Consolidated Financial Statements

The consolidated financial statements have been prepared to report the financial position, results of operations, and cash flows of the Department of Housing and Urban Development, pursuant to the requirements of the Chief Financial Officers Act of 1990 (31 U.S.C. 3515 (b)). While the financial statements have been prepared from HUD's books and records in accordance with formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The consolidated financial statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. One implication is that liabilities reported in the financial statements cannot be liquidated without legislation that provides resources to do so.

The consolidated financial statements included in this annual report are as follows:

- Statement of Financial Position;
- Statement of Operations; and
- Statement of Cash Flows.

These financial statements include all of HUD's activities, including those of the Federal Housing Administration and the Government National Mortgage Association. All of HUD's budget authority is covered by these financial statements.

Department of Housing and Urban Development
Consolidated Statement of Financial Position
As of September 30, 1997 and 1996

Dollars in Millions	1997	1996
ASSETS		
Entity Assets:		
Intragovernmental Assets:		
Fund Balance with U.S. Treasury, (Note 2)		
Non-interest bearing	$ 75,287	$ 91,624
Interest bearing	759	1,542
Total Fund Balance with U.S. Treasury	76,046	93,166
Investments (Note 4)	18,770	12,604
Other Intragovernmental Assets	276	212
Governmental Assets:		
Foreclosed Property Held for Sale, Net (Note 5)	1,476	1,169
Mortgage Notes and Loans Receivable, Net (Note 6)	9,843	12,781
Other Governmental Assets	1,456	794
Total Entity Assets	$107,867	$120,726
Non-Entity Assets:		
Intragovernmental Assets:		
Fund Balance with U.S. Treasury, (Note 2)	$ 81	$ 41
Governmental Assets:		
Other Non-Entity Assets	510	543
Total Non-Entity Assets	591	584
TOTAL ASSETS	$108,458	$121,310
LIABILITIES AND NET POSITION		
Liabilities Covered by Budgetary Resources:		
Intragovernmental Liabilities:		
Accounts Payable and Accrued Expenses	$ 876	$ 1,022
Borrowings (Note 8)	36	39
Other Intragovernmental Liabilities	195	42
Governmental Liabilities:		
Accounts Payable and Accrued Expenses	802	733
Distributive Shares and Premium Refunds Payable	180	154
Claims Payable	388	653
Loss Reserves (Note 7)	13,657	13,458
Unearned Premiums	7,221	6,931
Debentures Issued to Claimants	68	82
Other Governmental Liabilities	102	114
Total Liabilities Covered by Budgetary Resources:	$ 23,525	$ 23,228
Liabilities Not Covered by Budgetary Resources		
Intragovernmental Liabilities:		
Borrowings (Note 8)	$ 11,374	$ 11,659
Governmental Liabilities:		
Accounts Payable and Accrued Expenses	139	134
Borrowings (Note 8)	3,586	3,861
Total Liabilities Not Covered by Budgetary Resources	$ 15,099	$ 15,654
TOTAL LIABILITIES	$ 38,624	$ 38,882
Commitments and Contingencies (Notes 3, 10 and 11)		
NET POSITION (Note 9):		
Mutual Insurance Funds Equity	$ 2,662	$ 2,526
Invested Capital	15	10
Unexpended Appropriations Held for Commitments	70,265	84,381
Cumulative Results of Operations	(15,297)	(15,999)
Future Funding Commitments	(6,092)	(6,429)
Appropriated Capital	18,281	17,939
Total Net Position	$ 69,834	$ 82,428
TOTAL LIABILITIES AND NET POSITION	$108,458	$121,310

The accompanying notes are an integral part of these financial statements.

Department of Housing and Urban Development
Consolidated Statement of Operations
For the Years Ended September 30, 1997 and 1996

