Pennsylvania Housing Finance Agency Act of 1972

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The gap between available safe and sanitary private housing for low- and moderate-income families and the demand for such units has persisted over several decades. It was only in the late 1950's, however, that individual states began not only to recognize the problem, but to respond to the crisis. Pennsylvania's Housing Agency Act of 1959 was the first legislative response to the perceived need for state intervention in private sector housing development.

This early legislation acknowledged the critical shortage of low-priced homes in Pennsylvania. While builder disinterest in low-cost housing ventures contributed to the gulf between supply and demand, the problem was exacerbated by major urban renewal programs in the business districts of Pittsburgh and Philadelphia, which resulted in the displacement of many center-city citizens.

State lawmakers viewed financing as the major hurdle to development of new low- and moderate-income housing. Private finance institutions were unwilling to invest in these high-risk projects without a greater opportunity for profit, especially when large profits could be made through industrial and commercial property development investments. Federal financing was proposed as a solution, but it was not conducive to the goals of the state legislators, because the only direct federal subsidy programs at that time were for public housing. The legislature implicitly understood that there were financial, social, and political limits to the use of public housing to alleviate the housing shortage. Pennsylvania legislators finally conceived a new venture involving both public and private

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2 The Pennsylvania Housing Agency Act, No. 621, [1959] Pa. Laws 1688. While states have long recognized the need for local participation in public-owned housing through local housing authorities, the concept of state financial support or incentives for private residential construction was first advanced in this legislation. Art I, § 102, [1959] Pa. Laws 1688-90.


financial sources. Since it was assumed that private industry could and would supply the needed housing if "market and financial conditions warrant[ed] greater expenditure of private capital," the legislature concluded that there was a need for both state financing and creation of incentives for private industry to enter the low- and moderate-income housing field.

The 1959 Pennsylvania legislation, while commendable for its goals and its innovative financing concepts, proved inadequate over the years in meeting the changing housing needs in the state. In an attempt to correct the deficiencies of this legislation, Pennsylvania radically revised its housing law by enacting the Housing Finance Agency Act of 1972.

This note undertakes a historical analysis of both the 1959 Act and the 1972 Act. Then, the new act is contrasted with similar statutes in other states. Finally, the effectiveness of the Pennsylvania legislation as a stimulate to the development of new low- and moderate-income housing is critically analyzed.

I. LEGISLATIVE HISTORY

A. The 1959 Housing Agency Act

The 1959 Housing Agency Act created the Pennsylvania Housing Agency, a public corporation empowered to accept grants and subsidies from federal and state sources, to create additional working capital through sale of bonds, to purchase, service, and sell insured mortgages, and to make direct loans on the security of the insured mortgages. The agency's primary activity, lending its available funds, was directed toward assisting low- and moderate-income families to become homeowners and, to a lesser extent, financing construction of cooperative and elderly multi-unit family housing.

Agency loans were available only to a restricted class of eligible mortgagors. With respect to single-family homes, only the potential homeowner was eligible. Nonprofit housing ownership cooperatives and

13 Art. II, § 205, [1959] Pa. Laws 1692. Also included in this section are many powers commonly granted to any corporate operation, such as the power to use a corporate seal, the capacity to enter into all necessary contracts, and the power to sue or be sued.
14 Summary of the Pennsylvania Housing Agency Amendments, a memorandum of the Pennsylvania Department of Community Affairs, May 1, 1972, on file in the Pennsylvania Legislative Research Bureau Library, Harrisburg, Pa.
15 Art. III, § 301(4), [1959] Pa. Laws 1664. The mortgagor not only had to be the purchaser, he also had to occupy the dwelling personally. The mortgagor's income could be no higher than the "highest annual income level in the middle third of nonfarm family annual incomes as classified by the agency ...." Id. § 301(4)(ii). Moreover, the applicant's financial resources had to be judged insufficient to finance a purchase of an approved dwelling unit through normal credit channels. Id. § 301(4)(iii).
certain organizations sponsoring housing for the elderly were the only eligible mortgagors for multi-unit dwellings.

The loans were designed to attract potential purchasers of private housing by offering mortgage interest rates below the lowest prevailing market levels. The reduced interest rate resulted from issuance of the loan at the highest going market rate, and then reduction of that rate by use of a "reduced-interest rider." The rider thus served to entice mortgagors. However, special provisions allowed the Pennsylvania Housing Authority to terminate the reduced-interest rider if the mortgagor did not deal in good faith with the agency or did not comply with the conditions of the loan. In such cases the loan was not called, but the rider was removed, thereby returning the interest rate to the original market level. The funds for these Agency loans were to come from tax-free revenue bonds, issued by the Agency as a public corporation of the state though not backed by the credit of the state.

These were the major substantive provisions of the 1959 legislation. While the state was initially optimistic, believing the program would achieve the desired ends, by 1970 it was apparent that the Pennsylvania Housing Agency legislation had proven ineffectual. The legislation passed in 1959 was not actually implemented until 1971, and as of 1972, no bonds or notes had been issued by the Agency. Furthermore, while the state’s General Assembly appropriated over two million dollars to the Pennsylvania Housing Agency, this expenditure and the efforts of the Agency through 1972 assisted only forty-nine families.

Problems in the Act doomed it to failure, but changes in national housing policy were also needed before such legislation could be effective. A few of the problems with the structure and content of the Act can be singled out for analysis.

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23 See Summary of the Pennsylvania Housing Agency Amendments, supra note 14, at 1.
26 Id. at 1.
27 See notes 29-46 and accompanying text infra.
28 See notes 47-53 and accompanying text infra.
B. Problems of the 1959 Act

1. Focus on Homeownership—The 1959 Act was designed primarily to assist families who wanted to purchase homes of their own. Although the sponsors of the bill did not explicitly state the rationale for this limitation, many believe the aspiration to homeownership is a goal common to a majority of Americans at all income levels. This view may have led to the omission of rental units, except those for the elderly, from the 1959 legislation.

