



**REPORT TO CITY COUNCIL
City of Sacramento**

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**Staff Report
June 27, 2006**

Honorable Mayor and
Members of the City Council

Subject: 2006 Public Housing Authority(PHA) Budget Update and the Impact of Revisions to the Public Housing Operating Fund Program.

Location/Council District: All

Recommendation:

This is an informational update to the status of the Agency's 2006 Housing Authority budget. This report also summarizes changes in HUD's Public Housing Operating Fund Program which require major revisions in the management of our public housing properties by October 1, 2006. No action is required on this item.

Contact:

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Presenter:

La Shelle Dozier, Director Housing Operations

Department: Sacramento Housing and Redevelopment Agency

2006 Public Housing Authority Budget Update and the Impact of Revisions to the Public Housing Operating Fund Program

Summary: At its meeting of November 15, 2005, and November 22, 2005 respectively, the Sacramento City Council and Sacramento County Board of Supervisors adopted motions recommending the approval of the 2006 Agency budget including an interim budget for the Housing Authority for the City and County of Sacramento (Housing Authority). In addition, staff proposed to report back in mid year 2006 with a comprehensive plan to address the 2006 shortfall and identify longer term initiatives for financial sustainability.

At the time our 2006 budget was approved, major HUD regulatory changes were proposed for public housing programs nationwide. Agency staff proposed an interim Housing Authority budget until further clarification was available regarding changes to public housing programs being developed at the federal level. Subsequently the Housing Authority received operating subsidy calculation information in early February 2006 from which more accurate revenue projections were developed for Fiscal Year (FY) 2006. While these revenue projections are annualized, for budget purposes, HUD's current financial commitment only extends through June 30, 2006, at which point the operating formula can be extended or changed by HUD.

When adopted, the 2006 Housing Authority budget estimated a \$1.7 million shortfall in our Public Housing and Housing Choice Voucher/Section 8 programs after the reduction of 12.1 vacant positions. This report outlines immediate and long term strategies to address this shortfall.

The 2006 shortfall in our Housing Authority budget will be further increased in the current and future years as we implement HUD-imposed revisions to the Public Housing Operations Fund Program. These revisions require major changes in how we manage our public housing properties and include a phased in reduction of operating funds over the next five years. In order to minimize the financial impact on our Housing Authority programs we must be ready to implement all changes by October of 2006.

Although it is clear that the Housing Authority will receive less funding to operate public housing, our priority is to maintain the same number of units in our total inventory and continue to provide housing to extremely low income residents in our communities throughout the City and County of Sacramento.

Committee/Commission Action: At its meeting on May 17, 2006, the Sacramento Housing and Redevelopment Commission received an informational report on this item.

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Public Housing Authority Demographic Information

The Housing Authorities of the City and County of Sacramento own and operate 3,167 public housing units for extremely low income families, seniors, and disabled persons. Approximately 7,000 extremely low income people live in our public housing units. More details on the demographics of our public housing resident population are summarized in Attachment 1.

Of the total public housing units 65% are in the City of Sacramento, and 35% are in the County (including 93 units in Citrus Heights, 88 units in Rancho Cordova, and 46 units in Elk Grove). We have a diverse housing stock that is geographically dispersed throughout the County and City of Sacramento. Listed below is a breakdown of our housing stock characteristics.

| Complex Size/Characteristics | # of Units | Percentage of Total Housing Stock |
|-------------------------------------|-------------------|------------------------------------------|
| Large Developments (250+ units) | 904 | 28.54% |
| Senior/Disabled High Rise | 564 | 17.8% |
| Mid Size Developments | 1457 | 46% |
| Single Family/Duplexes | 242 | 7.66% |

The Housing Authority is in the process of selling most of our single family units for home ownership to qualifying low income residents; 88 homes have been sold to date and 45 are currently in the rehabilitation and sales process. The remaining 197 homes will be sold through a new homeownership program. The majority of these units are currently occupied.

Asset Based Management

On September 19, 2005, the Department of Housing and Urban Development (HUD) published the final rule on the project-based operating fund program which radically changes the way public housing authorities conduct business. The final rule was based on the Quality Housing and Work Responsibility Act of 1998 (QHWRA) which called on HUD to replace the older funding system with a new operating fund formula. To replace the funding system HUD contracted with the Harvard Graduate School of Design for a cost study. The Harvard cost study recommended that public housing adopt the asset based system that the private sector uses to account for and manage its property. Therefore, the final rule contains two main provisions: it establishes a new formula for determining operating subsidy and it introduces a new business model called asset management.

