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FROM THE ANALYSIS OF THE 1994-95 BUDGET BILL

# STATE HOUSING PROGRAM ISSUES FOR 1994-95

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***What housing program issues merit legislative oversight in 1994-95?***


## *Summary*

*Through its three housing agencies, the State of California operates 31 separate housing assistance programs. In this reprint from the* ***Analysis of the 1994-95 Budget Bill****, we examine whether these programs would be administered more efficiently by a single consolidated state housing agency.*

*In this reprint, we also discuss:*

- *The Department of Housing and Community Development's exorbitant costs to administer the housing programs financed by general obligation bonds.*
- *The Legislature's need for information regarding the cost to provide housing repair loans to victims of the Northridge earthquake.*
- *The high cost of repairing the state's migrant farm worker housing centers.*
- *The Department of Housing and Community Development's poor performance in enforcing the employee housing act.*

# Does California Need Three Housing Agencies?

***Our analysis indicates that the Governor's proposal to consolidate two of the state's housing agencies has merit, but that merging all three state housing agencies would result in even greater efficiencies and improved accountability.***

## Background

California has three state housing agencies:

- Department of Housing and Community Development (HCD).
- California Housing Finance Agency (CHFA).
- Tax Credit Allocation Committee (TCAC).

Figure 4 describes the mission of the agencies and provides information on their operations.

The budget reflects implementation of the administration's legislative proposal to consolidate the TCAC within the CHFA, effective January 1, 1995.

Figure 4

**Overview of California's Three Housing Agencies**

| Agency | Housing Assistance Programs Administered | Additional Agency Responsibilities | 1993-94 Estimated State Operations Expenditures | PYs | Exempt Positions |
|---|---|---|---|---|---|
| **HCD** | About 20 programs. Most programs assist the development/rehabilitation of multifamily projects affordable to lower income households. Additional programs assist disaster victims, farm workers, and other groups. | State housing policy, review of local housing elements, state housing law. | $44,107,000 | 703 | 17 |
| **CHFA** | About ten programs. The largest program assists first-time home buyers. Other programs assist sponsors of multifamily projects. | Provision of mortgage insurance. | $11,568,000 | 140.3 | 7 |
| **TCAC** | One program, which assists the construction/ rehabilitation of multifamily projects affordable to lower income households. | None. | $1,663,000 | 13.6 | 1 |

## SEPARATE HOUSING AGENCIES MAKES LITTLE SENSE

We find that the current division of state housing responsibilities between three agencies results in three major problems, as described in the sections below.

### Housing Assistance Resources Are Wasted

Given the significant need for affordable housing in California, it is incumbent upon each of the state agencies to work together to ensure that affordable housing resources are allocated in the most efficient manner possible. Our review indicates that this coordination is not occurring under the current governmental system.

Instead of providing most—or all—the funds needed to construct affordable housing projects, the state's housing assistance programs typically provide only a portion of the needed revenues. In order to secure all the revenues needed for a project, therefore, sponsors of affordable housing developments frequently seek financing from more than one of the state's 31 housing assistance programs. For example, nearly 90 percent of the projects funded by the HCD's Rental Housing Construction Program also received tax credit awards by the TCAC.

Our review indicates that spreading the cost of a housing project across a number of state programs increases state agency administrative costs considerably. This is because each state agency must review the project's application, process the financing award, and monitor the project's management for the term of the contract.

To illustrate the impact of multiple state agencies funding the same project, we show in Figure 5 the financing of two small family housing projects in Pasadena. Three state housing assistance programs—plus one state-required local housing assistance program—provided the resources for each of these projects. (While both of the projects received financing from four sources, we note that none of the funds provided by the public agencies "leveraged" other funds. That is, none of the funding commitments had the effect of making available to California more money for affordable housing than would otherwise be available for this purpose.)

**Figure 5**

**Financing for Two Affordable Housing Projects**

**(In Thousands)**

| | Financial Assistance Provided | | | |
|---|---|---|---|---|
| Agency | 8-unit Project | 12-unit Project | Type | Progam/Funding Source |
| HCD | $441 | $520 | Low-interest loans | Rental Housing Construction Program/ *state General Obligation bonds* |
| TCAC | 450 | 524 | Tax credits | Low-Income Housing Tax Credit Program/ *federal tax credits* |
| CHFA | 188 | 325 | Low-interest loans | Housing Assistance Trust/ *Investments of proceeds of CHFA bonds* |
| Local[a] | 327 | 300 | Low-interest loans | Local Low and Moderate Income Housing Fund Program/ *Property tax increment* |
| **Totals** | **$1,406** | **$1,669** | | |

[a] Pasadena Redevelopment Agency

While it is difficult to estimate the administrative costs incurred in providing the financing to these small apartment complexes, we estimate that for each loan:

- HCD will spend hundreds of thousands of dollars of state housing bond proceeds to award the loan and monitor project compliance with program regulations.
- TCAC will spend more than $10,000 reviewing and monitoring the project (all costs reimbursed by the housing sponsor)—and the housing sponsor will spend about $20,000 in legal costs to sell the tax credits awarded by the TCAC to raise funds for the project.
- CHFA and the redevelopment agency will also spend significant sums to administer loans to the housing project. (Part of the CHFA's costs are offset by fees charged to the housing sponsor.)