In the intervening years, however, Pennsylvania legislators and agency administrators recognized that promoting homeownership could not be the sole answer to the low-income housing problem. Most low-income families eligible for assistance were unfamiliar with homeownership as a living experience. The long-term commitment and the responsibility for taxes, maintenance expenses, and monthly mortgage payments were burdens that many were unable to assume. Furthermore, a substantial percentage of families enjoy and prefer rented over purchased housing.

2. Restrictions on Eligible Mortgagors—Agency loans were limited to the purchaser of the home or, if the structure were owned on a cooperative basis, to a nonprofit cooperative housing association. The Act contained no provisions for loans or advances to builders or developers of proposed low-cost houses, and thus there was little incentive for them to participate in the Agency programs. The risks were too great and the expected return too small for builders and developers to use their own venture capital or to borrow funds from commercial lenders to finance the construction. Conversely, the low-income purchaser was not prepared, either in terms of skill or finances, to become involved in the construction process. The limitation on eligible mortgagors, therefore, had an adverse effect on low-cost housing production under the Pennsylvania Housing Agency program.

3. Financing Limited to Dwelling Units—A related problem was the absence of any “project” concept. The Act provided that mortgage loans could be granted only for dwelling units. The statute overlooked the need for site development, land for park and playground areas, and land for access and easements. The necessity for ancillary structures such as

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30 Homeownership was the professed aspiration of a cross-section of families in the Detroit area. See Sengstock, *Homeownership: A Goal for All Americans*, 46 J. URBAN 317 (1969). Sengstock’s survey of nonhomeowners in Detroit indicated that 59 percent of those sampled desired to own a home. *Id.* at 322.

31 Id. at 341-349.

32 Id.

33 See note 15 supra.


community service, maintenance, and management buildings was also unrecognized. Nor were provisions made for street, sewer, and power services. While this defect was probably not of major importance in mortgage loans on single detached houses, it served to reduce the value of assistance given under Agency programs for multi-unit housing.

4. Loans Allowed Only on Insured Mortgages—The Agency could lend against only insured mortgages. Insured mortgage lending protected the Agency’s financial stability, but the requirement produced adverse results by severely limiting the number of loans which could be made and substantially increasing the processing time for those loans. FHA-mortgage insurance was available for some applicants, but the long processing periods and the numerous qualifications and requirements imposed upon the applicant may have deterred many potential mortgagors. Private insurance was difficult to obtain, often too expensive, and sometimes its terms were incompatible with the income limits for mortgagors under the Agency programs.

5. Unsatisfactory Bonding Provisions—The 1959 Act contained sections authorizing the Pennsylvania Housing Agency to issue tax-free revenue bonds. As of 1972, no such bonds had been issued. It is possible that the tax-free provisions were defective in the original Act; the tax-free provisions were defective in the original Act;

37 Id.
38 Truslow, State Housing Agencies Roles and Accomplishments, in DEALING WITH STATE HOUSING AGENCIES—THE EMERGING FORCE IN DEVELOPMENT, 66-68 (C.Edson ed. 1973) [hereinafter cited as STATE HOUSING AGENCIES]. Thirty-four months is the average processing time for HUD-insured units. Id.
39 Id.

40 One advantage of private insurance would be the possibility of lower Agency interest rates, since the Agency would not have to bear the risk of loss due to bad loans. However, because low-income housing is typically considered a very high risk insurance item, the insurance premiums demanded by private insurers could more than offset the lower interest rates.
42 Alexander, supra note 24, at 12.

43 Although the Pennsylvania Housing Agency was a public corporation, it was not a typical “political subdivision” whose bonds are exempted from taxes. See INT. REV. CODE of 1954, § 103(a)(1). The authority for the proposition that the Agency’s bonds were tax exempt, in 1959, was tenuous at best. In Commissioner of Internal Revenue v. White’s Estate, 144 F.2d 1019 (2d Cir. 1944), cert denied, 323 U.S. 792 (1945), Judge Augustus Hand held that the New York Triborough Bridge Authority was a “political subdivision,” although its bonds were obligations of the Authority and not of the State. The court emphasized, however, that the Bridge Authority was organized to operate a “public improvement.” The court also considered the Authority to be the alter ego of the city and so inextricably tied to the city that there was no merit to the Tax Commissioner's argument that since the bonds were only obligations of the Authority, they should not be exempted. The Tax Commissioner argued strenuously for this point, and it is probable that the Pennsylvania Housing Agency’s status and its questionable “public purpose” may have been enough of a distinction to cast doubt on the Agency’s tax-exemption provision.

Revenue Ruling 60-248 also did not help. Rev. Rul. 60-248, 1960 CUM. BULL. 35. The ruling took the position that the New York Housing Finance Agency bonds were “issued on behalf of the State” and were tax-free. However New York assumed full responsibility for the debts of its housing agency and the New York pattern can thus be distinguished from Pennsylvania’s potential liability. The lack of definitive ruling on the status of the Pennsylvania agency’s bonds may have been a controlling reason for their inability to issue bonds for the Agency.
if they were not defective, other inadequate sections\textsuperscript{44} and a lack of any state backing for the undertaking\textsuperscript{45} might have caused the investing public to view any bond issue with healthy skepticism.\textsuperscript{46}

6. Lack of Federal Support—The greatest obstacle to effective implementation of the program, however, was the lack of direct or indirect federal support. Federal programs in 1959 were geared for either higher income mortgagors, through FHA and VA mortgage insurance,\textsuperscript{47} or extremely low-income families, through federally subsidized public housing.\textsuperscript{48} Not until the early 1960's did federal programs respond to the housing problems of those with incomes in between.\textsuperscript{49} The tax laws were unclear both in their treatment of agency activities such as the issuance of tax-free revenue bonds\textsuperscript{50} and in regard to the taxability of revenue produced from reserves held by the Agency.\textsuperscript{51} Furthermore, few financial incentives existed either in the tax code\textsuperscript{52} or in the housing programs themselves\textsuperscript{53} to encourage builders and developers to enter this field.

Viewed in light of these problems, it is not difficult to understand the reasons for the stagnation of the Pennsylvania Housing Agency programs. Corrective legislation was necessary to revive the Act.

