Ways To Improve Management Of Acquired Residential Properties

B-156010

Department of Housing and Urban Development

Veterans Administration

UNITED STATES
GENERAL ACCOUNTING OFFICE

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RESOURCES AND ECONOMIC
DEVELOPMENT DIVISION

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Secretary of Housing and Urban Development
Administrator of Veterans Affairs

This is our report on ways to improve management of residential properties acquired by the Department of Housing and Urban Development and the Veterans Administration.

We are sending copies to the Director, Office of Management and Budget; the Chairmen of the House and Senate Committees on Appropriations, on Government Operations, and on Veterans' Affairs; the Chairman, House Committee on Banking and Currency; the Chairman, Senate Committee on Banking, Housing and Urban Affairs; the Chairman, Senate Committee on Finance; the Chairman, Joint Economic Committee; the Chairman, Joint Committee on Reduction of Federal Expenditures; and Congressmen Olin E. Teague and Les Aspin, pursuant to their requests.

Henry Eschwege

Henry Eschwege
Director

ABBREVIATIONS

GAO	General Accounting Office
HUD	Department of Housing and Urban Development
VA	Veterans Administration

GENERAL ACCOUNTING OFFICE REPORT TO THE SECRETARY OF HOUSING AND URBAN DEVELOPMENT AND THE ADMINISTRATOR OF VETERANS AFFAIRS

WAYS TO IMPROVE MANAGEMENT OF ACQUIRED RESIDENTIAL PROPERTIES
Department of Housing and Urban Development
Veterans Administration B-156010

D I G E S T

WHY THE REVIEW WAS MADE

Privately financed home loans are insured by the Department of Housing and Urban Development (HUD) or are guaranteed by the Veterans Administration (VA) under programs administered by these agencies. VA also makes loans to eligible veterans who cannot obtain private financing. Both agencies acquire residential properties as a result of defaults on these loans.

The General Accounting Office (GAO) reviewed HUD and VA policies, procedures, and practices for managing acquired residential properties to find out how the two agencies could attain greater economy and effectiveness in these activities.

Background

A management consulting firm concluded in 1968 that HUD and VA could improve their overall property management if they developed uniform policies and procedures for managing acquired residential properties. The consultant also said they could save money by improving their operations and more closely coordinating their efforts. (See pp. 6 and 7.)

Although HUD and VA entered into an agreement for this purpose in June 1968, their property management activities still differ. (See p. 7.)

FINDINGS AND CONCLUSIONS

By using open-end bulk-bid contracts (which provide repairs and services on an as-needed basis during specific periods at specific prices) HUD and VA reduced annual costs for acquired property in Jacksonville, Florida, by about $156,000.

HUD and VA did not widely use this form of contracting, however, for acquired properties in other areas. Such use could result in savings similar to those realized in Jacksonville. (See pp. 9 to 11.)

Fees which HUD and VA paid management brokers for similar services varied because the agencies had different contracting methods. HUD and VA should select the most economical and effective method of obtaining management broker services for HUD and VA properties in the same area. (See pp. 11 to 14.)

HUD and VA loan closing and servicing procedures also varied. If the two agencies had implemented their more economical policies and procedures in Alabama and Florida, for example, they could have saved $528,000 annually.

VA also could have realized an annual income of about $117,000 at one office in Florida if it had adopted the private lenders'

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Tear Sheet

policy--charging fees for delinquent payments, bad checks, and mortgage transfers--for VA-guaranteed loans. (See pp. 16 to 21.)

HUD's Detroit, Michigan, office and VA's Philadelphia, Pennsylvania, office, in deciding whether to repair acquired properties, used data that was incomplete or not based on recent experience. Therefore, these offices could not insure that their decisions would minimize the Government's losses or maximize its gains in disposing of acquired property.

Also, the HUD office used unrealistic estimates for the cost of razing a house and for lot values. (See p. 24.)

RECOMMENDATIONS

HUD and VA should require all field offices to use more open-end bulk-bid contracts. HUD and VA should also jointly (1) establish a uniform method of contracting for broker services in the same area, (2) contract for repairs and services to acquired properties, and (3) contract for management broker services in those areas where warranted. (See p. 15.)

HUD should require sales brokers to complete sales closings and to pay the cost of obtaining credit reports on purchasers; it should also require purchasers to pay loan-closing costs such as recording fees, transfer taxes, and a prorated share of certain property taxes. (See p. 23.)

VA should assess fees on VA-financed loans for delinquent payments, bad checks, and mortgage transfers in those areas where such fees are generally charged on VA-guaranteed loans. (See p. 23.)

HUD and VA should instruct their field offices to use realistic data in determining whether properties should be repaired before sale. (See p. 25.)

AGENCY ACTIONS AND UNRESOLVED ISSUES

HUD and VA agreed with the GAO proposal to require all field offices to use more open-end bulk-bid contracts. (See p. 14.)

