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Memorandum

U.S. DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT

TO : Samuel C. Jackson, Assistant Secretary
Community Planning and Management

DATE: Dec. 30, 1971

IN REPLY REFER TO:

FROM : William J. Nicoson, Office of
New Communities Development

SUBJECT: New Communities Initiatives

Enclosed is a summary of the initiatives proposed to strengthen the new communities assistance programs which are of sufficient importance to merit reference in the Growth Report and perhaps the State of the Union Address.

The summary of the National Community Development Bank departs in certain respects from the proposal by David Rockefeller in its most recent version (December 23, 1971):

1. No Federal guarantee by the Bank's borrowings is contemplated in the HUD proposal. The latest Rockefeller paper retreats somewhat from this position: "The Bank's ability to sell ... debentures without government guarantee would depend on the establishment and maintenance of a satisfactory credit rating." Under the HUD proposal the Bank's credit rating would have to be improved by an adjustment of the debt-equity ratio.

2. Ten District Banks based on the ten HUD regions are proposed rather than Rockefeller's 12 based on Federal Reserve Districts. Assuming regional decentralization of the new communities programs, the HUD proposal offers a more functional alternative. Furthermore use of Federal Reserve Districts might be interpreted as evidence of a bias favoring stockholders which are commercial banks, thus discouraging participation by other financial institutions.

3. The Board of Directors of the Central Bank in the HUD proposal would have 21 members: the Chairman appointed by the President; the 10 chairmen of the District Banks; and 10 other directors selected by stockholders. Under the Rockefeller proposal, a 25-man Board would be composed of the Chairman appointed by the President; 2 directors appointed by the chairmen of Congressional committees; one director appointed by the chairman of the Federal Reserve Board; the 12 chairmen of District Banks; and 9 other directors selected by stockholders.

4. Assisted development is limited in the HUD proposal to new communities approved by HUD or other development certified by the HUD Secretary as consistent with national growth policy. The Rockefeller proposal would appear to permit Bank financing for any development found by the Bank to comply with growth policy.

5. The mechanics of coordination between HUD and the Bank are spelled out in more detail under the HUD proposal.

You may wish to bring these points to the Secretary's attention.

Before any announcement of the proposal is made, it would be desirable to review the HUD proposal with David Rockefeller or Warren Lindquist. I also recommend that the President, Secretary Romney or Peter Flanigan call a private meeting of leading members of the financial community to discuss the proposal at least 2 weeks prior to any announcement in order to measure support for the Bank and permit comments to be taken into consideration.

Director

Enclosure

cc:
Fred McLaughlin

INITIATIVES TO STRENGTHEN THE NEW COMMUNITIES PROGRAMS

I. Background

1. New Communities and Growth Policy.

By its very nature, new community development addresses the problems of accommodating population growth. The potential of a well-directed Federal program of new community incentives to serve growth policy was recognized in the Urban Growth and New Community Development Act of 1970: Part A of the Act called for policy development by the Domestic Council with biennial reports to Congress; Part B of the Act established the existing new community assistance programs.

Proposed general objectives of growth policy to be included in the first report to Congress are--

-- encouragement of balanced growth: redressing the increasing population imbalance between urban and rural areas;

-- encouragement of orderly growth: planning for the full range of community uses of land properly related one to the other; for an appropriate housing mix within neighborhoods; and for equal opportunity in housing, employment and business enterprise; and

-- strengthening the <u>capacity of state and local government</u> to meet the challenges of growth.

A Federal new communities program which marshals resources to assist new town development in remote locations or in rural growth center locations would clearly serve the objective of encouraging more <u>balanced</u> growth. Wherever located, a Federally assisted new community will by definition serve the objective of more <u>orderly</u> growth, since the Act and regulations require assisted projects to embrace the full range of community uses of land--residential, commercial, industrial, recreational, municipal--properly related to each other by location and linkages under a sound master plan requiring an appropriate housing mix and an affirmative action plan to assure equal opportunity. Finally, land development on a community scale offers opportunities for creative participation by <u>state and local government</u> in the processes of site selection, land acquisition, planning, development and governance.

2. <u>Existing New Community Programs</u>.

Under Part B of the Act, the new community assistance programs are administered by HUD's New Community Development Corporation of which the Secretary of HUD is chairman.

The principal form of assistance is authority to guarantee long-term debt of public or private developers to finance land acquisition and land improvements for approved new communities. To be eligible for guarantees, public-agency developers must waive the Federal tax exemption for interest on guaranteed borrowing, and HUD is authorized to make direct grants in the amount of the increased interest resulting from the waiver. Funding for these grants has not been approved by the Office of Management and Budget, with the result that the program of guarantee assistance offers no incentive for state or local government participation in new community planning and development.