II. THE 1972 HOUSING FINANCE AGENCY ACT

A. Factors Prompting Enactment

Several stimulants provided the impetus for necessary changes in the 1959 Pennsylvania Act. The most important of these was passage of federal housing programs which were beneficial to state housing goals. The Housing and Urban Development Act of 1968,\textsuperscript{54} through its Section

\textsuperscript{44} Although a capital reserve fund was authorized in Art. V, § 508, [1959] Pa. Laws 1704, the statute left in doubt the plight of creditors if the fund proved inadequate to pay outstanding principal and interest on bond obligations. Bondholders were given some limited rights and remedies but these were not a truly satisfactory guarantee. \textit{See Art. V, § 512, [1959] Pa. Laws 1706.}


\textsuperscript{46} \textit{See Pennsylvania Department of Community Affairs, Questions and Answers Regarding the Pennsylvania Housing Finance Agency Bill, S.B. 1407, at 9 [hereinafter cited as Questions and Answers].}


\textsuperscript{49} The Section 221(d)(3) (Below Market Interest Rate) program was passed in 1961. Pub. L. No. 87-70 tit. I, § 101(a), 75 Stat. 149 (1961), as amended 12 U.S.C. § 17151 (d)(5) (1970). For a discussion of Section 221(d)(3) see Prothro & Schomer, \textit{The Section 221(d)(3) Below Market Interest Rate Program for Low and Moderate Income Families}, 11 N.Y.L.F. 16 (1965). In several ways the Section 221(d)(3) program was the predecessor of the Section 235 and 236 programs. \textit{See} notes 54-61 and accompanying text infra.

\textsuperscript{50} \textit{See note 43} supra.

\textsuperscript{51} The belief that tax-free bond revenue was being abused led to the 1969 amendment to the Internal Revenue Code which denied "arbitrage bonds" immunity from taxation. \textit{Int. Rev. Code of 1954}, § 103(d).

\textsuperscript{52} \textit{See} notes 63-66 and accompanying text infra.

\textsuperscript{53} \textit{See} notes 54-60 and accompanying text infra.

and Section 236 programs, furnished the financial assistance necessary for the state agencies to become viable. These programs provide direct "periodic interest reduction payments," on behalf of the homeowner or cooperative (in the 235 program) and on behalf of the owner of the rental project (in the 236 program), to the mortgagee for approved loans financing low- and moderate-income housing. Furthermore, these programs allow such payments to be made "under a State or local program providing assistance through loans, loan insurance or tax abatements...." Thus, a state housing agency could be the mortgagee who made the project loans and received the interest reduction payment. The federal assistance payments made it possible for the state programs to reduce substantially the amount of interest charged the mortgagor, thereby providing housing within the means of people in a wide range of income brackets.

Section 202 of the same Act authorized rent supplements to certain low-income families living in sub-standard housing. These rent supplements also complement state programs and can be "piggy-backed" on Section 236 subsidies to reduce rent even further, thereby making it possible to provide good private housing for people at lower income levels.

In addition, new income tax provisions were passed which, in combina-

55 12 U.S.C. § 1715z (1970). The Section 235 program provides assistance to lower income families in acquiring homeownership or membership in a cooperative housing association project.
57 In both programs the interest reduction payments from the federal government to the mortgagee are designed to reduce the amount of interest the mortgagor must pay to the equivalent of a 1 percent annual interest rate or 20 percent of the mortgagor's annual income, whichever is less. The program drafters estimated that maintenance costs for such housing should run around 5 percent of the owner's (or renter's) gross income, so that the low-income mortgagor under the 235 program and the low-income renter under the 236 program would presumably pay no more than 25 percent of their income for housing.
61 See Alexander, supra note 24, at 9, 12. As Alexander explains, the Section 236 interest reduction payments lower the project cost to the owner, as does the state agency loan, which carries a lower-than-market interest rate. In turn, the rental project owner must decrease the rent as required by his agreement with the agency. The Section 202 payment is paid to the owner on behalf of the low-income renter, reducing what is actually paid in rent.
tion with other provisions of the code, supplied incentives for investors and developers in the state housing programs. First, for the investor in the Agency revenue bonds, any doubts as to the tax-free status of the bonds were dispelled by new provisions in Section 103 of the Internal Revenue Code. The section specifically exempted from taxation the income from bonds of public housing corporations, such as the Pennsylvania Housing Financing Agency, even though such bonds might otherwise fit into industrial development bond or arbitrage bond categories. Clarification of the tax-exempt status of the bonds obviously enhanced their marketability and increased the capital-raising ability of the Agency.

Second, for the builder or developer, the tax code made tax shelters available by permitting use of accelerated depreciation, nonrecognition of gain, and deductibility of mortgage interest.

A final factor prompting change in the 1959 Act was the success of New York's housing program under its Housing Finance Agency. New York's accomplishments illustrated to the authorities and the investing public the great potential of state housing finance agencies. The New York program was instituted in 1960, one year after the Pennsylvania law. The New York agency, however, was given more extensive and flexible powers, and it flourished while the Pennsylvania program stagnated. The New York law was compatible with the new federal housing programs. In fact, the achievements of the New York agency and a few others may have prompted inclusion in the Section 235 and Section 236 programs of the clause specifically mentioning state programs.