VA also agreed with the proposal that HUD and VA jointly establish a uniform method of contracting for broker services in the same area. HUD, however, said that a uniform method of contracting for broker services would not insure that the most economical services were obtained. HUD also said that its practice of obtaining competitive bidding for management broker services was the most economical.

While it may not be feasible for HUD and VA to use a uniform contracting method nationwide, they should select the most economical and effective method of obtaining these services for HUD and VA properties in the same area. (See p. 14.)

HUD disagreed with GAO's recommendation about sales brokers and about purchasers.

HUD said that, since loan closings were functions of the lender, the lender should select a closing agent. HUD also said that payment of the closing cost by purchasers or brokers would adversely affect sales.

Because HUD pays the loan-closing fee, it is reasonable for HUD to expect lenders to use sales brokers, without additional cost, to close loans. In addition, brokers or purchasers of VA properties were paying the loan-closing costs with no apparent adverse effect on sales. HUD also permits these costs to be passed on to the purchaser under its mortgage insurance program. (See p. 22.)

VA did not agree with GAO's recommendation that it assess fees on VA-financed loans for delinquent payments, bad checks, and mortgage transfers, because the assessment of such fees could compound loan defaults and because the legal basis for the assessment of mortgage transfer fees was in doubt.

VA and HUD permit lenders to collect these fees under their respective loan guaranty and mortgage insurance programs. Consequently, if assessment of these fees compounds defaults or has no legal basis, VA and HUD should consider whether these charges should be permitted on VA-guaranteed and HUD-insured mortgages. However, assuming there is a legal basis for transfer fees and assuming that mortgage defaults are not compounded by fees for delinquent payments and bad checks, VA should assess such fees in those areas where the fees are generally charged on VA-guaranteed loans. (See p. 22.)

VA agreed with GAO's recommendation that field offices use realistic data in determining whether properties should be repaired before sale. HUD said it would issue a directive reemphasizing that data used in the repair-or-raze analysis be based on realistic estimates and an office's experience. (See p. 25.)

CHAPTER 1

INTRODUCTION

The Department of Housing and Urban Development (HUD), pursuant to the provisions of the National Housing Act, as amended (12 U.S.C. 1701 et seq.), insures mortgage loans made by private lending institutions on various types of housing. At December 31, 1971, HUD had about 5.3 million outstanding insured home loans with balances of about $65.7 billion.

The Veterans Administration (VA), pursuant to the Servicemen's Readjustment Act of 1944, as amended (38 U.S.C. 1801), guarantees home loans made by private lending institutions to eligible veterans of World War II and the Korean conflict. The Housing Act of 1950 (38 U.S.C. 1811) authorizes VA to make loans to eligible veterans living in small cities, towns, and rural areas if financing is not available from private lenders. The Veterans Readjustment Benefits Act of 1966 (38 U.S.C. 1818) makes the VA-guaranteed and VA-financed loans available to veterans who served in the Armed Forces after January 31, 1955. At December 31, 1971, VA had about 3.7 million outstanding guaranteed home loans with balances of about $38.5 billion and about 279,000 outstanding financed loans with balances of about $2.5 billion.

When borrowers default on home loans, HUD and VA often acquire residential properties similar in age, size, and design and in the same county, city, or subdivision. Sometimes these properties are adjoining.

MANAGEMENT OF ACQUIRED RESIDENTIAL PROPERTIES

HUD and VA assign custody and management of acquired properties to property management brokers who prepare repair specifications, solicit bids for repairs, prepare purchase orders, inspect the repairs, and manage the properties until they are sold. The management brokers are paid a fee for each property they manage.

Usually local real estate brokers, who can be management brokers for the properties, sell the properties to the public. Private lenders finance purchases of HUD-acquired properties and HUD insures these loans. When VA sells its acquired properties, it finances the loans.

The following table shows the number of properties on hand at the start and end of fiscal year 1971, the number HUD and VA acquired and sold during fiscal year 1971, and the average net loss for each property sold.

Properties	HUD	VA	Total
On hand (6-30-70)	21,947	9,980	31,927
Acquired	35,240	13,893	49,133
Sold	24,910	13,744	38,654
On hand (6-30-71)	32,277	10,129	42,406
Average net loss	$3,845	$ 2,273	-

We reviewed HUD and VA policies, procedures, and practices for managing acquired properties to identify actions they could take to achieve greater economy and effectiveness in these activities.

STUDIES ON MANAGEMENT, REPAIR, AND DISPOSITION OF HUD AND VA RESIDENTIAL PROPERTIES

In a report to the Congress[1] in May 1967, we concluded that consolidation of HUD and VA property management activities for acquired residential properties would provide significant cost benefits by reducing the overall size of the agencies' staffs and by contracting in volume for management broker services. Also, it would result in more uniform procedures and terms for dealing with brokers and potential buyers.

