Policy Brief

periodic analyses of issues before the Legislature

LAO

A Review of the Governor's Housing Initiative

In order to facilitate legislative consideration of the Governor's Housing Initiative, this policy brief reviews the proposal's characteristics, identifies the likely beneficiaries, and reviews the fiscal effects associated with implementing the proposal. The brief also identifies five key policy choices that this initiative presents to the Legislature.

Introduction

In January 1990, the Governor announced a $2 billion home loan initiative to increase home ownership opportunities for first-time homebuyers. In March, two legislative measures were introduced to establish part of the program. (These measures are identified in Figure 1.) In the following analysis we describe the Governor's proposal, identify the likely beneficiaries, discuss its fiscal effects, and identify the policy choices which this proposal presents to the Legislature.

What Is the Housing Initiative?

The initiative is comprised of two programs that will be administered by the California Housing Finance Agency (CHFA).

Expands an Existing Program. The first part of the Governor's initiative is a five-year, $1 billion expansion of CHFA's *existing* single-family home loan program. (Although the Governor has not proposed legislation to increase CHFA's debt limit to facilitate this $1 billion program expansion, the administration indicates that the increase in debt limit proposed by AB 1277 (Hauser) would be sufficient for at least the first two or three years of the initiative.) This program provides below-market rate mortgages to first-time homebuyers who meet certain income and home purchase price restrictions. CHFA finances this program by selling federal and state tax-exempt revenue bonds and repays the bonds with mortgage payments collected from program recipients.

Under federal tax law, there is a predetermined cap (about $1.5 billion for California in 1990) on the volume of private activity bonds which the state and local governments may issue on a tax-exempt basis each year. The Governor is proposing to statutorily reserve $400 million of this amount — plus any future increases in the federal bond cap — for expansion of CHFA's single-family home loan program. Currently, the California Debt Limit Allocation Committee (CDLAC) decides which of many competing programs (including CHFA's) obtain a share of these bonds.

Creates a New Program. The second part of the Governor's initiative is a new $1 billion loan program which would provide both (1) below-market rate mortgages and (2) low-interest deferred-payment second mortgages. (These second mortgages would reduce the amount which households must borrow for their primary mortgage. Homeowners would put off repaying these second mortgages for 30 years or until they sell or refinance their homes.) As Figure 2 shows, *a key difference between this program and CHFA's existing program is that households would be permitted to earn higher incomes and purchase more expensive homes than under the existing program.*

The administration proposes to finance this program by selling $1 billion in *federally taxable*, state tax-exempt bonds. About $800

Figure 1

Bills Related to the Initiative

AB 4236—Nolan	Permanently reserves $400 million of federal bond cap—plus all growth in the cap—for CHFA's single-family program.
SB 2870—Maddy	Establishes new CHFA program by amending the Cal-First program of 1982.

Overall, the Governor's housing initiative is likely to benefit small (one- to three-member) households of moderate and above-moderate incomes.

million of these bonds would be revenue bonds, repaid by program recipients. About $200 million of these bonds would be state general obligation bonds, repaid by the General Fund. None of these bonds would be subject to the federal bond cap. The state general obligation bonds would be made available by revising the "Cal-First" housing bond program (Ch 320/82 — AB 3507, Young) and submitting the revision to the voters for approval in the November 1990 election.

Who Benefits From This Initiative?

Existing Program. The administration projects that expanding CHFA's existing program will assist 10,000 to 12,000 households over the next five years. This program helps households save about $50 to $100 per month in housing costs, depending on the cost of the home and other factors.

Because the initiative does not propose any changes to the program's eligibility criteria, we expect that future beneficiaries will resemble current beneficiaries. Figure 3 shows that CHFA granted 47 percent of its loans in 1988-89 to individuals and families earning "moderate" incomes and 42 percent to households with above-moderate incomes. More than half of all CHFA loans were granted to households of one or two members. In addition, as we discuss in the *1990-91 Analysis* (please see pages 232-235), most of the program's loans are to households in counties with moderate or low housing costs.