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62 See note 43 supra.
63 INT. REV. CODE of 1954, § 103(c)-(d).
64 Two major depreciation deductions are now available to developers. Under Section 167(j), applicable to taxable years after 1969, most real property is no longer eligible for the double declining balance method of depreciation. Excluded, however, is new residential rental property, which includes low-income housing projects. Also, Section 167(k) provides for a sixty-month depreciation period for capitalization expenditures to rehabilitate low-income rental housing. Id. § 167(j), (k).
65 Under Section 1039, any gain on the sale of a low-income, 235 or 236 housing project is not recognized if the developer sells to an authorized tenant cooperative group or other similar nonprofit organization in a sale approved by HUD and within a certain time reinvests the gain in the construction or rehabilitation of another such project. Id. § 1039.
66 INT. REV. CODE of 1954, § 163.
68 See Morris, The Development of New Middle Income Housing in New York, 10 N.Y.L.F. 492 (1964).
70 See note 133 and accompanying text infra.
71 PA. HOUSING FINANCE AGENCY ANN. REP. 8 (1973). See also Summary of Pennsylvania Housing Amendments, supra note 14, at 1.
72 The other two state housing finance agencies in existence at that time were the Massachusetts Housing Finance Agency (Mass. ANN. LAWS ch. 708, (Vol. 10, Special Selected Laws 466-76) (1966), as amended, (Supp. 1972)) and the Michigan State Housing Development Authority (Mich. COMP. LAWS ANN. § 125.1401 et seq. (1967), as amended, (Supp. 1973)).
73 See note 58 and accompanying text supra.
B. Provisions of the 1972 Act

The new Pennsylvania law, enacted in 1972, is an attempt to achieve, to some degree, the extensiveness and flexibility found in the New York law and in later housing finance agency laws of other states. The 1972 Act reflects both the necessity for changes in the old programs and the need for legislation responsive to and compatible with the federal housing and tax laws.

First, the 1972 Act recognizes the importance of rental housing units in Pennsylvania's housing program. The revised act consolidates the loan program into the Housing Purchase Program, which covers loans to private and cooperative housing sponsors, and the Rental Housing Program, which covers loans for housing projects developed by eligible mortgagors and rented to low- and moderate-income families. Both programs have deleted the prior requirement for FHA mortgage insurance as security for the loan.

The 1972 Act also expands the eligible class of mortgagors or sponsors, enabling a builder or developer to take advantage of Agency loans. Furthermore, in a very important provision, the Act limits dividends or profits which the eligible mortgagors may distribute, and, by doing so, it qualifies the projects for federal assistance under Section 236 of the Housing and Urban Development Act of 1968.

The new law also expands the permissible uses of loan funds. Loans

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75 See notes 29-46 and accompanying text supra.

76 See notes 52-53 and accompanying text supra.

77 The Act asserts the need for "rental units for persons and families of low and moderate income" in its findings on the housing needs of Pennsylvania. The wording change, made in numerous sections, from "homes" to "housing" indicates philosophical shift away from strict adherence to single detached private dwellings as the program's goal. PA. STAT. ANN. tit. 35, § 1680.102 (Supp. 1973).


80 The statutory provision that covers the Housing Purchase Program does not specifically require mortgage insurance, but Agency rules may provide for it in certain cases. PA. STAT. ANN. tit. 35, § 1680.301A (Supp. 1973). The rental housing program authorizes loans secured by real property, a lease-hold estate, or mortgages insured by the FHA. The Agency's 1973 financial statement states, however, that all present mortgage loans "are insured by the Federal Housing Administration." PA. HOUSING FINANCE AGENCY ANN. REP., supra note 71, at 18. These loans may be carryovers from the old Pennsylvania Housing Agency organization which required FHA insurance.

81 The term "eligible mortgagors" now includes "individuals, joint ventures, partnerships, limited partnerships, trusts, corporations, cooperatives and condominiums, whether nonprofit or organized for profit." PA. STAT. ANN. tit. 35, § 1680.103 (Supp. 1973).

82 PA. STAT. ANN. tit. 35, § 1680.402a(c). (Supp. 1973). This provision limits distributed profits to 8 percent of the mortgagor's equity in the project, and therefore qualifies such projects under 12 U.S.C. § 1715z-1(b) (Supp. 1973), which sets forth the limited-dividend requirement for Section 236 projects.

can be made to finance the costs of complete housing projects that now include not only dwelling units but also

acquisition, construction or rehabilitation of lands, buildings, equipment, improvements and other ancillary facilities such as . . . streets, sewers, utilities, parks, site preparation, landscaping, and such ancillary facilities . . . as administrative, community, health, recreational, educational and welfare facilities as the agency determines to be necessary, convenient or desirable . . . .

The Act also authorizes construction loans so that the developer does not have to accumulate all the capital necessary to begin loan processing and construction. Thus, most of the development capital is provided by the Agency, which issues short-term construction loans and exchanges the short-term loans for long-term mortgage loans when the project is completed.

The entire Bonds and Notes section of the 1959 Act has been rewritten in the new Act. Provisions are included to foster investor confidence in these securities and to take advantage of newly enacted federal tax provisions. Furthermore, the bond provisions have been carefully drafted to include the best portions of successful programs such as those in New York and Michigan.