Our recommendation to consolidate HUD and VA property management activities was not implemented. Instead, the Office of Management and Budget contracted with a management consulting firm to determine what, if any, organizational

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[1]Report to the Congress on "Savings Possible by Consolidating Management of Acquired Residential Properties" (B-156010, May 31, 1967).

and other actions HUD and VA should take to more effectively and efficiently manage and sell acquired residential properties.

In a January 1968 report, the consulting firm stated that greater savings could be realized by improving intra-agency operations and increasing interagency coordination than by consolidating property management activities. Specifically, the consulting firm stated that increased uniformity in the agencies' management activities in the same areas or in housing subdivisions which had similar environments could result in

--increased effectiveness of management brokers;

--quantity discounts on standard materials and equipment;

--lower overall repair costs;

--more consistent pricing of properties offered for sale; and

--improved public image with regard to repairs, sales, prices, and sales procedures.

In response to the consulting firm's report, HUD and VA entered into an interagency agreement in June 1968.

SCOPE AND IMPLEMENTATION OF INTERAGENCY AGREEMENT

The interagency agreement provided for regular meetings of HUD and VA field office officials to establish sales prices, to consider the great variances in each agency's scope of repair, and to agree on the general price range and terms of sale of similar residential properties.

HUD and VA officials did meet, but were unable to resolve major program differences because the agreement did not permit the field offices to establish a common set of operating procedures which diverged from those promulgated by HUD and VA headquarters.

HUD and VA policies and procedures still differ. Some of these differences are discussed in the following chapters.

CHAPTER 2

CONTRACTING FOR REPAIRS, SERVICES,

AND MANAGEMENT OF ACQUIRED PROPERTIES

By using open-end bulk-bid contracts, HUD and VA reduced annual repair and service costs for acquired properties in Jacksonville, Florida, by about $156,000. However, HUD and VA did not widely use this form of contracting for acquired properties in other areas of the country.

Because of different contracting methods, fees which HUD and VA paid management brokers for managing acquired properties in the same area varied considerably even though the brokers' services were similar. HUD and VA should select the most economical and effective method of obtaining management for HUD and VA properties in the same area.

OPEN-END BULK-BID CONTRACTS FOR REPAIRS AND SERVICES

Under open-end bulk-bid contracts, the HUD and VA offices in Jacksonville obtained particular types of repairs or services for all properties as needed during specific periods and at specific unit prices. For example, a VA flooring contract provided for installation of grade D or better random pattern corktone, vinyl asbestos, or asphalt tile over a cleaned slab with old tile removed, at a unit cost of 30 cents a square foot. The contract covered VA properties in Duval, Clay, and Nassau Counties, Florida (Jacksonville area), which required tiling during the 12 months ended June 30, 1971.

When VA used open-end bulk-bid contracts, the cost to replace floors and roofs, install locks, and treat termites in VA properties in the Jacksonville area was much less than the cost for these repairs and services when they were contracted for on a house-by-house basis.

A VA official at the Jacksonville office stated that an open-end bulk-bid flooring contract had reduced floor-retiling costs by about $90 a property and floor sanding and refinishing costs by about $10 a property. Our review of 26 VA properties in the contract area showed that VA saved about $61 a property on floors retiled or sanded and refinished in about

58 percent of these properties. We estimate that VA reduced its total flooring cost in the Jacksonville area by as much as $48,000 during fiscal year 1970.

VA also awarded an open-end bulk-bid contract for replacing roofs and reduced average roofing costs by about $114. We estimate that the contract saved VA about $48,000 on 31 percent of its properties during fiscal year 1970.

Although VA was using open-end bulk-bid contracts for these services, the HUD Jacksonville office was contracting for them on a house-by-house basis. A comparison of VA's average unit cost under open-end bulk-bid contracts with HUD's average unit cost on a house-by-house basis indicated that VA's costs were about $41,000 less during fiscal year 1970 for termite treatments and locking services. HUD could realize savings similar to VA's by using open-end bulk-bid contracts.

The following table compares VA's average unit cost for 30 properties repaired under open-end bulk-bid contracts to HUD's average unit cost for 30 properties repaired on a house-by-house basis.

Repair or service	Unit of measurement	Average unit cost HUD	Average unit cost VA
Roof replacement	Sq. ft.	$ 0.37	$ 0.30
Floor replacements:			
Vinyl asbestos tile	Sq. ft.	0.35	0.30
Vinyl sheeting	Sq. ft.	0.65	0.60
Termite treatments	A house	112.25	40.72
Lock installations	A house	21.08	13.12

After our letter of inquiry to HUD in May 1970 concerning use of open-end bulk-bid contracts, the HUD office in Jacksonville awarded an open-end bulk-bid contract and reduced the cost of termite treatments from $112 to $63 for each house treated in the contract area. Based on the number of houses treated for termites during fiscal year 1970, HUD would have saved about $19,000 annually.