Dollars in Millions	1997	1996
REVENUES AND FINANCING SOURCES:		
Operating Revenues:		
FHA Premiums	$ 2,486	$ 2,142
GNMA Mortgage Backed-Securities Program Income	354	335
Interest and Penalties, Non Federal	971	1,060
Interest, Federal	1,133	1,037
Other	187	91
Financing Sources:		
Appropriated Capital Used	31,588	32,391
Imputed Financing Sources	11	
Total Revenues and Financing Sources	$36,730	$37,056
EXPENSES:		
Section 8 Subsidies	$15,257	$16,480
Community Development Block Grants	4,491	4,526
Operating Subsidies	2,812	2,777
Low Rent Public Housing Grants	3,918	3,879
HOME	1,211	1,201
Other Subsidies, Grants and Loans	3,123	2,804
Mortgage-Backed Securities Program Expenses	30	27
Increase in Loss Reserves	163	1,921
Provision for Losses on Foreclosed Properties	2,232	1,975
Provision for Losses on Mortgage Notes and Loans	461	(714)
(Gain) on Sale of Mortgage Notes	(92)	(187)
Interest		
Non Federal	5	101
Federal	924	988
Salaries and Administration	1,229	1,140
Other	138	87
Total Expenses	$35,902	$37,005
EXCESS OF REVENUES AND FINANCING SOURCES OVER EXPENSES	$ 828	$ 51

The accompanying notes are an integral part of these financial statements.

Department of Housing and Urban Development
Consolidated Statement of Cash Flows
For the Years Ended September 30, 1997 and 1996

Dollars in Millions	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES:		
Excess of Revenues and Financing		
Sources over Expenses	$ 828	$ 51
Adjustments to Reconcile Excess to		
Net Cash Used by Operating Activities:		
Appropriated Capital Used	(31,588)	(32,391)
Increase in Loss Reserves	163	1,921
Provision for Losses on Foreclosed Properties	2,232	1,975
Provision for Losses on Mortgage Notes and Loans	447	(758)
Loss (Gain) on Mortgage Notes Held for Sale	(92)	(187)
Premiums Earned	(1,205)	(1,058)
Premiums Collected	1,789	1,722
Premiums Refunded	(294)	(418)
Claims Settlement Payments	(6,131)	(5,542)
Collection of Principal on Notes Acquired in Claims Settlement	187	232
Proceeds from Disposition of Assets Acquired in Claims Settlement	5,986	6,534
Increase in Payables and Other Liabilities	(210)	96
Decrease (Increase) in Receivables and Other Assets	(685)	1,204
Other, Net	(73)	(91)
Net Cash Used by Operating Activities	$(28,646)	$(26,710)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Investment Securities	$(19,203)	$ (8,141)
Proceeds from Sale of Investment Securities	13,181	6,657
Proceeds from Disposal of Mortgages	4	4
Principal Collections on Mortgages and Loans	146	146
Acquisition of Assets	(170)	(142)
Other, Net	4	
Net Cash Provided (Used) by Investing Activities	$ (6,038)	$ (1,476)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Appropriations Received	$ 18,891	$ 23,959
Cash Returned to Treasury	(723)	(938)
Borrowings from U.S. Treasury	589	1,567
Issuance of Debentures to Claimants	47	65
Payment of Borrowings	(1,152)	(1,277)
Payment of Debentures	(61)	(70)
Distributive Shares Paid	(1)	(2)
Transfers from other Agencies	7	7
Other, net	8	471
Net Cash Provided by Financing Activities	$ 17,605	$ 23,782
Net (Decrease) Increase in Cash	$(17,079)	$ (4,404)
Funds With U.S.Treasury, Non-interest bearing – Beginning of Year	93,207	97,611
Funds With U.S.Treasury, Non-interest bearing – End of Year	$ 76,128	$ 93,207

The accompanying notes are an integral part of these financial statements.

Note 1 – Entity and Mission

The U.S. Department of Housing and Urban Development (HUD) was created in 1965 to (1) provide housing subsidies for low and moderate income families, (2) provide grants to states and communities for community development activities, (3) provide direct loans for construction and rehabilitation of housing projects for the elderly and persons with disabilities, and (4) promote and enforce fair housing and equal housing opportunity. In addition, HUD insures mortgages for single family and multifamily dwellings; insures loans for home improvements and manufactured homes; and facilitates financing for the purchase or refinancing of millions of American homes.

HUD's major programs are as follows:

The **Federal Housing Administration** (FHA) was created as a Government corporation within HUD and administers some 40 active mortgage insurance programs which are designed primarily to serve first-time home buyers and to provide affordable multifamily housing, and include insurance of loans for property improvements, cooperatives, condominiums, housing for the elderly and persons with disabilities, land development, group practice medical facilities and nonprofit hospitals.

The **Government National Mortgage Association** (Ginnie Mae) was created as a Government corporation within HUD to administer mortgage support programs that could not be carried out in the private market. Ginnie Mae guarantees the timely payment of principal and interest on mortgage-backed securities issued by approved private mortgage institutions and backed by pools of mortgages insured or guaranteed by FHA, the Rural Housing Service (RHS), and the Department of Veterans Affairs (VA).