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84 Id. § 1680.103(17).
85 Id. § 1680.402a(a). Construction loans are intended to cover the expenses of project construction and are usually disbursed in periodic allotments to cover each stage of construction, with further funds being contingent on the builder finishing previous stages.
86 Id. § 1680.501a et seq. This section of the Act establishes a general fund for all monies made available to the Agency or received by it as revenue from its housing loans; these funds are available for general Agency purposes. Id. § 1680.503a. Furthermore, a capital reserve fund is created to be used solely to pay off Agency bonds and notes. Id. § 1680.504a. This capital reserve must, at all times, have funds equal to the maximum amount of principal and interest maturing and becoming due on bonds for the next calendar year. Id.
87 As in the 1959 Act, there is a specific provision stating that the bonds do not constitute a debt of the state or any of its political subdivisions, and that the obligations are payable only out of the revenues of the Agency. PA. STAT. ANN. tit. 35, § 1680.502a (Supp. 1973). This provision had led to some doubt about the tax-free status of the Agency's bonds. See note 43 supra. However, the 1972 Act also contains a "moral commitment" clause. PA. STAT. ANN. tit. 35, § 1580.504a(c) (Supp. 1973). This clause does not legally obligate the state to make up any deficiencies, but does require the Governor to submit a report to the General Assembly in any year in which it appears that the capital reserve funds will fall short the required amount. The General Assembly may appropriate funds to make up the difference, although it is not required to do so. Furthermore, the Act specifically delineates the Agency's role as a public one for the benefit of the Commonwealth, "performing an essential governmental function." PA. STAT. ANN. tit. 35, § 1680.506a (Supp. 1973). This language is an additional assurance to investors that Agency bonds properly qualify as tax free under the Internal Revenue Code. See Treas. Reg. § 1.103-1 (1972).
88 The bonds come within the special rules qualification of Section 103(d)(4). This provision allows bond proceeds to be temporarily invested in other securities until the proceeds are needed. During this time, the bonds will remain tax free. INT. REV. CODE of 1954, § 103(d)(4).
More flexible and comprehensive restrictions and supervisory controls supplement the new Agency programs. The low-interest rider concept\textsuperscript{91} was repealed. Now, rather than specifying the mechanics of the interest rate structure, the Act gives the Agency broad discretionary power to fix interest rates on mortgage loans consonant with expenses of the Agency and bond rates.\textsuperscript{92} All sales of project property by mortgagors under the Housing Purchase Program are subject to approval and regulation by the Agency.\textsuperscript{93} In addition, all mortgagors participating in either the rental or purchase program are subject to stringent penalties for violation of the terms of the Agency loan agreement,\textsuperscript{94} including fines and jail sentences for purposeful fraud.\textsuperscript{95} Other violations of loan agreements may precipitate removal of the officers of any corporate mortgagor and their replacement by officers of the state agency.\textsuperscript{96} Corporate mortgagors' distributable profits under the rental housing loan program are restricted.\textsuperscript{97} There are also restrictions on the amount of rental charges,\textsuperscript{98} builder's and developer's profits,\textsuperscript{99} and fees.\textsuperscript{100} All project costs must be certified by the Agency.\textsuperscript{101} A special provision gives the Agency power to differentiate rents, charging higher rents for some units in order to lower rents of others in the same development, "to encourage developments which are not economically homogeneous."\textsuperscript{102} Finally the mortgagor must submit and the Agency must approve a tenant-selection program that meets all equal opportunity standards.\textsuperscript{103}

In making these changes in the 1959 Act, the Pennsylvania legislature intended to transform the Pennsylvania Housing Agency into a model, modern housing finance agency. The statute was built on the evolutionary formation and experiences of housing finance agencies in other states. To understand the potential effectiveness of the Pennsylvania law, it must be compared to housing finance agency statutes of other states.

\textsuperscript{91} See notes 18-20 and accompanying text supra.
\textsuperscript{92} PA. STAT. ANN. tit. 35, § 1680.402(b) (Supp. 1973).
\textsuperscript{93} Id. § 1680.301(b).
\textsuperscript{94} Id. § 1680.602a.
\textsuperscript{95} Id.
\textsuperscript{96} Id. § 1680.401a(4).
\textsuperscript{97} Id. § 1680.402a(c), (d).
\textsuperscript{98} Id. § 1680.402a(e).
\textsuperscript{99} Id.
\textsuperscript{100} Id.
\textsuperscript{101} Id. § 1680.402a(h).
\textsuperscript{102} Id. § 1680.403a. Although the statute does not clarify the mechanics of this procedure, if the Agency follows the procedures used in other states, the differentiation will work as follows. The project is built at reduced cost to the sponsor because of the low-interest Agency loan and the HUD assistance. The savings, however, is not prorated equally among the units, but rather certain units are set at market prices and others at various lower levels, thus presumably ensuring an economic cross section of tenants.
\textsuperscript{103} PA. STAT. ANN. tit. 35, § 1680.404a (Supp. 1973). The statute also contains a nondiscrimination provision. Id. § 1680.404a(a).
III. A COMPARATIVE ANALYSIS OF LEGISLATIVE EFFORTS IN OTHER STATES

A. State Housing Finance Agency Legislation

Since the enactment of the initial Pennsylvania legislation in 1959, there has been a remarkable increase in the creation of state housing finance agencies, indicating state concern and affirming state responsibility for today's housing problems. In 1960 only two states, New York and Pennsylvania, had housing finance programs, and even these differed in scope. They can be considered the forerunners of the modern Housing Finance Agency and remained the only operable programs for six years. Not until 1966 did other states, appreciating the potential benefits of such an enterprise, begin to enact similar legislation. From two state housing finance agencies in 1960, the number of such entities multiplied to eight in 1968 and to thirteen in 1970. By mid-summer of 1973, twenty-three states had initiated programs and several more agencies have been proposed.

An examination of the various state programs reveals a startling similarity in basic concepts, goals, and operative provisions. The states

104 The New York program included more than housing financing. For an explanation of the numerous aspects of the New York plan see Morris, supra note 68, at 492. See also notes 67-72 and accompanying text supra.


106 See Alexander, State Housing Finance Agencies Face Difficult Problems During Housing "Freeze" and Pending Federal Housing Re-evaluation, 30 J. HOUSING 120, 122 (1973).


108 See State Housing Agencies, supra note 38, at 47; Alexander, supra note 106, at 120, 122. Ohio has such a proposal pending in the state legislature at this writing. Governor's Housing & Community Development Advisory Commission, Legislative Report No. 2, Feb., 1972. Other states have agencies with more limited powers, but many of these agencies are acquiring more expanded powers characteristic of the modern housing finance agency. See also State Housing Agencies, supra note 38, at 48-49.

seemingly recognized the necessity for compatibility with federal programs and therefore modeled their programs after the earlier and now successful ones in New York, Michigan, and Massachusetts, which successfully complemented the federal programs. Funding and implementation powers, however, do vary from state to state and this variance could be the difference between success and failure for any particular housing finance agency. Several important factors should be considered.

B. Characteristics of State Housing Finance Agencies

1. Funding Authorization—Approximately half of the states with housing finance agencies, including Pennsylvania, grant their agencies unlimited bonding authority. Other states have agency bonding limits ranging from $20 million to $2 billion. There seems to be a positive statistical relationship between successful programs and higher bonding capacity. If latter supplementary state authorization is needed, considerable delay and political opposition may develop; this perhaps explains the observed correlation.

2. Construction Loans—Most housing finance agencies can make loans to cover costs incurred during project construction. To the extent that such loans allow builders to begin construction and development of these projects with smaller amounts of their own capital, there is a greater incentive for builders to enter the program and an earlier project completion date.