Our review indicates that the total administrative costs for these projects is substantially higher than would have been the case if a single state or local housing agency provided the full funding. Our review also indicates that these high administrative costs (paid by the housing agency or housing sponsor) reduced the total resources available for construction of affordable housing.

## Housing Assistance Programs Are Excessively Complicated

Housing sponsors indicate there are extensive technical and programmatic differences between the state's 31 housing assistance programs. For example, each of the state's multifamily housing assistance programs tends to have:

- Different application rules and processes.
- Different funding criteria and cycles.
- Differing maximum rent level and other restrictions.

Due to these complexities, sponsors of affordable housing projects frequently hire consultants to assist them through the maze of state programs. Our review indicates that the cost of these consultants—and the significant delays involved in coordinating assistance between the different housing programs—increases housing sponsor's costs to provide affordable housing.

### Program and Fiscal Accountability Is Minimal

Finally, dividing responsibilities for housing assistance programs among three agencies makes it difficult for the Legislature or public to know which state agency to hold accountable for housing assistance programs—or to have access to important cross-program data, such as the number of non-duplicated housing units financed from state resources. We also find that the separation of housing agencies, combined with the tendency of the agencies to provide only partial financing for projects, reduces the incentive for any single agency to insist on project cost reductions, such as the elimination of subterranean parking, or to obtain waivers of the development fees that are occasionally required of affordable housing projects by local governments.

## Consolidation Should Be Pursued

Our analysis indicates that similar programs tend to be administered most efficiently within a single agency. In the case of housing programs, our review indicates that a single consolidated housing agency—with strong program policy analysis capacity—would be most capable of coordinating and consolidating the multiple financing sources and providing improved fiscal and program accountability to the public, Legislature and administration.

Accordingly, we recommend that the Legislature:

- Consolidate the funding for the HCD and the TCAC within the CHFA Budget Item (2260) of the 1994-95 Budget Bill. Funds for the HCD and the TCAC would be displayed as sub-items and would be available for expenditure by the HCD and the TCAC.
- Adopt Budget Bill Language directing the CHFA, with assistance from the TCAC, HCD, Department of Finance and legislative policy committees, to prepare a new organizational plan for the housing agencies by December 1, 1994. This plan should describe how the existing functions of the housing agencies are to be carried out in the future. To the greatest extent possible, the organizational plan should group similar programs within a single division. A consolidated housing agency, for example, may need no more than four divisions, one each for multifamily housing programs, single-family housing programs, housing policy development and program analysis, and building standards.
- Enact legislation formally consolidating the housing agencies, effective no later than July 1, 1995.

- Charge the expanded CHFA with submitting a proposal for legislative consideration by July 1, 1996 for needed statutory modifications to state housing programs to improve efficiency in the delivery of the state housing assistance.

## HIGH COSTS TO ADMINISTER HCD'S BOND-FUNDED PROGRAMS

***The cost of administering the HCD's housing bond program is exceedingly high. We recommend that the Legislature consider alternative methods of providing housing assistance in the future.***

Over the last several years, the Legislature has expressed significant concerns regarding the mounting costs of the HCD to administer three recent housing bond measures: the Earthquake Safety and Housing Rehabilitation Bond Act of 1988 (Proposition 77) and the Housing and Homeless Bond Acts of 1988 and 1990 (Propositions 84 and 107). Figure 6 provides information about the programs funded through these bond programs.

In order to explore this concern in greater detail, the Legislature directed the department in 1990 to develop an estimate of its long-term costs for administration of these bond programs. On January 18 of this year, the department finally submitted its long-term cost estimates for three of the largest bond-funded programs. These include the:

- Rental Housing Construction Program (RHCP).
- California Housing Rehabilitation Program (CHRP).
- Family Housing Demonstration Program (FHDP).

In submitting the long-awaited cost estimates, the department indicated that the estimates represent the current management plan of the administration, but that the department will attempt to explore ways to reduce these costs in the future.

Figure 6

**Department of Housing and Community Development Overview of Housing Bond Programs Authorized by Propositions 77, 84, and 107**

(In Millions)

| Program/Purpose | Total Bonds Authorized |
|---|---|
| **Rental Housing Construction Program** | |
| Construction of multifamily housing | $300 |
| **California Housing Rehabilitation Program** | |
| Health and safety rehabilitation of multifamily and owner occupied housing | 117[a] |
| Seismic and health and safety rehabilitation of multifamily housing | 33[a] |
| Acquisition and rehabilitation of residential hotels | 40 |
| **Family Housing Demonstration Program** | |
| Construction of family housing | 15 |
| **Emergency Shelter Program** | |
| Construction and rehabilitation of emergency shelters | 35 |
| **Office of Migrant Services** | |
| Construction and rehabilitation of migrant farm worker centers | 10 |
| **Total** | **$550** |

[a] Proposition 77 authorized a total of $150 million for the CHRP. Of this amount, $80 million was to be used for seismic repairs and $70 million for health and safety rehabilitation. Because the HCD received few applications for seismic renovation funds, the Director of the HCD transferred $47 million of the funds for seismic renovation to the funds for health and safety rehabilitation. Figure 1 shows the *revised* amounts provided for these programs.

## Initial Review of the Department's Findings

While the late release of the department's report did not afford us sufficient time to review the document in detail, we discuss below several major findings.