The HUD office also obtained an open-end bulk-bid contract proposal which showed that installing new locks would cost $15.50 a property and resetting the tumblers for existing locks would cost $11.50 a property. On the basis of HUD's average lock-installing cost of about $21 a property and the number of properties located in the contract area, the HUD Jacksonville office could save $3,800 to $5,800 annually by awarding a lock contract at the proposed price. And, if the HUD office could obtain open-end bulk-bid prices comparable to the prices VA obtained for roof and floor replacements, it could save about $45,000 more annually.

Several HUD and VA offices used open-end bulk-bid contracts for lawn maintenance and property cleanup. Also, the HUD office in Tampa, Florida, made limited use of this type of contract for installing fences, carpet, aluminum siding, window glass, and bathtub enclosures and for connecting sewer lines to properties having septic tanks.

Although the HUD and VA offices included in our review used open-end bulk-bid contracts to a limited extent, they were obtaining most repairs and services, including roof and floor replacements, termite treatments, and locking services, on a house-by-house basis. In our opinion, the frequency of repairs and services obtained for the many properties these offices acquired justifies wider use of open-end bulk-bid contracts.

To obtain a more favorable price for repairs or services under open-end bulk-bid contracts--especially where the frequency of repairs or services or the number of properties of each agency is small--HUD and VA could combine their requirements under one contract, similar to the type of joint contract HUD and VA have for obtaining credit reports on prospective purchasers.

PROPERTY MANAGEMENT SERVICES

Each HUD and VA office contracts with management brokers who (1) periodically inspect properties, (2) arrange for property cleanup, lawn maintenance, termite treatment, and lock services, (3) prepare property evaluation reports, repair specifications, and purchase orders for repairs and services, and (4) solicit bids for repairs. In addition, HUD and VA management brokers supervise the repair program and investigate and resolve repair complaints received after the properties are sold.

HUD's management broker contracts are awarded on the basis of competitive bids. These contracts provide for a monthly management fee and, in some cases, fees for specified services, such as initial inspection of the property, preparation of the property evaluation report, or preparation of the repair specification. Tampa's HUD office awarded management broker contracts providing only for a monthly management fee which included the performance of specific services at no additional cost. The other four HUD offices awarded broker contracts which provided for specified fees for services in addition to the management fee.

Local VA offices select management brokers from applicants who want contracts. The VA offices establish all fees, which are not to exceed the maximum prescribed by VA regulations, and award the contract without formal advertising.

The following table shows the fees paid for management broker services by the HUD Jacksonville, Tampa, Detroit, and Philadelphia offices and by the VA Jacksonville, Detroit, and Philadelphia offices. The fees paid by the VA Jacksonville office apply to both the Jacksonville and Tampa areas. In addition to the fees shown in the table, VA management brokers are paid the lesser of 10 percent of the repair cost or $50 a property for supervising the repairs and for preparing the repair specifications. Although HUD management brokers also supervise the repairs, the cost for this service is included as part of their monthly management fees. HUD and VA management brokers do not receive any additional compensation for investigating and resolving repair complaints.

	Fees for property management services			
		Preparation of		
	Initial inspection	Evaluation report	Repair specification	Monthly management
HUD offices:				
Philadelphia	$20.00	$5.00	$5.00	$2.26[d]
Detroit	15.00	5.00	5.00	6.62[d]
Jacksonville	15.00	5.00	5.00	7.47[d]
Tampa	(a)	(a)	(a)	7.45[d]

	Fees for property management services			
		Preparation of		
	Initial inspection	Evaluation report	Repair specification	Monthly management
VA offices:				
Philadelphia	$15.00	(b)	(c)	$7.50
Detroit	15.00	(b)	(c)	7.00
Jacksonville	14.00	(b)	(c)	7.00

[a]Included in the monthly management fee.

[b]Part of the initial inspection report and included in the initial inspection fee.

[c]Included in the fee for supervising repairs to the property, which is the lesser of 10 percent of the repair cost or $50 a property.

[d]Amounts are weighted averages based on the contract amounts and the number of properties managed under each contract at the time of our review.

The following table demonstrates the effect of the different fees by showing the amounts payable for one property under each contracting method used in Florida, assuming the property was assigned to management brokers for 4, 9, 11, and 12 months. These periods represent the average number of months that HUD and VA assigned properties included in our review to management brokers in Jacksonville and Tampa.

	Average fees paid brokers per property		
Average number of months property in custody of management broker	HUD Jacksonville	HUD Tampa	VA Jacksonville and Tampa (note a)
4	$ 54.88	$29.80	$42.00
9	92.23	67.05	77.00
11	107.17	81.95	91.00
12	114.64	89.40	98.00

[a]Excludes the fee for supervising repairs to the property.

Because of the contracting method used, HUD's Tampa office paid less for broker services than VA's Tampa office and HUD's and VA's Jacksonville offices, although the services were similar. The method used by the HUD office in Tampa may not be feasible for properties in other areas of the country; however, the range of cost for broker services in Florida indicates that HUD and VA should select the most effective and economical method of obtaining broker services in the same area.