The **Section 8 Rental Assistance** programs assist low- and very low-income families in obtaining decent and safe rental housing. HUD makes up the difference between what a low- and very low-income family can afford and the approved rent for an adequate housing unit.

Operating Subsidies are provided to Public Housing Authorities (PHAs) and Indian Housing Authorities (IHAs) to assist in financing the operations and maintenance costs of their housing projects.

The **Community Development Block Grant** (CDBG) programs provide funds for metropolitan cities, urban counties, and other communities to use for neighborhood revitalization, economic development, and improved community facilities and services.

The **Low Rent Public Housing Grants** program provides grants to PHAs and IHAs for construction and rehabilitation of low-rent housing. This program is a continuation of the **Low Rent Public Housing Loan** program which pays principal and interest on long-term loans made to PHAs and IHAs for construction and rehabilitation of low-rent housing.

The **Section 202/811 Supportive Housing for the Elderly and Persons with Disabilities** programs, prior to fiscal 1992, provided 40 year loans to nonprofit organizations sponsoring rental housing for the elderly or disabled. During fiscal 1992, the program was converted to a grant program. The grant programs provide long-term supportive housing for the elderly (Section 202) and disabled (Section 811).

The **HOME Investments Partnerships** program provides grants to States, local Governments, and Indian tribes to implement local housing strategies designed to increase home ownership and affordable housing opportunities for low- and very low-income Americans.

Other Programs not included above consist of about 40 smaller programs which provide grant, subsidy funding, and direct loans to support other HUD objectives such as fair housing and equal opportunity, energy conservation, assistance for the homeless, rehabilitation of housing units, and home ownership. These programs comprise approximately 8.5 percent of HUD's consolidated assets and 7.7percent of HUD's consolidated revenues and financing sources for fiscal 1997, and 7.2 percent of HUD's consolidated assets and 6.8 percent of HUD's consolidated revenues and financing sources for fiscal 1996.

Note 2 – Summary of Significant Accounting Policies

A. Basis of Consolidation

The consolidated financial statements include all funds and programs for which HUD is responsible. All significant intra-fund balances and transactions have been eliminated in consolidation. Transfer appropriations are consolidated into the financial statements based on an evaluation of their relationship with HUD.

B. Basis of Accounting

The consolidated financial statements include the accounts and transactions of the Ginnie Mae, FHA, and HUD's Grant, Subsidy and Loan programs. These statements are different than the reports prepared to monitor and control the obligation and expenditure of budgetary resources, which are prepared from the same records.

The statements are presented in accordance with the Office of Management and Budget (OMB) Bulletin 97-01, Form and Content of Agency Financial Statements, as it applies to the fiscal 1997 financial statements, with the exception of the Statement of Federal Financial Accounting Standards Number 2 (SFFAS Number 2) requirements. HUD deviates from SFFAS Number 2 accounting and financial statements presentation requirements. Discussion of HUD's basis of accounting for post 1991 Loans and Loan Guarantees is discussed in Note 13.

The financial statements are presented on the accrual basis of accounting. Under this method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Generally, procedures for HUD's major grant and subsidy programs require recipients to request periodic disbursement concurrent with incurring eligible costs.

C. Operating Revenue and Financing Sources

HUD operations are principally financed by appropriations, collection of premiums and fees on its FHA and Ginnie Mae programs, and interest income on its mortgage notes, loans, and investments portfolio.

Appropriations for Grant and Subsidy Programs

HUD receives appropriations on both an annual and multiyear basis. Appropriations are recognized as revenue when related program expenses are incurred. Accordingly, for grants provided by HUD, revenue and related expenses are recognized as recipients perform under the contracts. For subsidies provided by HUD, revenue and related expenses are recognized when the underlying assistance (e.g., provision of a Section 8 rental unit by a housing owner) is provided.

FHA Premiums and Unearned Revenue

Prior to July 1991, FHA's largest activity, the insurance of single family mortgages by the Mutual Mortgage Insurance (MMI) Fund, charged a one-time premium upon initiation of insurance. On July 1, 1991, the premiums charged by FHA for this insurance were restructured to include both an up-front and a risk-based annual premium. The one-time and up- front premiums are recorded as unearned revenue upon collection and are recognized as revenue over the period in which losses and insurance costs are expected to occur. The risk-based annual premiums are recognized on a straight-line basis throughout the year. FHA's other activities, including most of those conducted through the General Insurance (Gl) and Special Risk Insurance (SRI) Funds, charge periodic premiums over the mortgage insurance term. Premiums on annual installment policies are earned on a straight-line basis throughout the year.