***Housing Bond Program Administrative Costs Are Extraordinarily High.*** The department's report shows that the HCD will have spent $30 million to administer the RHCP, FHDP, and CHRP through the end of the budget year—and that the department will spend about $200 million to administer these programs for the term of the regulatory agreements (generally 25 to 50 years). In short, the department expects to spend nearly 50 cents—over the course of a few decades—to administer each dollar it provides in housing loans.

***Measured on a per Project Basis, Administrative Costs Are Staggering.*** Our review indicates that by the end of the budget year, the HCD will have spent about $100,000 *per project* in administrative costs under the RHCP, FHDP, and CHRP multi-family programs. Moreover, by the end of the loan term, the HCD will have spent about $700,000 *per project* in administrative costs. Our review indicates that these costs are exceptionally high relative to the number of housing units assisted. The median number of housing units assisted by an RHCP loan, for example, is only 24.

We also reviewed these administrative costs estimates relative to the amounts loaned on RHCP and FHDP projects (we do not have comparable data for the CHRP program). Our review found that, in many cases, administrative costs are very high in relation to the amounts loaned. For example, we found that long-term project administrative costs *will exceed* the project loan amounts for one out of every six RHCP and FHDP projects. That is, the state will spend more money for administrative costs than it provides in loans.

***Administrative Costs Will Vastly Exceed Reserves.*** Administrative costs for these bond programs are paid from the bond proceeds, rather than the General Fund. In order to ensure sufficient funds for this purpose, the department reserved a total of $59.3 million of the $550 million in authorized bonds and allocated this amount among a series of program-specific administrative reserves. The use of the bond proceeds for this purpose is permissible under the bond acts.

Due to high costs of the bond program, two small bond programs have already depleted their administrative reserves. (The Emergency Shelter Program's administrative costs are now paid by the General Fund, and the CHRP *single* family program's costs are being paid by the CHRP *multifamily* program.) Moreover, by the end of the loan terms, the

HCD estimates that its administrative costs for all of the programs will exceed the funds it reserved for this purpose—by a factor of three-and-a-half times.

## Reasons the Housing Bond Programs Cost So Much

Our review indicates that three issues related to program design—combined with ineffective management at the HCD—are primarily responsible for the extraordinary costs of housing bond program administration. We discuss the issues related to program design below.

*Long-term Monitoring Requirement.* First, the bond acts require that the housing financed with their proceeds be reserved for low-income and very-low income households for long periods of time. In the case of the RHCP, for example, most of the projects will be reserved for low-income households for 50 years. The HCD indicates that it must monitor the projects for this entire period to ensure compliance with the regulatory agreements and to protect the state's investment. The HCD estimates that each project takes approximately 62 to 72 direct staff hours to monitor each year. Thus, long-term affordability requirements will result in significant state costs.

*Maximum Leveraging Requirement.* Second, the bond acts require the HCD to allocate bond proceeds in a manner which maximizes the use of private, local, and other funding sources. While this leveraging requirement was intended to increase the number of housing projects which could be assisted, the requirement has serious implications for HCD administrative costs. Spreading the same amount of bond funds over a larger number of projects means that the HCD must review many more applications, close more loans, and monitor more projects than it would otherwise. Extensive leveraging also means that each project's financing is much more complicated and costly for the HCD to review.

To illustrate the impact of leveraging upon the HCD's administrative costs, consider the following example: a nonprofit housing sponsor proposed to build six units of family housing in Menlo Park. Rather than providing the majority of the financing for these units, the HCD provided a $240,000 loan and financed *two* units. (The rest of the financing for the project came from the federal Low-Income Housing Tax Credit program—$466,000, the federal Community Development Block Grant program—$190,000, and private loans—$150,000.) We note that although the HCD lent only $240,000 to the project sponsor, the HCD's cost to review the application, close the loan, and make annual visits to the project for monitoring purposes does not appear to be significantly less than projects where the HCD lent much greater sums.

In addition, we note that although the housing project received financing from three state and federal sources, none of the funding commitments actually "leveraged" other funds. That is, none of the funding commitments had the effect of making available to California more public funds for affordable housing than would otherwise be available for this purpose.

*Specialized Programs.* Third, the bond measures divided the $550 million in bond proceeds among *six different* HCD programs—and further specified that 20 percent of the bond funds for each program be set-aside for projects in rural areas. Our review indicates that subdividing the bond proceeds in this fashion increases administrative costs, because each of the six programs tends to need its own specialized staff, managers, regulations, and loan application and review processes.

## Options for Legislative Consideration

Below, we present a series of options for legislative consideration. These options include actions which the department may take to reduce the cost of the *current* bond-funded housing programs, options for the design of *future* housing programs—and options for *restructuring* our state-local governmental system for providing housing assistance to needy Californians.

*Ways to Reduce Cost of the Current Housing Bond Program.* If HCD continues to administer the housing bond programs in accordance with its current management plan, the housing bond programs eventually will become a significant General Fund liability and/or housing project loan repayments will be diverted to pay administrative costs rather than be lent again to support the construction of affordable housing. Accordingly, it is imperative that the HCD develop options to reduce the cost of its current management plan.