To further minimize the cost of broker services, HUD and VA should consider jointly contracting for broker services, especially when the total number of properties held by either HUD or VA in a particular area is not large.

CONCLUSIONS

Limited use was made of open-end bulk-bid contracts for major repairs and services in areas where HUD and VA had large concentrations of properties. Wider use of open-end bulk-bid contracts could result in savings similar to those realized in Jacksonville, Florida. HUD and VA could also save by selecting the most effective and economical method of obtaining broker services for all HUD and VA properties in the same area.

AGENCY COMMENTS AND OUR EVALUATION

HUD and VA, in commenting on our draft report, agreed to require all field offices to use more open-end bulk-bid contracts.

VA also agreed to jointly establish a uniform method of contracting for broker services in the same area. HUD, however, stated that a uniform method of contracting for broker services would not insure that the most economical services were obtained. HUD believed that its practice of obtaining broker services through competitive bidding was the most economical.

We recognize that it may not be feasible for HUD and VA to use a uniform contracting method nationwide and that a uniform method would not necessarily insure that the services obtained are economical. However, HUD and VA should select the most economical and effective method of obtaining management broker services for HUD and VA properties in the same area.

VA agreed with our proposal that HUD and VA jointly contract for repairs and services for acquired properties in those areas where warranted. HUD stated that it and VA would initiate an in-depth study of joint contracting for repairs and services.

RECOMMENDATIONS TO THE SECRETARY OF HUD AND THE ADMINISTRATOR OF VETERANS AFFAIRS

We recommend that HUD and VA require all field offices to use more open-end bulk-bid contracts. We recommend also that HUD and VA jointly establish a uniform method of contracting for broker services in the same area and jointly contract for repairs and services to acquired properties and for management broker services in those areas where warranted.

CHAPTER 3

LOAN-CLOSING AND LOAN-SERVICING PROCEDURES

HUD and VA could realize annual savings of about $528,000 at three HUD and two VA offices in Alabama and Florida by implementing, State-wide, the more economical loan-closing and loan-servicing procedures used by one or more of the offices in these two States. Also, VA could realize annual income of about $117,000 at one office in Florida if it adopted the policy followed by private lending institutions and charged fees for delinquent payments, bad checks, and mortgage transfers.

PAYMENT OF CLOSING COSTS

HUD's general policy is to pay all the closing costs associated with selling its properties; VA's policy varies from office to office. Closing costs for a HUD property vary because HUD pays the private lender a loan origination fee which is 1 percent of the mortgage amount and a loan discount fee which is the difference between HUD's approved interest rate and the current market interest rate.

Both HUD and VA use local real estate brokers to sell acquired properties in Alabama and Florida and pay the brokers a 5-percent sales commission for each property sold. Other closing costs include (1) a sales-closing fee, (2) credit report costs, (3) a recording fee and transfer tax, and (4) a property tax resulting from loss of homestead exemption. HUD and VA differ as to who should pay these costs.

Sales-closing fees

Selling brokers closed sales for VA-acquired properties in Alabama and received no compensation other than the sales commission. VA employees prepared the closing documents and forwarded them with appropriate closing instructions to the selling broker, who obtained the purchaser's signature and had the applicable documents notarized and recorded. The selling broker also collected any funds (e.g., prepaid taxes and insurance, recording fees, etc.) due from the purchaser, paid certain closing costs, and remitted any remaining funds to the appropriate party. Although the selling broker was paid a commission for VA properties sold in Florida and for HUD properties sold in Alabama and Florida, an agent other than the selling broker closed the sales and was paid a closing fee by VA or HUD.

In Florida, VA employees also prepared the closing documents; however, private attorneys or title companies generally closed the sales, for which they were paid $35 a property. Agents who generally were paid about $50 to $100 a property closed HUD property sales in Alabama and Florida. However, unlike VA, HUD did not select the closing agent; instead, the lender, or its representative, made the selection and in some instances acted as its own closing agent. When the lender did not conduct the closing, a private attorney or title company was appointed to complete it after HUD had issued closing instructions and, in some instances, partially completed the closing documents.

HUD's sales-closing transactions are similar to VA's except that sales proceeds pass from the lender to the borrower and from the borrower to the seller. Because the closing agent is responsible for transmitting these funds, representatives of the lenders objected to selling brokers' acting as closing agents. However, this objection is not valid when selling brokers are bonded.

HUD and VA could have saved about $194,000 during fiscal year 1971 if the VA office in Florida and the HUD offices in Alabama and Florida had required selling brokers to complete sales closings, which was the policy followed by the VA office in Alabama.

Credit report cost

Both HUD and VA require the selling broker to obtain a credit report on a prospective purchaser of an acquired property from a credit source which HUD and VA have jointly contracted with to provide this service.

The HUD and VA contract provides for the purchase of credit reports at the following rates.