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Traditionally, the focus in Public Housing has been at the program level. Each housing authority was provided with funds to manage its entire portfolio of physical assets. Under asset based management, the focus is at the property level. Funding will be provided to individual "groupings" of properties. Each property grouping must have their own budget, accounting records, funding, and assigned staff.

The major impact of this change for the Housing Authority is to transition from a centralized to a decentralized operation. This will require the Housing Authority to reorganize and reassign staff to the individual property sites. This reorganization will result in a new way of doing business for the Housing Authority. The management and maintenance service levels are being compared to other non-profit and private sector asset management organizations to determine the most effective organizational structure to complement the needs of public housing developments and the residents we serve.

In addition to transitioning to asset management, the HUD final rule affects the calculation and distribution of operating subsidy or funding. While the final rule outlined the direction HUD was moving in relation to asset management and project based accounting, it did not provide guidance on the funding calculation methodology nor provide Housing Authorities with their actual funding level for 2006. Therefore, during the budget process staff recommended adoption of an interim 2006 Housing Authority budget until the final funding calculations could be accurately developed contingent on guidelines developed by HUD.

On December 28, 2005, HUD published a notice describing the calculation of funding subsidy to Housing Authorities. Although the HUD Final Notice described the procedure for calculating funding for each project, the notice omitted a variety of variables comprising the expense formula that are necessary components of developing an asset management and project based accounting system. HUD issued these variables in early February 2006 from which the Housing Authority has currently re-calculated its 2006 revenues.

Strategies to Address 2006 Housing Authority Budget (Short Term)

The Housing Authority has received the preliminary funding that covers the first half of 2006. Based on this information, we estimate an overall increase of \$598,655 (see Attachment 2) in annual revenues above our original projection to cover the operating expenses. However, this annual estimate is dependent on HUD not changing the funding formula mid year.

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In 2006 we propose to cover the projected shortfall by using the following strategies:

- Salary Savings through Attrition: Holding 12 positions vacant resulting in a savings of \$558,400 in salaries and approximately \$167,520 in associated benefits.
- Rent Increases: Increase of rent revenues where applicable.
- Full Cost Recovery through Fees/Charges: Revision to fees and charges schedule for maintenance service calls
- Vending/Laundry Service Contracts: The Housing Authority has negotiated new vending machine contracts and laundry service contracts.

| Funding Sources | Revenue Projection 2006 |
|----------------------------------------------------|----------------------------|
| Salary/Benefit Savings | \$ 725,920 |
| Full Cost Recovery | \$ 133,081 |
| Washer/Dryer income | \$ 22,163 |
| Interest Income | \$ 1,999 |
| Misc income (vending, surplus material sales, etc) | \$ 21,060 |
| Additional HUD Funding* | \$ 598,655 |
| One Time Fund Expenditures | \$ 202,000 |
| Total | \$1,704,878 |

**Additional HUD Funding based on unchanged operating funding formula*

If necessary, staff will return to Council and Board by September 2006 with recommended strategy to address any remaining shortfall. However, at this time it appears that we have addressed the projected shortfall for 2006.

Strategies to Address Housing Authority Fiscal Issues (Long Term)

In order to address the current and future Housing Authority budget shortfalls, staff has developed a comprehensive and aggressive long-term plan for financial sustainability. The proposed plan outlines the following key initiatives.

1. Develop a real estate reinvestment and disposition strategy

This is the cornerstone of our long term strategy to become fiscally self-sufficient. The Housing Authority is evaluating each property in its portfolio in light of the citywide and neighborhood-by-neighborhood demand for affordable housing for extremely low income families, seniors, and disabled individuals.

While our highest priority is the preservation of our public housing stock, HUD's new rule requires that we assess all properties to determine which units we should

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maintain, develop, renovate, sell, or otherwise reposition within the local market. Many housing authorities such as the Seattle and Vancouver Housing Authorities have strategically repositioned their public housing stock, and that has resulted in an increase in the number of affordable housing units and less dependence on federal funding. We have selected the consulting firm, CSG to assist the Housing Authority in developing a strategic plan to accomplish this goal. They are a nationally recognized firm that has provided assistance to numerous Housing Authorities across the country.

2. Organizational review

A salary study survey is currently being developed, taking into account current job descriptions and whether there is a need to update existing classifications to reflect overall organizational changes and or changes in duties and responsibilities resulting from the HUD mandated asset management conversion. A pilot of the initial organizational study has been launched at two of the sixteen communities. They are located in Oak Park and River Oaks. Staff is meeting with the union and employees' association on the organizational changes to keep them updated on proposed changes and also to obtain feedback in the development of the final structure. Staff will return with specific recommendations on new job classifications and organizational structure.

