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THE TROUBLED PHA AND TROUBLED PROJECT PROBLEM

By Greg Byrne

In the paper “[Beyond Public Housing](#)”, I argue for converting public housing – all of it – to Section 8, which would benefit residents, public housing agencies (PHAs) and HUD. In this paper, I discuss how the conversion to Section 8 could also be a powerful tool to help solve the long-standing problem of troubled projects and troubled PHAs.

Unfortunately, the public housing program is often defined in the public’s eye by the stories of troubled PHAs that seem incapable of reform. Indeed, some PHAs have been on and off the troubled list for decades. Why is it so hard to turn these agencies around? And why has our track record been so dismal?

Here, I examine HUD’s prevailing practice in dealing with troubled PHAs/troubled projects, why that strategy is flawed, and why conversion to Section 8 can help solve that nagging problem.

A Troubled Strategy

The legal contract between HUD and PHAs is called the Annual Contributions Contract, or ACC. As with other contracts, it spells out both the basic requirements of any PHA and the remedies for default. In the 1990s, concerned that HUD wasn’t doing enough to monitor PHAs effectively and consistently, Congress directed HUD to develop what is now known as the Public Housing Assessment System, or PHAS, where PHAs would be measured on up to 12 indicators and then designated as either High Performer, Standard, Substandard, or Troubled. For any Troubled PHA, HUD must perform a management review and enter into a formal recovery agreement, wherein the PHA must improve its score by 50% within one year and be completely recovered within two years. If a Troubled PHA fails to meet these benchmarks, HUD can take title to the properties, among other actions.

On the face of it, the PHAS program sounds like a reasonable approach to monitoring PHA performance, i.e., new standards have been developed (vacancy rates, rent collections, etc.), new monitoring systems have been implemented, and clear penalties established for non-performance. What, then, is the problem?

First, while the system was updated in 2011 to generate property-specific scores for most indicators, those results are rolled-up into an entity-wide score, which is used to determine

Troubled status. As a result, bad projects, however defined, can get lost or hidden within this entity-wide scoring structure.¹

Second, the PHAS system doesn't incorporate any routine system of on-site management reviews, which is standard practice in HUD's multifamily programs.² Granted, certain key performance data can be ascertained through annual financial statements (e.g., vacancy loss, bad debt, operating expense ratios, etc.), but there's really no substitute, in real estate, for on-site reviews in monitoring management performance.³

But the major problem is less the PHAS system itself as it is the long-standing belief in needing to save the organization – the PHA – and preventing it from failing. The goal of any recovery effort, then, is to help repair the organization, mostly via various forms of technical assistance, from providing new board training to adopting new personnel policies. Not surprisingly, this approach leads to a focus on process and elaborate recovery agreements, with interim goals and timeframes, which rarely are met and often just extended.

This goal of trying to solve the PHA organizational problem stands in sharp contrast to HUD's approach in its multifamily programs. There, HUD has a much clearer mind-set, which is that it is the responsibility of the owner to maintain the project in good repair and to correct any problems identified. In the case of breach or substantial breach, the owner is notified of the condition to correct, and the timeframe for correction, after which, if improvement is not made, HUD will, among other remedies, either take possession of the property and install new management or terminate the Section 8 contract. HUD might suggest to a private Section 8 owner certain actions to take, but HUD would never think to provide a private owner or management company with technical assistance to install, say, better accounting systems or develop improved preventive maintenance procedures.⁴ The focus is much more on the performance of the asset. As necessary, management can be replaced and contracts can be terminated.

This aversion, in the case of substantial PHA default, to installing new ownership or management has both political and structural origins.

¹ Unfortunately, there is also no organized effort to track performance of individual projects year-over-year.

² HUD proposed such a system in 2008 as part of a change to the PHAS system but then dropped that proposal in 2011 amid concerns over (1) a lack of resources and capacity to implement on-site management reviews and (2) scoring subjectivity. At that time, it indicated that it would continue to work to develop a more objective management review tool, which has yet to be implemented.

