution on the Budget for Fiscal Year 2016, CBO has also prepared a cost estimate for this section of H.R. 3700 using a fair-value approach to estimating the impact on FHA and GNMA. That alternative is discussed under the heading, "Additional Information."

FHA guarantee from 50 percent to 35 percent. The bill also would eliminate a prohibition on providing FHA guarantees for units that are subject to certain fees that are assessed to owners who sell their condominiums.

Based on information provided by FHA and industry representatives, CBO estimates that implementing H.R. 3700 would increase offsetting collections generated by FHA and the Government National Mortgage Association (GNMA) by $117 million over the 2017-2021 period, assuming appropriation actions to allow FHA to increase the amount of mortgage guarantees it provides by an amount sufficient to meet the increased demand for mortgage guarantees under the bill. That estimate also accounts for uncertainty regarding administrative actions that may be taken by FHA under current law.

**Additional FHA Offsetting Collections.** CBO estimates that, over the 2017-2021 period, implementing H.R. 3700 would increase offsetting collections for FHA's single-family program by $214 million. Those additional offsetting receipts would stem from an increase in the volume of FHA loan guarantees. The increase in the volume of guarantees would occur because changes to FHA rules under the bill would allow additional condominium buyers to qualify for FHA guarantees.

CBO estimates that under current law FHA will guarantee about $1 trillion in new mortgages over the 2017-2021 period. We estimate that, over the same period, enacting H.R. 3700 would increase mortgage guarantees from FHA's single-family program by roughly $8 billion—an increase of about 0.75 percent. The combination of guarantee fees charged by FHA and estimated defaults and mortgage prepayments over the next five years yields an estimated average subsidy rate for FHA's guarantees of -2.7 percent.[2] Multiplying that subsidy rate by the additional volume of mortgage guarantees expected to be offered by FHA under the bill would result in additional estimated offsetting collections of $214 million over the 2017-2021 period. Because CBO estimates that there is a 50 percent chance FHA will make similar rule changes under current law, we estimate that new offsetting collections under the bill would total $107 million over that period.

**Additional GNMA Offsetting Collections.** Through its Mortgage-Backed Securities (MBS) program, GNMA is responsible for guaranteeing securities backed by pools of mortgages that are insured by federal agencies such as FHA. In exchange for a fee paid by lenders or issuers of the securities, GNMA guarantees the timely payment of scheduled principal and interest due on the pooled mortgages that back those securities. Because the value of the fees collected by GNMA is estimated to exceed the cost of loan defaults in each year, CBO estimates that the GNMA MBS program will have an average subsidy rate of -0.28 percent over the 2017-2021 period, resulting in net receipts collections to the federal government.

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2. A negative subsidy cost for a federal credit program can occur if the net present value of upfront and annual fees charged for a loan guarantee are greater than the estimated cost of a default on that loan.

CBO estimates that each year about 90 percent of the new mortgage loan guarantees made by FHA would be included in GNMA’s MBS program. We also estimate that changes in FHA’s requirements for loan guarantees on condominiums under the bill would increase FHA’s loan-guarantee volume by $8 billion over the next 5 years. Multiplying 90 percent of that amount by the subsidy rate (-0.28 percent) results in additional offsetting collections by GNMA’s MBS program totaling $20 million over the 2017-2021 period. Because CBO estimates that there is a 50 percent chance that FHA will make similar rule changes under current law, we estimate that implementing the bill would increase offsetting collections from GNMA’s MBS program by $10 million over that period.

## ADDITIONAL INFORMATION

This section provides additional information on the estimated effects of title III of H.R. 3700 on the fair-value costs of the FHA single-family, FHA multifamily, and GNMA programs. CBO is required to provide this information by S. Con. Res. 11. Under current law, the costs of those programs are measured in the budget according to the procedures established in the Federal Credit Reform Act (FCRA).

The fair-value approach is an alternative to the approach specified in FCRA. Both the FCRA approach and the fair-value approach rely on the same projections of future cash flows for the guarantee programs, and both approaches take into account the lifetime cost of the new guarantees made in a given year (including the expected cost of defaults, net of fees collected). The fair-value estimates differ from the FCRA estimates by recognizing that the government’s assumption of financial risk has a cost that exceeds the average amount of losses that would be expected from defaults. In practice, the main difference between FCRA estimates and fair-value estimates is the discount rates used to calculate the present value of estimated future guarantee costs and receipts.

Using the fair-value approach, CBO estimates that implementing H.R. 3700 would decrease offsetting collections generated by FHA and GNMA by $117 million over the 2017-2021 period, assuming appropriation actions to allow FHA to increase the amount of mortgage guarantees it provides by an amount sufficient to meet the increased demand for mortgage guarantees under the bill. Using a FCRA approach, CBO estimates that implementing H.R. 3700 would increase offsetting collections generated by FHA and GNMA by $117 million over the 2017-2021 period.

**PAY-AS-YOU-GO CONSIDERATIONS**: None.

## INCREASE IN LONG TERM DIRECT SPENDING AND DEFICITS

CBO estimates that enacting H.R. 3700 would not increase net direct spending or on-budget deficits in any of the four consecutive 10-year periods beginning in 2026.

## INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 3700 contains no intergovernmental or private-sector mandates as defined in UMRA. State, local, and tribal governments would benefit from housing assistance activities authorized in the bill. Any costs those governments incur to comply with grant requirements would result from conditions of federal assistance.

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