HUD is also authorized to make 20% grants supplementing funds available under 13 basic infrastructure grant programs scattered throughout the Federal Government: mass transit, highways and airports at DOT; hospitals, libraries and institutions of higher education at HEW; water and sewer, open space and community facilities at HUD; recreational land at Interior; water and waste disposal at Agriculture; treatment facilities at EPA; and EDA assistance at Commerce. Supplementary grants are available if the assisted infrastructure will serve a new community meeting HUD's requirements.

Other programs under Part B of the Act include grants and loans for innovative planning by public and private developers and grants to local governments during initial development for public services--neither of which programs have been funded. A program of direct loans to developers to cover interest costs is less attractive than guarantee assistance (which also finances interest costs) and has aroused little interest among developers.

3. Program Activity.

At the end of December 1971, HUD had announced approval of 7 new community projects expected to accommodate a total of some 400,000 people in 20 years. A total of $136.5 million in guarantee authority was committed (of which $97 million was issued). Fees and charges of about $4 million for guarantee assistance had been collected.

More than 50 additional proposals were in various stages of processing, including 10 submitted by public agencies pending resolution of the funding question for tax-waiver grants.

It is estimated that beginning in FY 1973, between 10 and 15 projects per year will be found eligible for assistance. This level of activity would involve annual commitments of between $200 and $300 million in guarantee authority.

4. Shortcomings of Existing Programs.

Major deficiencies of existing authority to assist new community development include the following:

-- The program merely reacts to proposals from private developers with sites selected for reasons largely unrelated to growth policy.

-- The potential for new community development, particularly in rural areas, suffers from lack of incentives for location of industry or other job-producing activities.

-- To meet its full potential in serving growth policy, the new community program will bring heavy pressure to bear on Federal credit resources.

To remedy these shortcomings, HUD has proposed (i) measures which will encourage direct state participation in new community planning and development and (ii) establishment of a privately-financed National Community Development Bank to supplement Federal financing of new community development.

II. Measures to Encourage State Action

1. Implementing Existing Authority to Assist Public Developers.

Acquisition of land and master planning by state agencies for new community development is a powerful tool in the implementation of state growth plans. It permits states to control the location and quality of large-scale urbanization. It is particularly important for development in rural areas where private developers would hesitate to undertake land assembly and development due to high economic risks.

Two alternative forms exist for Federal debt financing of state land assembly, planning and development: guarantees with tax-waiver grants or direct loans. Guarantees with tax-waiver grants have the following advantages:

-- <u>No new legislation</u> is needed, only executive authorization to fund the tax-waiver grant program from collected fees and charges or from treasury borrowings. No appropriation is required.

-- The <u>fiscal impact</u> would be favorable. Unlike other Federal grants, tax-waiver assistance generates revenue (by reason of increased tax collection) as well as outlays. Though it is difficult to predict the fiscal impact with assurance, studies indicate that the increased tax revenue should equal or exceed grant outlays.

-- The <u>budget impact</u> would be favorable. In the absence of statutory exemption of direct loans from the budget (which is opposed by OMB and Treasury), guarantees with tax-waiver grants would have far less impact on the budget than loans for public land assembly, planning and development.

-- Political support exists for implementation of existing authority to assist state action. The Governors' Conference has been actively campaigning for funding of the tax-waiver grants. Leaders of both parties in Congress (e.g., Senators Allott and Humphrey) have urged such funding. Strengthening the role of the states is consistent with the New Federalism.

Some concern has been expressed that implementation of tax-waiver grants (or for that matter direct loans at tax-exempt rates) would extend special assistance to public developers to the disadvantage of private developers. In fact, however, the savings in cost of money by reason of guarantee assistance to the private developer exceeds the savings to the public developer by reason of guarantee assistance with tax-waiver grants. The experience of the New York State Urban Development Corporation indicates that state participation in new community development stimulates rather than competes with private-sector activity.

For fiscal year 1972, HUD requested a reservation of $25 million for tax-waiver grants to assist 3 publicly-developed new communities. The reserved amount would be expended over a 20-year period, with outlays in 1972 amounting to only $100,000, and would be funded entirely from fees and charges or Treasury borrowings rather than appropriations.

2. Financing of New Community Strategies.

Under the existing program, assistance to new community development is extended on a project-by-project basis. It is proposed that, upon approval by HUD of a state strategy for new community development (including detailed criteria to be followed), financing for land acquisition and development in the furtherance of that strategy be made available to the state agency without submission or approval of plans for each new community. Assistance for any year would be limited to $50 million for any one state, but a state could borrow against allocations of up to 4 future years.

The advantages of this initiative include the following:

-- Avoiding the necessity of project-by-project review and approval will encourage long-term state planning for growth.

-- Financing strategy rather than individual projects permits borrowing aggregation with lower interest rates, lower financing costs and less cumbersome financing procedures.

3. Grants to States for Administrative Costs.

This proposal would authorize $12,500,000 in the first year to make available a sum of up to $250,000 per state. The grant would be renewed for a second year, but not thereafter. It could be used to pay for personnel, for planning costs, for the conduct of management training in new community development, or related purposes. If states wished, they could combine this with their share of planning funds for land use planning, which the Administration's bill on that subject would authorize, and use the same entity for both purposes.