³ I do not advocate, however, spending any significant administrative resources to substantially re-work the PHAS system at this time. I would prefer that the Department put all its energies into moving public housing over to Section 8. The reforms in this paper will greatly help deal with the troubled PHA/troubled project problem in the interim. See concluding paragraph.

⁴ I'll concede that, even in multifamily programs, HUD performs more hand-holding for small project owners and/or non-profit owners, particularly in the area of subsidy billing. That said, there is a world of difference in the two approaches to contract monitoring.

- **Political.** Although PHAs are quasi-public bodies that are not a direct arm of city hall, a failure of the agency is often perceived as a reflection on city leadership, creating pressure to, again, fix the organization rather than replace it, particularly since any change in management or ownership means a loss of public jobs (although generally not a loss of overall jobs to the community).
- **Structural.** In the early years of the public housing program, there really were no other affordable housing providers for HUD to turn to in the case of substantial default. HUD was pretty much stuck with the PHA. Who was HUD going to find to take over? Fortunately, for at least half a century now, there has been no shortage of capable affordable housing sponsors. But while the assisted housing marketplace has grown dramatically, there are still few affordable housing operators *who understand the unique requirements of public housing*. Public housing is a program unto itself, one that is exceedingly difficult to penetrate from the outside. Moreover, if HUD were to assign a public housing project to a capable affordable housing sponsor, what is the funding (the subsidy) that would come along with the project? Up until very recently, there was no project-level funding to grab. All public housing funding was at the entity level. HUD would need, essentially, to extract funding from the agency and assign it to the new management or ownership entity and there was no accepted methodology for doing that. Moreover, even if HUD were to find a way to assign such funds to the new management or ownership entity, that entity would still have to get its funds each year through the PHA, i.e., there was no way no way for HUD to assign the funds directly the alternative entity, which made such arrangements even less appealing to any capable entity wanting to take on the troubled property.

It is not surprising, therefore, that there has been far less stomach to replace the management or ownership in the case of PHA non-performance than in multifamily housing and, instead, to try to salvage the organization, as fraught as that exercise is.

An Alternative Route

But this problem can be readily remedied if public housing assets were converted to Section 8 upon a declaration of substantial default, which would suddenly open up a whole universe of entities that know how to own and manage Section 8 housing. Then, if a PHA cannot perform the basic responsibility of ownership, HUD won't feel as compelled to save or preserve the PHA as an organization.⁵ The interests of the residents, and the property, can predominate and HUD can approach any troubled public housing project as it approaches any troubled multifamily project, where the PHA would be given a satisfactory period to correct the conditions, after which HUD could take possession of the asset,

⁵ But do PHAs perform some other larger planning function that must be preserved? Not really. At various points in the program's history, it was considered that PHAs would perform municipal-level housing planning tasks. But those ideas never materialized. Today, with few exceptions, PHAs are really just operators of housing assistance, no different than other non-public operators of housing assistance.

convert to Section 8, and turn the property over to a capable sponsor.⁶ In fact, solving the structural problem will help with the political problem in that it will be easier to remove or intervene at the project level.

Under this new approach, HUD could, during the period of time that a project first appears on its watch list, be making the determination of whether the economics of the project are such that a new ownership entity can turn the project around (and refinance the property, as needed) or whether the project is in such bad shape that it should be closed down and the residents issued vouchers. And, as part of HUD's takeover, HUD would then have the authority (as permitted under the ACC) to abrogate all labor contracts, if necessary.

And what if the entire public housing inventory at a particular PHA needed to be taken over, i.e., not just some isolated assets? How would HUD avoid getting bogged down in the morass of organizational issues? HUD would simply replicate the process described earlier for each property. A PHA should be viewed as simply a collection of assets, each with its own subsidy contract. Like Lego blocks, the assets could be readily pulled apart, converted to Section 8, and the ownership or management assigned accordingly. There would be no need to attempt to fix the organization because there would be no need to preserve the organization. Each asset would be assigned to capable operators, which is all that HUD should be concerned with.