Because most of the housing loans have been awarded already and relatively few new loans will be awarded in the coming years, our review indicates that the HCD should focus its efforts on reducing the high cost of monitoring its housing projects. We estimate that the current HCD monitoring plan costs roughly $4,000 per multi-family project each year. This cost includes two separate on-site visits per year (one by a program staff representative and one by a construction inspector) for up to 50 years.

Ultimately, the purpose of the monitoring program is to ensure that: (1) housing units are rented in accordance with the program requirements, (2) housing complexes are well-maintained, and (3) the state's loans are repaid. Our review indicates that HCD should be able to meet these objectives in a less costly manner than outlined in their current management plan.

We note, for instance, that the state has two other housing agencies which also provide support for the construction of affordable housing: the California Housing Finance Agency (CHFA) and the California Tax Credit Allocation Committee (TCAC). These agencies also require long-term monitoring of housing projects they assist. Our review indicates that housing projects frequently receive financing from two—and occasionally all three—of these state agencies. For example, nearly 90 percent of the projects funded under the RHCP also received funding under the tax credit program. It should be possible, therefore, for the HCD to enter into an agreement with the TCAC to share monitoring and inspection responsibilities and to reduce both agencies' administrative costs.

Alternatively, the HCD may be able to (1) train its staff to review the physical condition of the facilities *and* monitor program compliance, thereby reducing by half the number of required site visits, (2) contract with local private inspection companies for inspections of the physical condition of the facilities, or (3) monitor projects on a less frequent basis.

***Options for the Design of Future Housing Programs.*** Despite some recent reductions in the cost of housing in California, the state continues to suffer from a severe shortage of housing affordable to people with low income. As the Legislature contemplates new programs to provide assistance to these households, we urge the Legislature to think broadly about different approaches.

Our review indicates that there are many ways to provide affordable housing assistance—and that a state housing bond loan program may be suitable for financing large housing projects in areas of the state with low housing vacancy rates and very high housing costs. In these parts of California, a 50-year state investment in affordable housing may be an efficient and effective way to provide housing assistance. This is because the state's administrative costs could be spread over many units and the state could be assured of an increase in the supply of housing. Even in these areas of the state, however, the current bond-funded programs could be made more efficient by (1) reducing the emphasis on leveraging other publicly provided funds, (2) consolidating the separate bond-funded programs, and (3) lowering the on-going monitoring costs, as discussed above.

In many other parts of California, our review suggests that our current housing bond program is an *inefficient* method of providing housing assistance and that it yields *fewer* units of affordable housing than would other programs funded at the same level. Accordingly, we urge the Legislature to consider alternative methods of providing housing assistance in these areas, including:

- **Housing vouchers,** or other direct subsidies to low-income households to enable them to rent moderate cost, privately provided housing.
- **Grants** to help construct housing projects financed by federal or local housing programs. Awarding grants, instead of loans, eliminates most of the state's long-term monitoring costs and reduces the state's costs to review applications and process funds. The state's interest in long-term housing affordability would be addressed by on-going federal or local housing program monitoring.
- **Private-sector contracts,** whereby the state or local agency contracts with apartment owners for the provision of housing units for low-income families. Families living in these units pay reduced rents to management for the duration of the contract.

***Options for Restructuring Governmental Responsibility for Housing Programs.*** Finally, our review indicates that our current governmental system for providing housing assistance to low-income individuals and families has serious shortcomings which reduce the efficiency of virtually all California housing assistance programs. These shortcomings stem from a failure of our current governmental system to assign responsibility for the provision of affordable housing to any single level of government. Instead, responsibility for—and control of—the development of affordable housing is spread between three state agencies, cities and counties, redevelopment agencies, and the federal government. This division of responsibility tends to result in each governmental entity shifting costs to—and assigning blame on—the other governmental entities.

Our review indicates that virtually any housing program operating within this system is likely to have significant inefficiencies from a state-wide point of view. As a result, the Legislature may wish to consider options for *restructuring* the current governmental system to improve accountability and efficiency in the delivery of housing assistance. We outline two options below.

- ***Governor's Proposal.*** The budget proposes consolidating the TCAC within the CHFA. While we have certain concerns regarding this proposal (which we discuss in our review of crosscutting business and labor program issues contained in this *Analysis*), the concept of consolidating the housing agencies has merit. In fact, we believe that consolidating all *three* state housing programs would reduce state administrative costs and provide for a more efficient allocation of state resources.

- ***Making Government Make Sense.*** In our *1993-94 Perspectives and Issue* (please see pages 111-132), we propose assigning local governments full responsibility for housing assistance programs. Specifically, we propose a transfer to cities and counties of all funds currently provided by the state for housing assistance. Local governments would have broad flexibility to structure housing programs to meet the needs of their residents, provided the outcomes of the programs meet certain performance standards. Our review indicates that this model would improve accountability and efficiency in the development of affordable housing.

## COST OF NORTHRIDGE EARTHQUAKE UNKNOWN

***We recommend that the department report at budget hearings on its estimate of cost to provide CALDAP loans to victims of the Northridge earthquake.***

Under the California Natural Disaster Program (CALDAP), residential property owners are eligible for below-market interest rate state loans to rebuild their disaster-damaged property if they do not receive sufficient monies from insurance, private loans, or other state or federal programs. Over the last several years, the state has provided a total of $142 million in loans under this program. The terms of the CALDAP, as revised recently by Chapter 1105, Statutes of 1993 (AB 1677, Hauser), are shown in Figure 7.