Basic report	$5.25
Additional charges:	
Out-of-town report	4.00
Subject lives and works in different towns	1.00

However, the Jacksonville area, together with several other metropolitan areas, were excluded from the contract. The average cost of credit reports at the Jacksonville office was $11.

HUD regulations state that, when the sale is closed, the selling broker will be reimbursed for the cost of a credit report. Although VA regulations permit VA to pay for credit reports, VA offices in Alabama and Florida required the selling broker to pay.

In Tampa, HUD reimbursed the selling brokers at a flat rate of $10 for each credit report instead of the amount charged under the contract. Tampa officials said that experience had shown that a credit report cost an average of $10; however, they did not have cost data to substantiate this. In Birmingham, Alabama, HUD reimbursed selling brokers for the contract amounts charged (about $6).

By revising its policy to require selling brokers to absorb the cost of these credit reports, HUD could save about $26,000 annually at the three HUD offices included in our review. HUD property sales at these three offices were only 11 percent of HUD total sales during fiscal year 1971; therefore, nationwide savings could be substantial.

VA should also require that selling brokers pay for credit reports.

Recording fees and transfer taxes

When an acquired property is sold, the deed and mortgage documents must be recorded, and the transfer tax levied on these documents must be paid. Except for the VA office in Montgomery, Alabama, VA and HUD were paying the recording fees and taxes. VA regulations state that:

> "* * * closing costs and prepaid items may be financed by the VA and either added to the purchase

price or absorbed fully by the VA at the discretion of the Manager."

*   *   *   *   *

"* * * all instruments will be recorded by the sales closer who will, at time of closing, collect from the purchaser an amount estimated by him to be sufficient to defray all recording expenses to be paid by the purchaser, giving him a receipt therefor. If any funds remain after recording the closing instruments, such unused amount will be refunded by the sales closer direct to the purchaser."

A VA official at the Jacksonville office cited the first quote above as the basis for allowing VA to pay the costs of recording sales documents and transfer taxes. He said that VA assumed its sales program would be enhanced if it paid these costs and therefore the Government's best interest would be served.

A VA official in Montgomery said that the decision to require the purchaser to pay the recording fee and transfer tax was based on the second quote above. This official said that due to the nominal amount involved--about $25 a property--the purchaser's payment of these expenses had no noticeable effect on VA's sales program in Alabama.

The HUD offices in Alabama and Florida paid the recording fee and transfer tax in accordance with the following HUD regulations.

"* * * Immediately following closing, the documents (deed, mortgage, etc.) shall be filed for recordation. If funds are not available from the sales proceeds in cash, and if it is necessary to do so, the individual representing the seller in the closing is authorized to advance the required funds for this purpose and to obtain reimbursement by submitting a properly executed voucher supported by the receipted bill."

Even though VA and HUD are allowed to pay recording fees and transfer taxes, they should require the purchaser to pay these expenses. There may be instances when it would benefit the Government to pay these costs; however, such instances should be handled individually. VA and HUD should not pay these costs when the housing market is strong and many purchase offers are received for a property.

The average costs for recording fees and transfer taxes were about $28 a property at the HUD office in Birmingham, $48 at the HUD office in Jacksonville, $49 at the HUD office in Tampa, and $32 at the VA office in Jacksonville. On the basis of these costs and the number of sales at these offices, HUD and VA could have saved as much as $148,000 during fiscal year 1971 if the offices had followed the policy adopted by VA in Alabama.

Property taxes resulting from loss of homestead exemptions

Both Alabama and Florida have a homestead exemption law which provides a tax benefit to individual homeowners who occupy a property between October 1 and December 31 in Alabama or on January 1 in Florida. However, the exemption is not allowed on properties owned by HUD and VA.

In Alabama, the exemption is on the first $2,000 of assessed valuation and, because the tax rate is uniform throughout the entire State, the maximum amount of the annual tax advantage is $13.60 for each qualified homeowner. In Florida, the exemption is on the first $5,000 of assessed valuation, but the tax rates are not uniform throughout the State. In Duval County, the maximum amount of the annual tax advantage to each qualified homeowner for the homestead exemption was about $127. In some areas the tax advantage was greater than in Duval County and in other areas it was less.

When a HUD or VA property in Alabama is sold, the tax applicable to the lost homestead exemption is prorated between the seller and purchaser on the basis of the number of months each party held title to the property during the tax year. However, when a HUD or VA property in Florida is sold, the additional tax resulting from loss of the homestead exemption is paid by HUD or VA rather than prorated between the buyer and the Government.

On January 1, 1971, HUD and VA owned more than 2,500 properties in Florida. The tax on these properties resulting from loss of the homestead exemption would be about $320,000 for 1 year, assuming the tax rate applicable to these properties was the same as the rate in Duval County. Assuming property sales were evenly balanced throughout the year, prorating the additional tax between the seller and the purchaser could have saved the Government about $160,000 in Florida.