3. Seed Money—One disincentive, which tends to discourage developer participation in agency programs, is the prospect of the developer’s sustaining substantial precommitment expenses without ultimate assurance of loan approval. To counter this disincentive, seed money grants are provided by some states. These grants cover much of the potential developer’s expenses prior to agency approval of his project. It is not clear whether developers will get seed money grants under the new Pennsylvania law.

4. Mortgage Insurance—While a few housing finance agencies still restrict mortgage loans to FHA-insured mortgages, most states have eliminated this requirement. The complexity of the federal application process, the time required to get approval, and the additional restrictions on

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113 See Alexander, supra note 106, at 122.  
114 Id.  
115 See STATE HOUSING AGENCIES, supra note 38, at 47-49.  
116 See Alexander, supra note 106, at 122.  
117 Id.  
118 Pennsylvania’s law, while not specifically giving seed money grants, has been interpreted to authorize such grants. See Alexander, supra note 106, at 122. However, the language of the act does not appear to support this conclusion. See PA. STAT. ANN. tit. 35, §§ 1680.301a, 1680.401a (Supp. 1973).  
119 See Alexander, supra note 106, at 122.
federal projects are the most important reasons for this change. A state housing finance agency can protect itself through a scrupulous and thorough application and approval process. The state application process has numerous advantages over the federal process, the foremost advantage being the reduced processing time. While the processing period may be two or three years for federal programs, it is six to eight months for the typical state housing finance agency. The states’ relatively fast processing time is made possible by the smaller size of the state agency, its proximity to the potential site, and the more personal contact between agency officials and developers.

The advantages and disadvantages of mortgage insurance are widely debated. While mortgage insurance might allow the agency to lower the interest rates charged, dependence on such insurance, especially if it is FHA insurance, might result in lax administration and approval of questionable housing projects. One alternative to FHA insurance is insurance supplied by the state housing agency. However, at present, only a half dozen state agencies are authorized to provide state mortgage insurance, and most of these programs are unfunded.

5. Subsidy Administration—The Section 235 and Section 236 federal subsidies have become an essential ingredient of housing programs for low- and moderate-income families. Of the twenty-three operating agencies, fourteen administer Section 236 program funds. Only six housing finance agencies have participated in the Section 235 program. The degree to which the state housing finance agencies are independent of HUD offices varies. All state agencies must negotiate with the regional HUD office for their “adjusted fair share” of HUD subsidies, and these negotiations may lead to some HUD control over the local agency’s portion. Nevertheless, some states, such as Michigan, have obtained essentially a block grant of their portion of HUD funds and use these funds in their programs without being subject to HUD control. Generally, the greater the independence of the state agency, the greater its flexibility in utilizing the funds.

6. Land Acquisition—Some housing finance agencies have land acquisition power. This power increases the Agency’s ability to make land

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120 See State Housing Agencies, supra note 38, at 271. This reprint of the Illinois Housing Finance Authority Manual gives the details of the application process in Illinois. These procedures are similar to those followed by most state housing finance agencies.
121 See State Housing Agencies, supra note 38, at 211.
122 Id. at 122-23.
125 See Alexander, supra note 24, at 14-15.
126 See Alexander, supra note 106, at 122-23.
127 Id.
128 See Alexander, supra note 24, at 11. For the authoritative explanation of this process see HUD HANDBOOK 4530.1, NON-INSURED ASSISTED PROJECTS BY STATE AND LOCAL GOVERNMENTS, Feb. 6, 1973.
129 See Alexander, supra note 106, at 122.
130 See Alexander, supra note 24, at 13.
available that might otherwise be unattainable by the participating private developer. At the same time, this power can be exercised in politically unpopular ways, thus bringing the Agency into conflict with local authorities and utilimately adversely affecting the agency's operation. Land acquisition power, therefore, has significant drawbacks, at least at this time.132

7. Results—The Pennsylvania agency's operations, as evidenced by its 1973 Annual Report, are still in the formative stage and offer no insight into its future successes or failures. The results of efforts by similar state housing finance agencies, however, provide some grounds for optimism.133 Between January 1, 1969, and March 1, 1973, the eleven housing finance agencies then operational had financed 90,587 housing units at a total project cost of $2.64 billion.134 These statistics indicate that housing finance agencies, created through a combination of state and federal legislation, have achieved in a short timespan a viable and effective program for development of needed private low and moderate-income housing.

IV. THE FUTURE OF STATE HOUSING FINANCE AGENCIES

Pennsylvania's present housing finance agency law reflects the changes which state housing agencies have undergone in the last decade. The defects and strictures that made prior state housing agencies and programs unworkable have given way to new, flexible programs involving both the private and public sectors and properly balancing the different interests of each sector. The advantages of the organizational structure created by the new act compare favorably with those of other housing finance agencies.135 Barring any extraordinary or unforeseen difficulties, the Pennsylvania Housing Finance Agency should perform as well as similar bodies

131 New York's Urban Development Corporation (UDC), the agency counterpart to the state housing finance agency that handles the actual development of low-income housing projects, was given land acquisition powers, including the power to override local zoning ordinances. Turning from urban areas to the suburbs in the last three years, the UDC asked nine middle-income suburban communities to accept 900 units of housing. The localities responded with vigorous lobbying and, in May, 1973, succeeded in having the UDC stripped of its override powers. TIME, Oct. 1, 1973, at 97. Cf. Note, Judicial Review and Discrimination in Federally Assisted Housing: The Enforcement of Title VI, 7 U. MICHE. J. REFORM 135 (1973).
132 No state has successfully implemented a land acquisition program integrated into the state housing finance program. Alexander, supra note 106, at 122.
133 Under Michigan's program, over $200 million in bonds have been issued, 6,000 multifamily units have been completed, and 7,000 units are in the process of completion. Under the Illinois program, $55 million of bonds and $21 million of notes have been issued, 3,550 units have been completed and 4,000 are in various stages of completion. Under the New York program, $3 billion in bonds have been issued since the New York agency began operations, and over 60,000 units have been completed. QUESTIONS AND ANSWERS, supra note 46, at 3.
134 Truslow, supra note 38, at 65.
135 See part II supra.
136 See part III supra.
in such states as Michigan,\textsuperscript{137} Massachusetts,\textsuperscript{138} and New York.\textsuperscript{139} The success of the Pennsylvania agency depends on its ability to surmount the ominous problems facing all housing finance agencies in the near future.

