November 22, 1969

NOTE TO SHERMAN UNGER:

Attached are some comments on issues in the title IV new communities regulations. These reflect points that I have had an opportunity to discuss with Hilbert and Nicoson, omitting editorial matters and the like. You should note that the parts of the regulations which are probably most important have been the subject of very little discussion. They largely reflect Nicoson's input; I first saw them a few days ago; and the time I have spent with him since has principally been devoted simply to trying to understand his thinking.

(Signed) John A. Bell, Jr.

John A. Bell

Attachment

JABell:esm
cc: Bell
    Legal
    Chron
Major Questions

1. Inclusion of Land at Value. The regulations (p. 36) provide that where the allowed value for raw land put in by the developer exceeds the price he paid for that land, the Secretary may restrict disbursements of that excess out of the funds borrowed to assure that it is "applied to further the purposes of the Act." Nicoson believes that it is simply not prudent to permit a developer to immediately take out his profit on the land and that to do so simply largly defeats the provisions in the Act which requires the Secretary to establish cost certification or other controls to assure that proceeds from the sale of guaranteed obligations are expended pursuant to a program of land development. He says that even if it is customary to do this in other FHA programs, the reasons for doing so seem dubious when applied to a program where so large, if not the largest part, of the loan proceeds will be for land. Fefferman believes it is necessary as a matter of practice to allow developers to draw out their land value initially. Nicoson would like to be told that he is required to permit this.

2. Staging. The regulations do not provide for the staging of projects, although there is legislative history which contemplates (or can be read to contemplate) that larger projects will typically be staged. Nicoson believes that if there are to be stages in a project, they would be in the order of 5 to 10 years, and he leans toward the upper figure, following particularly the example of the Jonathan proposal which contemplates a 20-year project in two 10-year bites. He bases this upon the view that sufficient time must be allowed to permit the creation of what is truly a new community and that this will probably take 5 to 10 years at the minimum. Fefferman sees no inherent problem with a 10-year stage but views the matter more in terms of the minimum time required to develop and market enough land for housing to offset the costs of central facilities put in at the beginning. It is probably possible to develop some wording for the regulations that would satisfy both ways of looking at the matter. But there may be nevertheless a major question on which a full understanding in fact should be achieved. For to the extent there are stages, the Government has some convenient points for "bailing out" of a project that it considers no longer desirable or prudent; and to the extent the stages are relatively short, the problems of forecasting economic trends, land values and costs in the future, exercising continuing controls, and of making adjustments to reflect all the unanticipated changes in circumstances, are less formidable.

3. Cost Certification or Control Procedures. The regulations, stating the matter generally, contemplate a cost certification procedure that is limited to assuring that the total amount of the guaranteed loan is applied to project
purposes; development costs could, for example, apparently be paid out of borrowings at 100 percent in the early years of a project (or stage) so far at least as the certification and advances system is concerned. By contrast, the FHA title X "cost certification" system is really a device for assuring that the borrower does not get loan funds in excess of what the formula would allow (90 percent of costs) on a continuing basis. This difference in treatment is not without support in the statutory language, but is probably nevertheless a major matter of policy to the extent that the procedure to be adopted is apt to be surprising to those who view the land (and mortgage) as the Government's basic security.

4. Procedure for Issuance. These regulations have not been placed in any clearance (even informal) within the Department; apparently, the thought is that once they are acceptable to MD, the General Counsel and the Under Secretary, they should be published for comment and simultaneously distributed or offered for clearance and comment within HUD. The objective is to save time. Alternatively, a Departmental priority could be placed upon an expeditious clearance within the Department prior to publication for comments by the outside; in the end this might take little if any more time and avoid possible misunderstandings.

Other Questions

a. Appraisal. The regulations do not reflect, or at least reflect very clearly, all of the restrictions on valuation of land before development that appear in the Senate committee report. Adjustments on this point may, however, not be very difficult.

b. Equal Opportunity. The material on this appears technically defective, in that it apparently assumes that there currently are Department-wide regulations under the Executive order on housing. There may also prove to be some policy differences in this area, and in related areas of citizen participation, social planning and the like, within the Department.

c. Prior Costs. The regulations, as currently written, would permit loan proceeds to be used for payment of actual costs of land development contributing to the project, even though these may have been incurred well before an application or proposal was received. There is and has been continuing confusion in this area, and some potentially significant differences in handling between this program and title X of essentially similar problems.

d. Architectural Controls and the like. The regulations contemplate considerable emphasis of the "attractiveness" of a community, extending to continuing architectural controls. This is not a legal matter but Fefferman for one considers that it is a serious mistake to undertake the kind of supervision apparently contemplated.
e. "Equity" Requirements. The regulations appear very general and weak in this area. Some tightening is probably in order.

f. Security. The regulations do not seem very accurately to suggest the Government's "security" under the guarantee arrangements now being contemplated and, in particular, appear to attach considerably greater importance to a mortgage as the Government's security than would in fact be the case.

g. Related Matters. Questions of how cash would be paid as contemplated, and the Government's position in the event of an early unanticipated total default, or failure of Congress to enact legislation to permit Treasury borrowing, etc., all of course not covered in these regulations (and need not be). Presumably, there is some understanding as to just how such things will work.