Ginnie Mae Fees

Fees received for Ginnie Mae's guaranty of mortgage-backed securities are recognized as earned on an accrual basis. Fees received for commitments to subsequently guarantee mortgage-backed securities and commitments to fund mortgage loans are recognized when commitments are granted.

D. Loss Reimbursements Financed by Credit Reform Appropriations

FHA's Gl and SRI funds are not intended to be self-sustaining. As a result, the National Housing Act, as amended, provides for appropriations from Congress to cover losses in these funds. The Credit Reform Act of 1990 changed the method by which FHA receives appropriations from Congress. Beginning in fiscal 1992, appropriations to the GI and SRI Funds are made at the beginning of each fiscal year to cover estimated losses on loans to be insured during that year. The revised appropriation structure also authorizes permanent indefinite appropriation authority to finance the cash requirements of operations resulting from endorsements in years prior to fiscal 1992.

E. Future Funding Commitments

HUD is responsible for repaying borrowings incurred by certain public housing organizations from private investors and the Federal Financing Bank. However, appropriations to repay these borrowings are obtained on an annual basis. Since HUD is ultimately responsible for repaying these borrowings, they have been recorded as a liability in the Consolidated Statement of Financial Position (included in "Borrowings"), and a deficiency in HUD's net position has also been recorded and is referred to as "future funding commitments."

F. Fund Balance with the U.S. Treasury

Substantially all of HUD's receipts and disbursements are processed by the U.S. Treasury which, in effect, maintains HUD's bank accounts. HUD's fund balances with the U.S. Treasury as of September 30, 1997, were as follows (dollars in millions):

	Obligated	Unobligated		Total
Description		Available	Restricted	
Appropriated Funds	$51,512	$17,708	$116	$69,336
Revolving Funds	5,465	1,224	21	6,710
Total – Entity Fund Balance	$56,977	$18,932	$137	$76,046
Non-Entity Fund Balance with the U.S. Treasury	$ 64	$ 17	$ –	$ 81

HUD's fund balances with the U.S. Treasury as of September 30, 1996, were as follows (dollars in millions):

	Obligated	Unobligated		Total
Description		Available	Restricted	
Appropriated Funds	$70,814	$12,650	$60	$83,524
Revolving Funds	8,882	760	–	9,642
Total – Entity Fund Balance	$79,696	$13,410	$60	$93,166
Non-Entity Fund Balance with the U.S. Treasury	$ 21	$ 20	$ –	$ 41

The substantial portion of the obligated fund balance is required for payment of HUD's commitments under its various grant, subsidy, and loan programs. The majority of funds designated as "Available" above represent administrative commitments. Administrative commitments are reservations of funds for a specific project by HUD (for which a contract has not been executed) to obligate all or a part of those funds. Both commitments and reservations are discussed in greater detail in Note 3. Restricted fund balances relate to funds for which the related appropriation has expired. These funds can only be used for payment of unrecorded or under-recorded obligations relating to the expired appropriation, until the account is closed and returned to Treasury. Non-entity fund balances relate to transfer appropriations.

In accordance with the Federal Credit Reform Act of 1990 (Credit Reform), all cash generated by FHA from insurance endorsed on or after October 1, 1991, is deposited in an interest-bearing account. The account earns interest at a rate based on maturity intervals of 10 years and longer, as determined by the U.S. Treasury.

Prior to Credit Reform, cash generated from FHA insurance endorsements, and not needed for short term operating purposes was invested in non-marketable U.S. Government Securities with terms similar to Government securities that are publicly marketed.

For purposes of the Consolidated Statement of Cash Flows, HUD's funds in the U.S. Treasury (including FHA's non-interest-bearing funds) are considered cash. FHA's interest-bearing funds at the U.S. Treasury are considered an investing activity, since Credit Reform did not, in substance, change the liquidity of the funds.

G. Investments in U.S. Government Securities

HUD's investments, which principally comprise investments by FHA's MMI Fund and by Ginnie Mae, are limited to non-marketable Treasury interest-bearing obligations (i.e., investments not sold in public markets). The market value and interest rates established for such investments are the same as those for similar Treasury issues which are publicly marketed.