\textit{A. Current Housing Finance Agency Problems}

Despite current optimism, certain forces still threaten the future of state housing finance agency programs. The foremost threat is reduced federal financial support, as illustrated by the present partial suspension of federal subsidy funds, the real possibility of complete termination of these funds in the near future, and the apparent stalemate between the Administration and Congress over the proper role of the federal government in achieving the goal of "a decent home and a suitable living environment for every American family."\textsuperscript{140} Until the federal government resolves this impasse, the fate of the housing finance agencies is unclear.

A second and related problem is the inflated cost of land acquisition and housing construction.\textsuperscript{141} Given the present upward spiral of housing costs, there is a distinct possibility that, even with HUD subsidies at their present levels, the housing finance agencies will be unable to help even moderate-income families to obtain decent housing.


\textsuperscript{140} On January 5, 1973, the Nixon Administration announced that Section 235 and Section 236 program funds were suspended. There was an immediate halt to any new commitments under these programs. See 119 Cong. Rec. S1408 (daily ed. Jan. 19, 1973) (Budget Message of the President for Fiscal Year 1974). See also 1973 Cong. Q. 40, for a more explicit examination of which funds were cut off and congressional response to these actions. On September 19, 1973, the President announced new housing proposals that included a short-term partial revival of Section 236 funds. 119 Cong. Rec. H8070-71 (daily ed. Sept. 19, 1973) (Federal Housing Policy Message from the President). The Administration's long-term program, S. 2507, H.R. 10688, 92d Cong., 1st Sess. (1973), would ask for a total conceptual change from housing subsidies to allowances paid directly to low-income families.

Congress has responded with two bills. The Senate proposal would consolidate the existing programs and retain the Section 235 and Section 236 "production" subsidies. S. 2182, 92d Cong., 1st Sess. (1973). This is the most traditional of the new proposals. The House bill would scrap the existing programs, including Sections 235 and 236, and authorize giving block grants of funds for housing and other community development projects to the cities and states. These funds would be divided within each state to give urban areas three out of every four dollars of the grant money. Funds from block grants would be used locally for such diverse purposes as rehabilitation of older housing, seed money grants, interest-reduction payments, and rent supplements, all of which would be administered by local or state governments. H. 10036, 92d Cong., 1st Sess. (1973).

\textsuperscript{141} As early as 1969, many believed Section 235 subsidies were insufficient to provide housing for anyone with an income under $5,000. See Schafer & Field, Section 235 of the National Housing Act: Homeownership for Low Income Families? 46 J. Urban L. 667, 684 (1969). Moreover, the price of new one-family housing has risen 23 percent between 1967 and 1972. The wholesale price of construction materials rose 19.5 percent during that period and union hourly wages in the building trades were up 44 percent. 1972 Statistical Abstract 677.
The third problem stems from pressure on Congress to change the tax provisions that presently exempt interest from municipal and other public corporate bonds from taxation.\textsuperscript{142} Since the housing finance agencies rely on private investors to purchase their bonds, sufficient revenue can only be obtained if the bonds are financially attractive. Repeal of this tax preference would perhaps place a difficult hurdle in the way of housing finance agency operations.

The final threat relates to the adequacy of the housing produced by the housing finance agencies. There is some dispute as to whether the housing provided really fulfills the goal of supplying decent private housing for low-income families. One study indicates that priorities are misplaced when housing finance agencies concentrate on new construction in suburban areas, while relegating urban and rural construction to a secondary status.\textsuperscript{143} Several agencies now in operation have been reviewing their policies on housing rehabilitation, questioning the effectiveness of their efforts and expenditures.\textsuperscript{144} The ultimate question is whether the states, in the face of reduced federal assistance, can reshape their programs and objectives to meet the most crucial housing needs of the people.

\textbf{B. Recommendations for Change}

The House,\textsuperscript{145} Senate,\textsuperscript{146} and Administration\textsuperscript{147} bills to reshape federal housing policy appear, at first glance, so dissimilar as to prevent any simple compromise. A reconciliation may be possible, however, by looking behind the words to the goals represented by each proposal. The Administration's bill relies on a direct housing allowance and discontinues production programs \textit{(i.e., Sections 235 and 236), but the plan is only tentative.}\textsuperscript{148} Such a concept has never been tried in the housing context, and direct welfare allowances have proved so problem-prone that its successful application is dubious, even to some Administration officials.\textsuperscript{149} The Administration proposal also faces a financing problem. The program would cost $8 to $11 billion a year if it provided "universal entitlement" for all low-income families.\textsuperscript{150} Commentators therefore doubt whether the Administration's proposal is feasible either administratively or finan-


\textsuperscript{143} See Alexander, supra note 106, at 121.

\textsuperscript{144} Id. at 122.


\textsuperscript{146} S. 2182, 93d Cong., 1st Sess. (1973).

\textsuperscript{147} S. 2507, 93d Cong., 1st Sess. (1973).

\textsuperscript{148} Initially only an experimental program would be conducted for a period of eighteen months to determine the feasibility of the concept. S. 2507, 93d Cong., 1st Sess. \textsection 104 (1973). Similar experiments have been underway since 1970 under prior authorization, 12 U.S.C. 1701z-1 (1970).

\textsuperscript{149} See 119 CONG. REC. H8070-71.

cially. Moreover, present conflicts between Congress and the White House may demand compromise by the latter if any program is to be enacted this year.\textsuperscript{152}

The block-grant concept was also given serious consideration by the Administration\textsuperscript{153} and may well be the starting point for consensus. Block grants embody the revenue-sharing and decentralization precepts of the Administration. Under the House proposal,\textsuperscript{154} the block grants would be administered by local government, which would distribute funds under an "overall community development and housing program"\textsuperscript{155} between urban renewal and housing for low-income families. By lowering the cost of HUD administration and allowing the localities to distribute funds as they believe the funds are most needed, this bill counters the White House argument that the present subsidy system is inequitable and too expensive.\textsuperscript{156} The block grant proposal is also more attractive to the Senate, since it contains some of the machinery to continue production programs favored by the Senate.\textsuperscript{157}

A federal policy based on block grants would solidify the state housing finance agencies' position as an appropriate agency to assist the cities in administering block grants. The state agency could work in conjunction with a community development agency in states where these entities are separated. Thus, the only real threat to the survival of state housing agencies is the possibility of a lengthy stalemate between the Administration and Congress.