In view of these potential savings, HUD and VA should implement their Alabama policies in Florida and in any other homestead exemption State.

FEES FOR DELINQUENT PAYMENTS, BAD CHECKS, AND MORTGAGE TRANSFERS

Private lending institutions that hold and service loans insured by HUD or guaranteed by VA charge fees for delinquent mortgage payments, mortgage payments made with bad checks, and mortgage transfers. Private lending institutions holding VA-guaranteed mortgages in Florida charged (1) 4 percent of the amount of the mortgage payment for a delinquent payment, (2) $5 for a bad check, and (3) from $25 to $40 to transfer the mortgage to another party.

VA does not charge fees for these items when it finances loans but it should do so. Such a change in policy would mean that all purchasers of properties sold with HUD-insured, VA-guaranteed, or VA-financed loans would be treated equally. The income received could be used to offset the additional expenses incurred by VA for servicing delinquent accounts, processing bad checks, and processing mortgage transfers.

By collecting the fees the VA office in Jacksonville could realize an annual income of about $117,000. The VA Jacksonville office has less than 6 percent of all VA-financed mortgages; therefore, nationwide collections by VA could be substantial. Charging delinquent payment fees could also encourage property owners to keep their mortgage payments current.

AGENCY COMMENTS AND OUR EVALUATION

In commenting on our proposal to use selling brokers as closing agents, HUD said that loan closings were functions of the lender and that the lender should designate agents to close loans. VA, who is the lender for VA-financed loans, agreed with our proposal.

We recognize that loan closings are normally functions of the lenders; however, inasmuch as HUD pays the loan-closing fee, it is reasonable for HUD to expect lenders to use the least expensive means to close loans.

VA agreed with our proposals that selling brokers pay for credit reports and that purchasers pay recording fees, transfer taxes, and a prorated share of additional property taxes resulting from loss of homestead exemption privileges; HUD, however, said that payment of these items by the broker or purchaser would adversely affect the sale of acquired properties.

As noted on page 19, a VA official in Alabama said that purchasers' payments of recording fees and transfer taxes had not noticeably affected VA's sales. Nor was there any evidence to show that HUD and VA sales were adversely affected because purchasers had to pay a prorated share of the taxes resulting from the loss of homestead exemption privileges in Alabama or because selling brokers had to pay for credit reports on the purchasers of VA properties in Alabama and Florida. Under HUD's mortgage insurance program, the purchaser can be charged for the cost of credit reports, recording fees, and taxes.

We recognize that there may be instances when it would benefit the Government to pay these costs; however, HUD and VA should not pay them unless it can be shown that the sale of acquired properties in a specific area would be adversely affected by not paying such costs.

VA did not agree with our proposal for VA-financed loans that it adopt private lending institution policies regarding collection of fees for (1) delinquent mortgage payments, (2) bad checks, and (3) mortgage transfers. VA said that, when a borrower has difficulty meeting his loan obligation on time, additional late charges can compound the problem and could even cause the next installment to be late.

VA said that any advantage gained and any amounts collected as a result of late charges and bad check charges would not compensate VA for losses incurred through defaulted loans. Moreover, administrative costs for collecting the fees would be excessive. VA indicated that it did not attempt to collect a mortgage transfer fee because the legal basis for such assessment was considerably in doubt.

VA said also that the collection of these fees by private lenders under VA's loan guaranty program was optional and that, while some holders impose these charges, a substantial number do not.

If the charging of fees for late payments and bad checks compounds the problems of a borrower who has difficulty in meeting his loan obligation and could cause a loan default and if the charging of mortgage transfer fees has no legal basis, we wonder why such charges are permitted on VA-guaranteed and HUD-insured loans. On the other hand, if fees for late payments and bad checks do not adversely affect the loan guaranty or mortgage insurance programs and mortgage transfer charges do have a legal basis, VA should charge these fees for VA-financed loans in those areas where private lenders do so for VA-guaranteed loans.

RECOMMENDATIONS TO THE SECRETARY OF HUD AND THE ADMINISTRATOR OF VETERANS AFFAIRS

We recommend that HUD (1) require purchasers to pay recording fees, transfer taxes, and a prorated share of additional property taxes resulting from loss of homestead exemption privileges and (2) require selling brokers to complete sales closings and to pay the cost of credit reports obtained on purchasers.

We also recommend that VA assess fees on VA-financed loans for delinquent payments, bad checks, and mortgage transfers in those areas of the country where such fees are generally charged on VA-guaranteed loans.

CHAPTER 4

BETTER ESTIMATES NEEDED IN DETERMINING

WHETHER PROPERTIES SHOULD BE REPAIRED

The HUD Detroit office and the VA Philadelphia office, in determining whether acquired properties should be repaired for sale, used data that were either incomplete or were not based on recent experience; therefore, they could not insure that such decisions would minimize losses or maximize gains in disposing of acquired properties. Also, the HUD office used unrealistic estimates for the cost of razing a house and for the lot value.