Because the Northridge earthquake occurred *after* the release of the Governor's budget, the budget does not identify funds to provide CALDAP loans to earthquake victims. Chapter 1105 requires the HCD to estimate the demand for CALDAP loans within 90 days of a disaster and request a deficiency appropriation from the Department of Finance. In order for the Legislature to have information on the cost of this housing program, we recommend that the department report at budget hearings on its estimate of demand for CALDAP loans in both the current and budget year.

Figure 7

**CALDAP Program Terms**

| | |
|---|---|
| **Eligibility** | Loans are available for single-family housing and multi-family rental property. |
| **Loan of last resort** | Individuals must exhaust other state, federal, and private lender resources before they are eligible for the CALDAP. |
| **Loan terms** | Primarily 30-year term for single-family loans and 20-year term for multi-family loans. Interest rates may not exceed the rate charged under the CAL-VET program (currently 8 percent), plus one-half percent for state administration.<br>Payment on loans is generally deferred until loan expires or property is sold. |
| **Loan limits** | $50,000 limit per single-family home. $35,000 per-unit limit on multi-family rental property. |
| **Disasters covered** | The program is available to victims of any disaster in which the Governor calls a state of emergency. |

## COSTS OF FARM WORKER CENTER REHABILITATION UNFUNDED

***We recommend that the Legislature adopt Budget Bill Language directing the HCD to increase rents charged to farm workers to pay for the on-going costs of the farm worker community rehabilitation proposal.***

Through the department's Office of Migrant Services (OMS), the state provides 2,166 units of low-cost housing to farm workers. These facilities are generally open from mid-spring to mid-fall, when most of the state's crops are harvested. Farm workers and their families pay rents averaging about $4.50 per day for this housing. These rent revenues offset about thirty percent of the cost of the OMS program; the remaining costs are paid by the General Fund.

***Most of the Housing Units Are in Poor Condition.*** Especially in recent years, housing units at the OMS centers have fallen into poor condition and many facilities have significant health and safety hazards. As we discussed in our *Analysis of the 1991-92 Budget Bill* (please see pages 223 - 226), about half of the farm worker housing units were built as temporary structures and have outlived their useful life. The rest of the housing units have deteriorated because on-going maintenance has been neglected due to insufficient funds.

***Multi-year Program to Repair and Reconstruct Housing.*** To correct the dilapidated and unsafe housing conditions at the OMS centers, the HCD proposes a five-year, $53 million program of housing unit reconstruction and repair. Figure 8 highlights the major components of the proposal.

Figure 8

**Office of Migrant Services Five-Year Reconstruction And Repair Proposal**

| Housing Units | HCD Proposal |
|---|---|
| 235 | Units closed for safety reasons; replacement facilities to be constructed. |
| 870 | Repair critical health and safety hazards, and begin replacing units over a five-year period. |
| 921 | Repair all health and safety hazards and improve energy efficiency of units. |
| 140 | No repair or replacement of units necessary. |
| **2,166** | **Total** |

The department commenced this reconstruction and repair program in the current year, using federal monies, state special funds, and $198,000 of the department's General Fund appropriation. The cost of the remaining work in the proposed program is approximately $39.7 million, with a total of $5.1 million proposed from the General Fund over the next four years. Figure 9 shows the distribution of the costs of the proposed program.

***Proposal Has Merit, but On-going Costs Are Ignored.*** If the state is to provide seasonal housing for farm workers, then the many health and safety hazards at these facilities must be abated. The department's proposal appears to be a reasonable effort in this regard.

We are concerned, however, that the proposal fails to specify how the cost of two on-going program liabilities will be paid. Specifically, the proposal does not identify a source of funds to cover: (1) the repayment of the proposed federal construction loans and (2) the necessary repair reserves to pay for maintenance of the rehabilitated farm worker communities. We estimate that these costs will total nearly $1 million annually.

Figure 9

**Office of Migrant Service
Proposed Budget For Housing Facility
Repair and Reconstruction**

In Thousands

| Year | General Fund | Special Funds[a] | Federal Funds | Total |
|---|---|---|---|---|
| 1993-94 | $198 | $5,420 | $8,450 | $13,511 |
| 1994-95 | 1,434 | 5,549 | 12,774 | 14,458 |
| 1995-96 | 1,690 | — | 8,476 | 10,167 |
| 1996-97 | 645 | — | 8,385 | 9,030 |
| 1997-98 | 1,367 | — | 4,753 | 6,119 |
| **Totals** | **$5,334** | **$10,969** | **$42,838** | **$53,285** |

[a] Special funds include state bond funds.

***Options and Recommendations.*** Our review indicates that the Legislature and administration have two major options regarding these unfunded costs. First, the Legislature and the administration could increase annual General Fund support for the OMS program. Alternatively, the HCD could raise farm worker rents at the OMS communities. (We estimate that a $2.75 per day average rent increase would be sufficient to raise these funds. This rent increase would bring average OMS rents to $7.25 per day, or $220 per month.)