While this proposal involves the establishment of a new categorical grant program, it is believed necessary, particularly in rural states, to encourage the creation of public agencies for new community land assembly and development.

III. NATIONAL COMMUNITY DEVELOPMENT BANK

A Federally-chartered, privately financed National Community Development Bank is proposed to work in tandem with HUD's New Community Development Corporation.

1. Functions.

The Bank would finance land acquisition and land improvements by private developers for new communities meeting HUD's requirements, but only after neutralization of "political risks" such as controversy endangering zoning and other local approvals. The Bank would make its own assessment of economic feasibility and would finance only projects representing an acceptable "business risk."

The Bank, through the wide contacts of its members, would also assist in attracting commercial and industrial activities to approved new communities.

Developers would be free to arrange private financing from other sources; and the Bank would not engage in the financing of construction or other activities for which financing was readily available from commercial sources.

2. Organization.

The Bank would consist of a Central Bank and a District Bank System.

The Central Bank would have a board of 21 directors of which the chairman would be appointed by the President, 10 directors would be chairmen of the 10 District Banks and 10 directors selected by the stockholders of the Bank. Stockholders would be members of both the Central Bank and the District Bank in which they are headquartered.

Each of the 10 HUD regions would also be a Community Development Bank District. Each District Bank would be a subsidiary of the Central Bank and subject to its policies and regulations.

The Board of Directors of the District Bank would consist of directors appointed by each state Governor in the District and an equal number of directors selected by

District stockholders. A chairman would be elected by these directors but not from among them.

3. Capitalization

It is proposed that the Bank seek equity contributions from all types of financial institutions as well as interested industrial and commercial companies. Initial equity contributed or committed in the amount of $100 million would probably support borrowings of $400 million.

The Bank would borrow in national markets as needed to fund its loans. Its borrowings would not be Federally guaranteed. If its interest costs should prove too high to permit loans at an acceptable cost to developers, the Bank's recourse would be modification of its debt-to-equity ratio.

It is contemplated that the return to investors would be of a "limited dividend" nature, but that the risk would not be disproportionate to the yield.

4. Financing Procedures

An application for assistance from HUD's NCDC would be studied simultaneously by the Bank. Commitments by each would be coordinated, though NCDC might extend assistance in the absence of a Bank commitment. The Bank would assist only new community projects approved by NCDC or other development projects certified by the Secretary of HUD as consistent with national growth objectives.

Upon approval of a developer's application, NCDC would enter into an agreement with the developer requiring development to proceed in accordance with a detailed plan and providing guarantee assistance by NCDC. Simultaneously the Bank would enter into a commitment with the developer that, upon the occurrence of specified events (such as zoning and other local approvals), it stood ready at the developer's option to take out the guaranteed debt. NCDC's guarantee assistance would be terminated at that time. The developer would be free to refund through the Bank or through other private sources.

Termination of guarantee assistance would not, however, terminate the developer's obligation to NCDC to perform in accordance with the approved plan, and NCDC would continue to monitor the developer's performance. The property securing the guarantee obligation would be freed to secure repayment to the Bank (or other lender), and rights of acceleration and foreclosure would pass from NCDC to the Bank (or other lender). NCDC would retain other remedies (including the exercise of voting control of the developer) in the event of performance default.

5. <u>Advantages</u>

The proposed Bank would:

- facilitate attraction of a job base to new communities;

- relieve heavy pressures on Federal credit resources;

-- make available a new source of funds for new community development; and

-- supplement Federal expertise in the review process, particularly as to economic feasibility.

6. Related Proposals

A memorandum dated November 29, 1971 from John R. Price proposes establishment of a National Growth Bank, as a separate Federal agency, to administer the new community assistance programs. It is apparently intended that the existing program of guarantee assistance would be supplanted by direct loans. The Bank would also have power to acquire land in order to guide growth in accordance with national policy.

For the reasons mentioned above, HUD believes the existing guarantee program (with tax waiver grants for public developers) is preferable to a new loan program. HUD also believes that the land assembly function can best be carried out at the state level of government. If, however, a new Bank is proposed by the Administration to replace HUD's NCDC, it should be created within the proposed Department of Community Development which will administer essential complementary programs of assistance, particularly assistance for low and moderate income housing.

Should a National Growth Bank, in whatever form, replace HUD's NCDC, it would be able to work in conjunction with the privately-financed National Community Development

Bank in the manner outlined above. The two Banks should not be viewed as mutually exclusive alternatives.

Similarly, creation of a Rural Credit Corporation within the Department of Agriculture to finance programs of the Farmers Home Administration would not in any way duplicate functions of the proposed National Community Development Bank, although such a Corporation might be inconsistent with the Federal Financing Bank proposed by the Treasury Department and supported by HUD.