Of 29 HUD-acquired residential properties in a four-block section in southeast Detroit, which we considered to be representative of those in the area, HUD had decided to repair 16 and to raze eight. HUD had not made a decision about the other five properties at the time of our review.

Of the 16 properties, six had been repaired or were being repaired. The repair cost for the six properties exceeded HUD's estimated repair cost by an average of $620 a property--ranging from $152 to $1,052 a property.

HUD's decision to repair three of the 10 remaining properties was made without the benefit of repair estimates for the plumbing, heating, and electrical systems. Our analysis of 18 comparable properties indicated that repair costs for plumbing, heating, and electrical systems averaged about $3,000 a property.

In addition, HUD's estimate of the cost to raze a house was not realistic because HUD used a standard amount--$1,500--regardless of whether the property was a one- or two-family house. The actual cost to raze a house in the four-block section of Detroit ranged from $800 to $1,300, with an average cost of $1,000. In other areas of Detroit the average cost to raze a one-family house was $800 and $1,100 for a two-family house.

In its repair-versus-raze analysis, HUD's Detroit office generally used a standard lot value of $500. For 19 properties razed by the HUD Detroit office, the lot values ranged from $600 to $1,600, with an average of $1,100.

HUD officials in Detroit said that, when they were determining whether to repair or raze a house, they also considered factors such as positive and negative selling features of the house, the number of HUD-acquired houses in the area, potential maintenance costs to the buyer, vandalism, and structural soundness of the house.

Of 30 VA-acquired residential properties in Philadelphia, which we considered to be representative of those in the area, 19 were sold unrepaired and 11 were repaired before sale. VA's decision on repairing these properties was based on unrealistic estimates of the sale prices of unrepaired houses and the cost of repairs. For example, the sale prices for 11 of the 19 properties sold without repairs ranged from about $500 to $2,000 a property lower than VA's estimates and averaged $1,300, or about 33 percent, lower a property. Also, the repair costs for 11 properties which were repaired before sale averaged $1,900 a property, compared with VA's estimate of $1,200--a difference of nearly 60 percent.

Without realistic estimates, the HUD Detroit office and the VA Philadelphia office could not insure that their decisions to repair acquired properties minimized the Government's losses or maximized its gains in disposing of acquired properties.

RECOMMENDATION TO THE SECRETARY OF HUD AND THE ADMINISTRATOR OF VETERANS AFFAIRS

We recommend that HUD and VA instruct their field offices to use realistic data in determining whether properties should or should not be repaired before sale.

In commenting on the matter, VA agreed and HUD stated that it would issue a directive reemphasizing that data used in the repair-or-raze analysis be based on realistic estimates and an office's experience.

CHAPTER 5

SCOPE OF REVIEW

We made our review at HUD and VA headquarters in Washington, D.C., and at the following HUD and VA field offices.

States	HUD offices	VA offices
Alabama	Birmingham	Montgomery
Florida	Jacksonville	Jacksonville
	Tampa	
Michigan	Detroit	Detroit
Pennsylvania	Philadelphia	Philadelphia

These offices sold about 17 percent of the 38,654 properties sold by HUD and VA nationwide during fiscal year 1971.

We reviewed HUD and VA policies, procedures, and practices for managing, repairing, and disposing of acquired properties. We examined home loan statistics and various reports on property repair and disposition costs at HUD and VA headquarters. At each HUD office included in our review we selected at least 30 properties for detailed review. For each VA office included in our review, we selected 30 VA properties near the HUD properties. We reviewed the files for each property to compare the types and extent of repairs made and the related costs. At each HUD and VA field office, we reviewed the practices followed in obtaining property management services and in selling properties and the related costs.

We interviewed HUD and VA officials, inspected selected HUD and VA properties, and had more HUD and VA properties inspected by city code inspectors and management brokers.

PRINCIPAL OFFICIALS

RESPONSIBLE FOR ADMINISTERING

THE ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office From	To
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT		
SECRETARY:		
George W. Romney	Jan. 1969	Jan. 1973
James T. Lynn	Feb. 1973	Present
ASSISTANT SECRETARY FOR HOUSING MANAGEMENT:		
Lawrence M. Cox	Feb. 1970	July 1970
Norman V. Watson	July 1970	Present
VETERANS ADMINISTRATION		
ADMINISTRATOR OF VETERANS AFFAIRS:		
D. E. Johnson	June 1969	Present
DEPUTY ADMINISTRATOR OF VETERANS AFFAIRS:		
F. B. Rhodes	May 1969	Present
CHIEF BENEFITS DIRECTOR:		
R. H. Wilson	July 1969	Feb. 1970
O. B. Owen	Feb. 1970	Present
DIRECTOR, LOAN GUARANTY SERVICE:		
J. M. Dervan	Mar. 1961	Jan. 1972
E. A. Echols	Jan. 1972	Present

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