Given the state's current fiscal condition, and the generally modest rent levels currently charged at the OMS communities, we recommend that the Legislature adopt Budget Bill Language (BBL) directing the HCD to increase farm worker rents to cover the maximum possible portion of the $1 million unfunded costs. We further recommend that the Legislature specify in BBL that any rent increase be subject to the following restrictions:

- Farm worker rents shall not exceed 30 percent of the farm worker household's income, or other commonly used affordability standards.
- No rent increase shall be levied for a housing unit until its repairs and/or reconstruction is complete.
- Rent increases shall not be imposed before January 1, 1995.

# Employee Housing Program: A Record of Poor Performance

For decades, the Legislature has expressed significant concerns over the housing conditions of agricultural workers, noting that they are "one of the worst-housed population groups in California." In an effort to improve these housing conditions, the Legislature and the Governor have created a number of programs to assist the estimated 900,000 farm workers in the state. The two largest of these programs are the Office of Migrant Services (discussed earlier in this analysis) and the Employee Housing Program, which regulates certain privately provided housing accommodations for agricultural workers.

*Reporting Mandate.* Over the years, the Legislature has had many questions regarding the implementation of the employee housing program, but has not been able to examine these issues in detail, due to limited data. To address this problem, the Legislature mandated in Chapter 1031, Statutes of 1979 that the HCD submit an annual statistical report. This mandate has been broadened several times, most recently by Chapter 952, Statutes of 1993 (AB 2011, Polanco). Chapter 952 also requires the Legislative Analyst to review the HCD's statistical report and to include a summary of the data and an evaluation of the HCD's enforcement efforts in the 1994-95 *Analysis*. The following report is submitted in fulfillment of this requirement.

## Employee Housing Program Background

*What Is Employee Housing?* The Employee Housing Act (EHA) generally applies to two types of employee housing: (1) living quarters provided for five or more employees by their employer and (2) housing accommodations in rural areas provided for five or more agricultural workers, *not* in connection with any work place.

*What Are the Housing Owner's Responsibilities?* The EHA requires the owner to maintain the housing in compliance with certain minimum health and safety standards, developed by the HCD, and to obtain a permit from the HCD prior to allowing the housing to be occupied.

*HCD's Role in Enforcing the Employee Housing Act.* Under the EHA, the HCD is responsible for:

- Annually inspecting proposed employee housing facilities, issuing permits to conforming facilities, and reinspecting nonconforming facilities.

- Locating employee housing facilities operating without permits and prosecuting serious offenders of the EHA.
- Monitoring local government enforcement of the EHA.

*Local Governments May Be Delegated EHA Authority.* Local governments may apply to the HCD for authority to implement the EHA in their jurisdiction. In the event of inadequate enforcement of the EHA by a local agency, the HCD may assume inspection and enforcement activities in that jurisdiction. Currently, 13 counties enforce the EHA in their jurisdictions: Fresno, Kern, Merced, Monterey, Napa, Orange, Riverside, Sacramento, San Benito, San Joaquin, San Mateo, Santa Cruz, and Stanislaus. The HCD enforces the EHA in the rest of the state *and* in most of the incorporated cities in the counties listed above.

*Federal Government's Farm Worker Housing Standards.* Federal law also sets forth requirements for employer-provided housing for agricultural workers. In cases where both state and federal law apply, federal law requires operators to receive permits from the HCD or the local enforcement agency.

## Major Errors Plague HCD's Report to the Legislature

In fall of 1993, the HCD submitted to the Legislature its statistical report on EHA enforcement activities in calendar-year 1992. Our review indicates that the HCD's statistical report contains major errors which compromise its validity and render parts of it useless. For example, the HCD reports that there were 1,685 employee housing facilities in 1992. A careful examination of the document reveals, however, that this total includes facilities which were demolished, closed, double-counted, or never permitted. Overall, we estimate that the HCD's report overstates the number of employee housing facilities by at least 406 facilities—or by at least 24 percent.

Our review also found numerous other examples of serious data irregularities. In some cases, we note that the HCD was aware of the data weaknesses and took preliminary actions to correct them. In other cases, obvious errors were overlooked—or attributed to ambiguities in the statutory reporting requirements.

Chapter 952 requires the LAO to use the data compiled by the HCD to report summary information on the EHA program. Figure 10 summarizes the HCD information, and notes our findings as to the quality of the reported data.

Figure 10

**1992 Employee Housing Program Statistics As Reported by the HCD**

| Information | HCD | Local | Total |
|---|---|---|---|
| Number of Employee Housing Facilities | 706 | 979 | 1,685[a] |
| Facilities found operating without a license | 137 | 71 | 208[b] |
| Inactive employee housing facilities | 1,892 | 146 | 2,038[c,d] |
| Number of occupants when inactive facilities last occupied | 604 | 1,991 | 2,595[d] |
| Number of inspections performed: | | | |
| • pre-occupancy | 410 | 358 | 768 |
| • occupancy | 142 | 478 | 620 |
| • reinspection | 221 | 362 | 583 |
| Total, all inspections | 773 | 1,198 | 1,971[c] |
| Number of violations found in employee housing facilities | 2,048 | 8,972 | 11,020[d] |
| Fees collected | $282,622 | $200,329 | $482,951[b] |
| Fines and penalties collected | $15,030 | $9,622 | $24,652[b] |
| Number of prosecutions undertaken | 0 | 9 | 9[b] |
| Staff time dedicated to EHA enforcement (personnel-years) | 16 | 6.5[b] | 22.5 |
| Personnel-years devoted to locating and prosecuting serious violators and operators of illegal facilities | .85 | —[e] | .85[e] |

[a] Number of facilities overstated by at least 406.
[b] Quality of data unknown.
[c] Significant differences in HCD and local data reporting.
[d] Errors or gaps in data noted.
[e] Local agencies not required to report this data.