The problem of inflated housing costs is not easily solved. It is a composite inflation caused by union wage demands,\textsuperscript{158} restrictive and non-uniform building codes,\textsuperscript{159} increased housing material costs,\textsuperscript{160} extremely inflated land costs,\textsuperscript{161} zoning limitations\textsuperscript{162} and the general high demand for housing.\textsuperscript{163} One possible approach to check this inflation

\textsuperscript{152} See 1973 Cong. Q. 40 for the bitter congressional reaction to the January, 1973 suspension of housing funds.
\textsuperscript{153} See Edson, supra note 150, at E-5.
\textsuperscript{155} Id. at H7555.
\textsuperscript{158} 1972 Statistical Abstract 677.
\textsuperscript{159} See State Housing Agencies, supra note 38 at 146.
\textsuperscript{160} See note 141 supra. The rise in construction material prices is a result of both greater builder demand and increased exports. See also 1973 Cong. Q. 2718.
\textsuperscript{161} Time, Oct. 1, 1973, 80. The article observes:
The new land rush has set off an inflation that far outstrips price rises on commodities like food, gasoline and steel. Nationwide, the price of land for industrial parks has tripled in a decade. Suburban residential property has been gaining in value by some 8 percent a year. The average price of the land under a house with a Federal Housing Administration-insured mortgage is now $5,300, up about 80 percent since 1963, while the average plot size has shrunk from about 11,000 sq. ft. in 1965 to 7,000 sq. ft.
\textsuperscript{162} Id. at 94-99.
\textsuperscript{163} Id. at 86.
would be a concentrated and coordinated effort by both state and federal governmental agencies to initiate intensive research and development of alternatives in housing production methods, materials, and designs. Such agencies could also implement state- or area-wide standard building codes and review ineffective labor practices, while proposing measures to remedy these problems. Passage of a block-grant bill would free HUD of some of its current administrative duties, allowing it to concentrate on a national policy of housing research and development.

Consideration should be given to retention of the tax provisions which induce investors to participate in housing finance agency programs, at least until such time as it can be shown that the demand for new housing no longer justifies the incentives. As long as the social goals of the housing finance agencies that issue bonds are considered worthwhile, the incentives that make the program viable should continue until feasible alternatives become available.

Agency housing production will probably always have certain maximum limits. At present the production programs of some state agencies barely keep up with housing abandonments, much less close the housing gap. The size of new housing projects is also limited by neighborhood acquiescence and local government support. Because of these limitations, it is increasingly important that housing finance agencies make the most effective use of their resources to achieve their primary goals. One suggested way to maximize these benefits is to formulate a long range state production program. This program would define where the need for housing is and will be greatest and set priorities for location, housing type, and construction starting dates. Priority of loans and housing agency benefits could then be established on the basis of the plan.

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164 See note 142 and accompanying text supra.
165 Aside from financial limitations, a housing finance agency is restricted in the number of applications which it can process in a year. The housing finance agency application process, while not as lengthy as HUD program applications, nevertheless is a detailed and complicated procedure involving three basic stages: feasibility determination, agency commitment, and an initial closing. There are numerous steps which must be followed within each stage. See STATE HOUSING AGENCIES, supra note 38, at 271. The application process involves many Agency man-hours, and necessarily the number of projects is determined by the size and workload limit of the agency staff. Production capacity can be slightly improved by additions to the staff, but only to a point. See Alexander, supra note 24, at 16. The larger the agency and the greater the number of applications, the more difficult will be the task of maintaining control over all of the stages of project application (processing, development, loan servicing, and management of the project), and the more likely will be the possibility of lax performance.
166 See Alexander, supra note 24, at 16.
167 Id. Nonacquiescence can take many forms. One method used is discussed in Rubinowitz, Exclusionary Zoning: A Wrong in Search of a Remedy, 6 U. MICH. J.L. REFORM 625 (1973).
168 The success or failure of Agency-financed projects may well depend on the degree of cooperation and assistance given by the local government in providing services, lower tax assessments, and similar benefits.
169 See Alexander, supra note 24, at 16-17.
170 Those prospective projects which fit into the production plan would be given first priority. Those ill-suited to the plan or in conflict with the land use objectives would be given the lowest priority.
To implement such a program effectively, the plan would have to be part of a larger and more general land use and development plan for the state, region, or locality. The plan would therefore take into consideration the impact on housing of factors such as industrial location, job creation, commercial service areas, private investment, social services, transportation, and the maximum beneficial utilization of available land. These plans necessarily will entail politically difficult policy choices by the leaders of state governments. Nevertheless, the plans seem indispensable if the states currently opting for the state housing finance agency concept wish to achieve maximum social benefits.

V. CONCLUSION

The Pennsylvania Housing Finance Agency Act of 1972 has remolded one of the older state housing agencies into a model, and potentially successful, housing finance agency with the appropriate powers and resources to act as the mortgage-lender intermediary, bringing public and private capital together for production of much-needed low-income housing. The future, however, holds several serious threats to the success of this state agency. To remove these threats will take the unified support of all states with housing finance agencies. By pressing for the needed legislation at the federal level and by making the necessary reforms in local law to maximize the effectiveness of the state housing finance agency, these states can move closer to the goal of a decent home for all.

—John A. Stevens

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171 See Alexander, supra note 24, at 17. If the house proposal were enacted, H. 10036, 92d Cong., 1st Sess. (1973), its requirement for a community development plan on which to base the allocation of block grant funds would be another force pressuring the localities to implement land use and development plans. See 119 Cong. Rec. H7553 (daily ed. Sept. 5, 1973).