Obviously, these powers should only be reserved for substantial default. But, like all effective programs of enforcement/discipline, it is the real threat of remedial action that shapes behaviors.

Implementation Concerns

Other than the obvious cultural shift for HUD, there are three major challenges in standing up such a new approach to dealing with troubled PHAs and troubled projects:

- **The first is whether HUD's Office of Public and Indian Housing (PIH), which oversees the public housing program, has the requisite skills and knowledge to implement such an "asset-based" program.** No doubt, the public housing program over the years has been run more like a social program than a real estate operation. As a result, PIH field personnel don't have the same expertise in troubled project workouts as their multifamily counterparts. But's that just a function of systems and training. I'm not saying it will be easy, but it can be overcome. Also, the good news is that HUD has recently begun testing these waters at a couple of troubled PHAs.

⁶ Comparatively, HUD actually has more remedial authority over PHAs than Section 8 PBRA owners. Under the public housing ACC, HUD can take title to the property. In Section 8 PBRA, except for temporary possession, HUD has no authority to take title. It can terminate (and even transfer) the Section 8 contract, and it can seek other penalties, but it cannot take title.

- **The second is what to do with troubled projects requiring substantial redevelopment.** It's one thing to transfer the asset away from a PHA when there has been bad management but the property is otherwise still viable. But what about projects that need to be redeveloped? Will HUD be ready to step in and make appropriate redevelopment decisions? Should the property be rehabbed or torn down? Should the assistance be transferred elsewhere? What's in the best interests of the residents and the community? And what is the source of funding to pull these plans off? If HUD takes over, it then has to make these determinations, which, understandably, is something that it prefers to leave to local PHAs. But here is where HUD has to be willing to bite the bullet. It has to say to PHAs, "We want you to make these decisions. But if you fail to perform, and if you fail to exercise proper stewardship, we will come in and make those decisions for you." HUD can't just sit back.⁷
- **The third is to make it easier for HUD to immediately convert troubled projects from public housing to Section 8.** How might HUD convert a troubled property today to Section 8? Of course, projects could be converted under the Rental Assistance Demonstration (RAD) program, but that would require an application, a financing plan submission, and other steps. And, some troubled projects would likely qualify for Section 18 obsolescence, which would result in the issuance of Section 8 tenant protection vouchers (TPVs) that could be project-based, if appropriate. In other words, HUD could still likely get there within existing program rules, but it would be a bit of a work-around. It would be far preferable if HUD had clear and immediate authority to convert any troubled project to Section 8 following a declaration of breach.⁸

Arrested Development?

To the extent that the entire public housing program eventually converts to Section 8, does the troubled project/troubled PHA problem go away? Is this, then, just a short-term problem and we will grow out of it? Well, yes and no. Indeed, as projects convert, they will be monitored like other assets in our affordable housing programs, which is to say that the focus will be entirely on the project and not on the organization. PHAs, as ownership entities, will be indistinguishable from any other sponsors of affordable housing, with oversight and enforcement at the project level, where it should be.

⁷ The first priority, obviously, is the protection of existing residents. If the project does not provide decent, safe, and sanitary housing, HUD could require that all residents be relocated with Section 8 vouchers and that the project be removed from the public housing program, after which it is no longer HUD's concern what is done with the property, other than to ensure that any disposition is done for fair market value or, provided there is commensurate public benefit (as defined by program rules), for less than market value.

⁸ It's possible that HUD may already have this authority under the ACC or under other statutory authority, which would be worth more exploration.

But even in the most ideal scenario, full conversion of the public housing program is still many years away and HUD cannot afford for bad projects to linger. Consequently, the troubled project/troubled PHA problem will be with us for a little longer. During this interim period, converting troubled projects to Section 8, and transferring the management or ownership to other capable sponsors, offers a better strategy than trying to recover them through the public housing program.

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