## Trends in the Stock of Employee Housing

Although the shortcomings in the data reported by the HCD greatly limited our analysis, our review did reveal three important trends in the stock of employee housing over the last decade. We confirmed these trends in discussions with state and local enforcement officials and through independent research.

***Decline in the Amount of Employee Housing.*** Overall capacity at employee housing facilities appears to have declined substantially, perhaps by as much as a third (or housing for roughly 13,000 employees) over the last decade. Our review indicates that this decline in capacity results in part from a withdrawal from the stock of employee housing of some large facilities owned by farmers. In place of these larger facilities, the data suggests—and enforcement agency officials confirm—that there has been an increase in the number of smaller employee housing facilities. These smaller facilities tend to be auxiliary buildings (such as converted garages) adjacent to single-family residences in rural areas and not provided in connection with work.

***More Housing Reserved for Year-round Employees.*** While employee housing regulations and other program documents tend to refer to employee housing as *seasonal* housing, we note that in the three counties which reported data on the topic, slightly more than half of the facilities were reserved for *year-round* employees. Enforcement agency officials indicate that more housing is reserved for year-round employees than a decade ago.

***Many Violations of Housing Standards.*** While it is impossible to determine from the data whether conditions at employee housing facilities have improved or declined over the last decade, we note that most enforcement agencies report high numbers of violations. Frequently cited violations include: broken windows, missing window screens, filth, inappropriate use of electrical extension wires, and lack of fire extinguishers. Relatively few violations posed an immediate life or safety risk.

## Enforcement Agencies Not Following Law

The lack of complete and consistent data also impaired our ability to review the enforcement of employee housing law as required by Chapter 952. Despite the many weaknesses of the data, however, four serious shortcomings were evident in our review—and merit attention by the department and the Legislature.

***HCD Fails to Conduct Required Inspections.*** Operators of 706 proposed employee housing facilities submitted fees and applications for permits to the HCD to operate employee housing facilities in calendar year 1992. Our review indicates that the HCD failed to inspect or issue permits to 130 of these facilities. In addition, our review indicates that the department failed to inspect at least another 19 proposed facilities, but issued operating permits to them contrary to state law. In total, therefore, the HCD failed to carry out its statutory inspection duties for at least one in five applications for employee housing permits in 1992. Our analysis revealed a similar record of poor performance in 1991.

***Housing with Many Violations Got Operating Permits.*** Our review indicates that some jurisdictions issued permits to facilities with multiple violations of the EHA health and safety standards. In one extreme example, a county granted an operating permit to a facility for 24 employees which had 114 violations. The county reinspected the facility twice during the year and each time the facility had 110 or more violations. The local report indicates that the county did not revoke the employee housing permit, fine the operator, or refer the case for prosecution. Unfortunately, the lack of comparable inspection data in the HCD's report precludes us from determining how widespread this problem is among local agencies—or whether the HCD *also* issues permits to nonconforming facilities.

***Local Agencies Got Only a Cursory Review.*** While the EHA charges the HCD with conducting an annual investigation of local enforcement activities, our review indicates that this review is too short and superficial to be meaningful. In most cases, the HCD inspectors spent no more than two days on-site reviewing local enforcement efforts and providing training. In addition, the HCD did not review much of the enforcement data local agencies submitted.

***Limited Searches to Find Illegal Facilities.*** Because vacant, affordable, temporary housing in rural areas is limited, experts believe that farm workers in many counties live in employee housing facilities operated *without* permits. In an effort to ensure that all farm workers live in decent and sanitary housing, the EHA charges enforcement agencies with locating illegal employee housing facilities. Enforcement agencies then provide assistance to owners of these facilities in identifying deficiencies and applying for permits.

In recent years, the HCD and Riverside County have had increasing success in locating illegal facilities. Despite this improvement, however, our review indicates that the EHA mandate to seek out illegal facilities throughout the state is not being carried out. Instead, enforcement activities have been concentrated to a small number of areas of the state. For example, in 1991 and 1992 nearly a quarter of *all* the illegal facilities discovered statewide were located in three small Tulare towns situated within five miles of one another (Dinuba, Orosi, and Cutler). The majority of the rest of the illegal facilities were located in Fresno, Riverside, or Kern Counties. Conversely, our review indicates that few, if any, illegal facilities were found in many other counties, including four major agricultural producers which also depend on the work of large numbers of seasonal agricultural workers: San Joaquin, Monterey, Ventura, and San Diego.

***Conclusion: EHA Enforcement Needs Improvement.*** Given the deficiencies noted above, we conclude that enforcement of the EHA by the HCD and by some local agencies is weak and uneven and needs improvement. Below, we discuss the HCD's explanation of the problems and then outline recommendations for improvement.