New Program. The administration projects that this new program will (1) help

Figure 2

Key Characteristics of the Initiative

Expansion of Existing CHFA Program	Creation of New CHFA Program
Assistance	
Below-market rate mortgages.	Below-market rate mortgages and deferred - payment, low-interest second mortgages.
Financing	
$1 billion increase in the sale of housing revenue bonds—all federal and state tax-exempt.	$800 million housing revenue bonds and $200 million general obligation bonds—all federally taxable, state tax-exempt.
Income Limits	
Generally limited to households earning up to 115 percent of county or state median family income (whichever is higher). Exceptions for small households and for people purchasing homes in high-cost areas and targeted areas of blight.	Limited to households earning up to 150 percent of county or state median family income (whichever is higher).[a] No adjustments for household size, high-cost or target areas.
Home Purchase Price Limits	
Generally limited to 90 percent of average price. area sales price. Exceptions for target areas.	Limited to 110 percent of average area sales

Examples

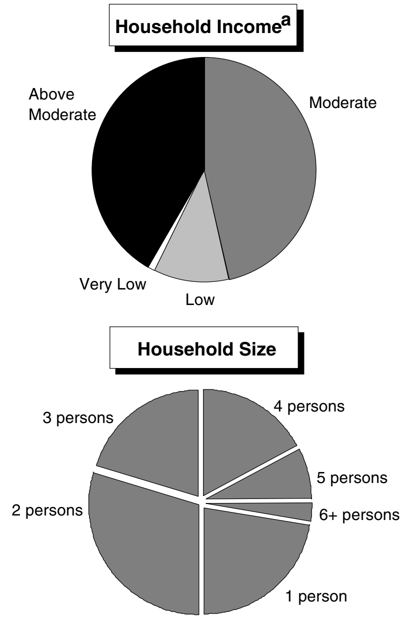
	Existing: Income Limits			New: Income Limits	
County	1 or 2 Person Household	3+ Person Household	Sales Price Limit	All Household Sizes	Sales Price Limit
Fresno	$39,800	$45,700	$85,100	$59,700	$104,100
Los Angeles	40,000	47,000	153,900	59,700	188,100
Orange	49,100	56,465	168,400	73,700	205,800
Sacramento	39,800	45,770	109,900	59,700	134,300
San Francisco	54,700	63,800	195,700	68,400	239,100
Tulare	39,800	45,700	73,400	59,700	89,800

[a] The bill to establish this program (SB 2870—Maddy) grants broad discretion to CHFA to establish income limits. The limit shown here is that which is proposed by the administration. The limit is not specified in SB 2870.

Figure 3

Beneficiaries of Existing CHFA Program

1988-89 Fiscal Year



[a] State housing policy defines "very low", "low" and "moderate" incomes as less than 50 percent, 50 percent to 80 percent and 80 percent to 120 percent, respectively, of county median income. Income levels are adjusted for family size.

5,000 households purchase a home and (2) be effective in areas of the state with higher housing costs. Although many of these households might purchase a home anyway, this program would make the home more affordable and give the household greater choice in selecting a home. For example, a typical family could save $100 to $300 per month in housing costs, depending on the cost of the home and other factors. (The family would be obligated, however, to repay any second mortgage when they sold the home.)

Our review of the new program indicates that the program is very similar to the housing revenue bond program operated by CHFA and local governments prior to 1986. When we reviewed this program in 1985 (please see our report *The Use of Mortgage Revenue Bonds in California*), we found that (1) 50 percent to 80 percent of the loans were granted to households with above-moderate incomes and (2) this program primarily assisted small (one- or two-member) households.

What Will the Initiative Cost?

While there would be no direct cost to the state to expand CHFA's *existing* housing program, the *new* program would directly cost the state a total of $400 million to pay principal and interest on the $200 million of state general obligation bonds. This cost would be spread over a period of 20 years or more.

Will the Initiative Affect Other Programs Under the Federal Bond Cap?

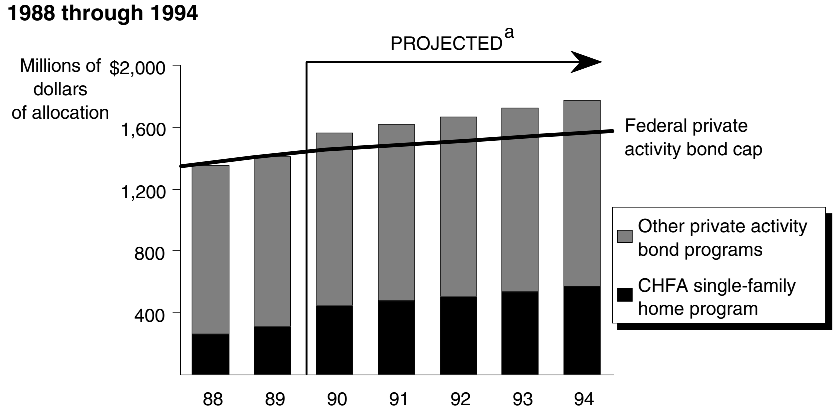
A wide variety of programs compete for private activity bond allocations. These programs include local and other state single and multifamily housing, industrial development, solid waste disposal, and student loan programs.