3. Increase rent revenue for non-public housing units

The Housing Authority will review the rent potential at the project levels and will analyze the ability to generate market rate rents at our non-public housing units by increasing property appeal and/or amenities consistent with market rate units.

4. Implementation of the new software system to increase staff efficiencies

The Housing Authority implemented the new software system in August 2005 for its Housing Choice Voucher (HCV) Program and April 2006 for its Public Housing programs. Staff has already identified operational efficiencies and continues to identify additional efficiencies to become sophisticated users of the new software system. Over time these efficiencies will enable the Housing Authority to effectively manage our HCV and Public Housing programs at reduced staffing levels.

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Financial Impacts of HUD's Revisions to the Public Housing Operating Fund Program

The Operating Fund final rule also reduces the amount of operating subsidy that our Housing Authorities will receive starting in 2007 and phases the reduction over five years conditioned on compliance with certain requirements. By implementing the HUD requirements before the October 1, 2006 compliance date the Housing Authority can achieve the maximum mitigation of revenue reductions for FY2007.

HUD's asset management requirements involve a continuous and ongoing review of the physical, fiscal, and management performance of each property. HUD regulations mandate that a PHA that has not developed the supporting systems to monitor project-level performance and/or has not regularly incorporated the use of that performance data into executive decision-making is not practicing proper asset management and is subject to subsidy reduction and or financial penalty. SHRA must demonstrate substantial compliance with the required project-based management/monitoring system by October 1, 2006, or be subject to a transitional subsidy reduction for each year of non-compliance. That amounts to a reduction of approximately \$500,000 over the five year period.

Projected Deficit for FY2007

HUD intends to implement the new operating fund formula and program in FY 2007, for which the public housing industry estimates a need of \$4.3 billion. However, the President's 2007 budget request is \$3.554 billion, or an estimated 81 percent of the need. HUD has also indicated that in line with the implementation of the asset based management requirement, HUD will also provide additional guidance related to Capital Funding. Preliminary information indicates that HUD will take a restrictive approach and limit the amount of Capital Funds that can be used to cover administrative costs. The President's 2007 budget has also called for reductions in the Capital Fund allocation.

Based on the reductions at the federal level to the operating subsidy, capital fund, administrative fees to operate the HCV program, costs associated with conversion to asset management and increased costs associated with operating our developments, the Housing Authority could face a shortfall of up to \$3 million in 2007, and potentially up to \$4 million in 2008. Therefore, it is imperative that we move aggressively with the long term strategies outlined previously in this staff report to mitigate the projected deficit in future years and ultimately decrease our reliance on federal funding.

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Timeline for Transition

The chart below shows the major milestones the Housing Authority must complete to transition to Asset Management.

| Asset Management Transition Key Events | Completion Date | Status |
|---------------------------------------------------------------------|-----------------------|--------------------------------------------------------------------------|
| Project Grouping Submission to HUD | April 21, 2006 | Submitted to HUD on March 13, 2006- approval pending |
| Implementation of 2 Pilot Asset Mgt Sites (River Oaks and Oak Park) | August/September 2006 | Implemented on June 5 and using data to finalize future site transitions |
| Reorganization Recommendations | July, 2006 | On schedule |
| Staff Asset Management Training | July, 2006 | On schedule |
| Asset Management-Implementation All Physical Sites | September, 2006 | On schedule |
| Full Conversion to Asset Management | October 1, 2006 | On schedule |
| Submit Compliance Documentation to HUD Field Office | October 15, 2006 | Awaiting additional info/training from HUD to submit info |
| New Operating Subsidy Formula Implementation | January 1, 2007 | HUD Deadline |

Environmental Considerations:

This is an informational report so no environmental review is required.

Policy Considerations:

The actions recommended in this report are consistent with previously approved policies and federal requirements.

M/WBE Considerations:

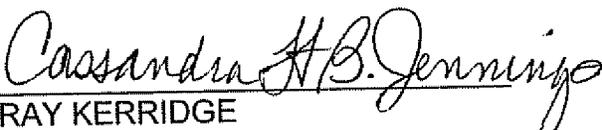
Minority and Women's Business Enterprise requirements will be applied to all activities to the extent required by federal funding.

Respectfully submitted by: _____



ANNE M. MOORE
Executive Director

Recommendation Approved:


for RAY KERRIDGE
City Manager

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