## HCD's Response: Not Enough Money

The HCD department staff were very helpful to us as we compiled this report. When asked to comment regarding our findings, the department staff indicated that the shortcomings we discovered stem from actions the department took to offset reduced financial support for the program. Specifically, in order to reduce costs, the department (1) left the employee housing manager position unfilled for most of the last two years and (2) reduced the level of inspections. These actions resulted in reduced program coordination and oversight—and left significant numbers of facilities uninspected.

Figure 11 illustrates the decline in program resources since 1989-90. The reductions in General Fund support are generally attributable to unallocated General Fund reductions imposed by the budget during the last few years. The constant level of reimbursement revenues reflects the decision of the administration not to increase permit fees. (Permit fees were last increased in 1980-81.) The top line shows the decline in total program revenues.

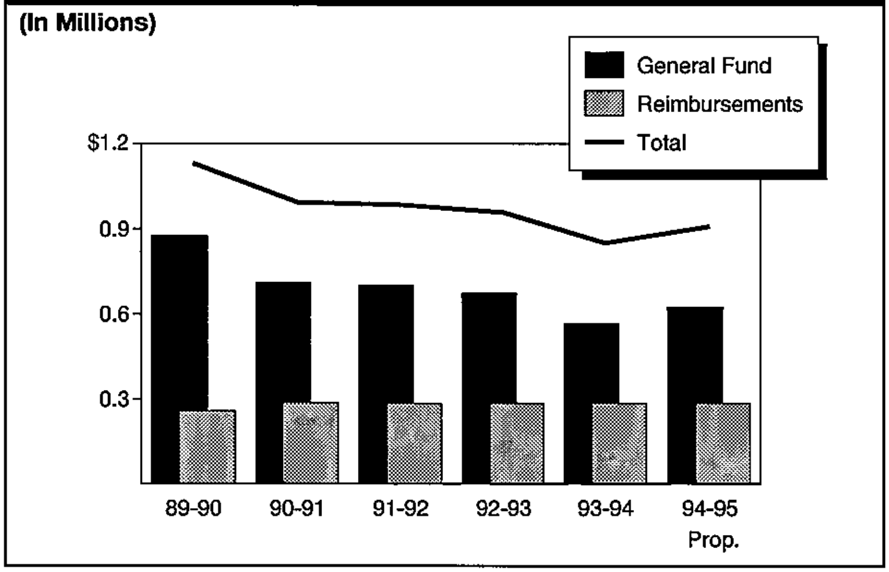
## Recommendations for Improving Performance

Given the many serious problems in the operation of the employee housing program, we believe the department must adopt a plan of corrective action. This plan should include three elements: (1) a proposal to bring into balance employee housing program revenues and responsibilities, (2) a coherent program management system, and (3) a task force to address data irregularities. We examine each of these below.

***Bring Program Revenues and Program Responsibilities into Balance.*** If the HCD can not carry out its full responsibilities under the EHA with its existing level of funding, it is incumbent upon the department to submit a proposal to the Legislature for *reducing* program responsibilities or *increasing* its revenues. Our review indicates that there are at least four ways to bring about a better balance between employee housing program responsibilities and revenues. These are outlined in Figure 12. The options we present are not mutually exclusive. It may be that the best solution lies in combining a number of these options. Each of them, however, requires difficult trade-offs.

Figure 11

**Funds for HCD's Employee Housing Program Have Fallen in Recent Years**




*Consolidate Management Efforts.* Currently, as we discussed above, the department does not have a manager for the employee housing program. Rather, the department has spread these responsibilities among five (higher paid) managers. Our review indicates that this division of responsibilities has greatly undermined the ability of the department to effectively manage and coordinate this program, so that the department should either fill the employee housing program manager position or reorganize its staff to consolidate responsibilities for the program.

*Address Data Irregularities.* Because the Legislature needs data to evaluate the employee housing program, the HCD should convene a task force of local enforcement agencies, HCD field inspectors, legislative staff, and experts on the topic of farm workers. This task force should examine the data collection efforts mandated by statute and make recommendations for needed changes.

Figure 12

## Options for Bringing Employee Housing Program Revenues and Responsibilities into Balance

| Proposal | Advantages | Disadvantages |
|---|---|---|
| Shift *all* inspection responsibilities to local governments. HCD would retain responsibility for local agency oversight and program management. | Transfer would consolidate employee housing program enforcement with local building, health and safety inspection programs. Potential for greater efficiencies. | Transfer of responsibility would require an improved program of state supervision, including a system of sanctions or incentives to ensure adequate local enforcement. Local agencies likely to charge fees in excess of current state fees, because state fees do not cover costs. |
| Modify employee housing permit process as follows:<br>• Issue permits by mail, upon payment of fees and self-certification by owner of compliance with housing standards.<br>• Inspect facilities on a selective basis.<br>• Revoke permits and/or impose fines on operators found with substandard facilities.<br>• Reinspect all facilities found with violations of employee housing standards. | Focuses enforcement efforts on major violators of the EHA. | May result in a greater level of nonconformity with employee housing standards. |
| Increase permit fees. | Additional funds may enable the HCD and local governments to provide an increased level of enforcement as required by law. | Increasing cost of providing employee housing may reduce the amount of housing provided. |
| Increase General Fund support for Employee Housing Program. | Additional funds may enable the HCD to provide an increased level of enforcement and oversight as required by law. | State fiscal condition may prohibit increased state support. |

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