Figure 4 displays what would happen if CDLAC (1) granted the proposed increase to CHFA and (2) granted other bond programs small increases for population growth or inflation. Figure 4 shows that CDLAC allocations would *exceed* the federal bond cap by $100 million in 1990 and by $200 million in 1994. Even if CDLAC held other bond programs *constant*, CDLAC would still have an $87 million annual overage. Because the federal government does not permit CDLAC to exceed the bond cap, this overage

Figure 4

Not All Programs Would Fit Under the Federal Bond Cap

1988 through 1994



[a] All data after 1989 is projected and assumes (1) 2 percent growth in the federal cap and individual program allocations and (2) implementation of Governor's Housing Initiative.

would necessitate allocation reductions.

Thus, increasing CHFA's share of the cap as the Governor proposes would necessitate allocation reductions for other bond-funded programs. Which programs would be affected is a policy decision which—under current law—would be made by the CDLAC, a commission on which the Legislature is not represented.

Key Policy Choices

Assuming the state wishes to expand bond programs to provide housing assistance, the Legislature faces a series of major decisions with respect to the Governor's Housing Initiative. We identify five policy choices below.

> *"The Legislature faces a series of major decisions with respect to the Governor's Housing Initiative."*

1. Should the Initiative Focus on Homeownership? The first policy choice is to what extent this initiative should provide assistance to first-time homebuyers instead of other groups that the Legislature has expressed interest in serving, such as low-income renters, migrant farmworkers, seniors and the homeless. For example, if the Legislature wished to focus on the problems of low-income renters, the Legislature could modify the initiative to (1) provide deferred-payment second mortgages to developers of multifamily housing, and/or (2) reserve a portion of the federal cap for programs providing multifamily housing.

2. Who Should the Initiative Assist? The second policy choice is whether the initiative should principally benefit individuals and small families with moderate or above-moderate incomes as the Governor proposes. If the Legislature wished to assist a *different* population group, it could modify the initiative. For example, the Legislature could target assistance to moderate-income households of all sizes by (1) revising the income limits of both programs to require that they are fully adjusted for household size and county income, and (2) restricting eligibility by lowering the income limits for the new program.

3. What Level of Assistance Should the Initiative Provide? The third policy choice is determining the appropriate balance between (1) the *level* of assistance provided to each household and (2) the *number* of households assisted by the initiative. The proposed new program, for example, provides substantial long-term assistance to a relatively limited number of households (about 5,000). If the Legislature wished instead to provide assistance to more households, it could (1) reduce the permitted home purchase price, (2) charge market interest rates on the deferred-payment second mortgages, or (3) institute equity sharing provisions.

4. How Specific Should the Initiative's Mandate Be? The fourth policy choice is whether the Legislature wishes to specify how the housing programs are to be implemented. The initiative, as proposed, grants broad discretion to CHFA. For example, unlike other housing programs, the new program has *no* statutory (1) ceiling on income eligibility, (2) limit on loans for resale housing or (3) guidelines on the geographic distribution of loans. Should the Legislature wish to include more specific program details, it could amend the enabling legislation to include the appropriate program parameters. Statutory direction may be particularly pertinent for this program because, unlike other state agencies, *the Legislature does not review CHFA's annual budget, and thus has less oversight of its programs once they are statutorily established.*

5. What Role Should the Legislature Play in Allocating the Bond Cap? Currently, the Legislature plays no direct role in the allocation of the bond cap. The policy choice here is whether the Legislature wishes to unconditionally reserve about one-third of the cap for CHFA's single-family home program, or whether it wishes to modify the allocation process in some other way. For example, the Legislature could (1) add a legislative member to CDLAC, (2) more fully specify legislative priorities for making bond cap allocations, or (3) specify performance criteria that CHFA must meet prior to receiving any reserved bond allocation. Because there is limited "room" under the bond cap, *any decision* the Legislature makes regarding the cap will affect other state and local bond programs.

Conclusion

In summary, the Legislature has significant policy decisions to make in the coming months regarding the Governor's Housing Initiative. These decisions involve *who* is to benefit from the initiative, *how* much assistance should be provided, and *what role* the Legislature should play in establishing the housing initiative *and* making allocations under the federal bond cap.❖

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