HUD's investment decisions are limited by Treasury policy which: (1) only allows investment in Treasury notes, bills, and bonds; and (2) prohibits HUD from engaging in practices that result in "windfall" gains and profits, such as security trading and full scale restructuring of portfolios, in order to take advantage of interest rate fluctuations.

FHA's normal policy is to hold investments in U.S. Government securities to maturity. However, as a result of Credit Reform, cash collected on insurance endorsed on or after October 1, 1991, is no longer available to invest in U.S. Government securities, and may only be used to finance claims emanating from insurance endorsed during or after fiscal 1992. FHA may have to liquidate its U.S. Government securities before maturity to finance claim payments from pre-fiscal year 1992 insurance endorsements. However, management does not expect early liquidation of any U.S. Government Securities and believes it has the ability to hold these securities to maturity.

Investments in U.S. Government securities are reported at amortized cost. Premiums or discounts are amortized into interest income over the term of the investment. HUD's intent is to hold investments to maturity, unless needed for operations. No provision is made to record unrealized gains or losses on these securities because, in the majority of cases, they are held to maturity.

H. Mortgage Notes and Loans Receivable

HUD finances mortgages and provides loans to support construction and rehabilitation of low rent housing, principally for the elderly and disabled under the Section 202 program. Prior to April 1996, mortgages were also assigned to HUD through FHA claims settlement (i.e., mortgage notes assigned, MNAs). Single family mortgages were assigned to FHA when the mortgagor defaulted due to certain "temporary hardship" conditions beyond the control of the mortgagor, and when, in management's judgment, it is likely that the mortgage could be brought current in the future. In addition, multifamily mortgages were assigned to FHA when lenders filed mortgage insurance claims for defaulted notes.

During 1996, Congress mandated that FHA discontinue the single family assignment program and develop and implement a loss mitigation program to reduce defaults and related costs. FHA, however, continues to take single family assignment on those defaulted mortgage notes that were in process at the time the assignment program was terminated. In addition, multifamily and single family performing notes insured pursuant to Section 221(g)(4) of the National Housing Act may be assigned automatically to FHA at a pre-determined point.

Mortgage notes and loans are recorded at the lower of cost or fair value. Fair value is estimated based on prevailing market interest rates at dates of mortgage assignment. When fair value is less than cost, discounts are recorded and amortized to interest income over the remaining terms of the mortgages or upon sale of the mortgages. Interest is recognized as income when earned. When full collection of principal is considered doubtful, an allowance for losses is recorded. The allowance is estimated based on historical loss rates and recovery rates resulting from asset sales and property recovery rates, net of cost of sales. Mortgages and loans are reported net of the allowance for loss and any unamortized discount.

I. Foreclosed Property Held for Sale

Foreclosed property held for sale is reported at cost (the amount of the mortgage claim paid by HUD) net of an allowance for loss, which is established to reduce the property carrying value to its fair value – the amount HUD expects to receive in cash upon sale of the property – less cost of sale. Foreclosure holding and disposition costs are charged to operations as incurred.

J. Accrued Unfunded Leave and FECA Liabilities

Annual leave and compensatory time are accrued as earned and the liability is reduced as leave is taken. The liability at year-end reflects cumulative leave earned but not taken, priced at current wage rates. Funding for earned leave deferred to future periods is to be provided by future appropriations. HUD offsets this unfunded liability by recording future financing sources in the Net Position section of its Statement of Financial Position. Sick leave and other types of leave are expensed as taken.

HUD also accrues the portion of the estimated liability for disability benefits assigned to the agency under the Federal Employees Compensation Act (FECA), administered and determined by the Department of Labor. The liability is based on the net present value of estimated future payments based on a study conducted by the Department of Labor and is $57 million as of September 30, 1997. Future payments on this liability are to be funded by future appropriations. HUD offsets this unfunded liability by recording future financing sources.

K. Loss Reserves

HUD records loss reserves for its mortgage insurance programs operated through FHA and its financial guaranty programs operated by Ginnie Mae. FHA loss reserves are recorded for actual or probable defaults of FHA-insured mortgage loans. Ginnie Mae reserves are established for actual and probable defaults of issuers of Ginnie Mae-guaranteed mortgage-backed securities. Such reserves are based on management's judgment about historical claim and loss information and current economic factors.

L. Retirement Plans

The majority of HUD's employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). FERS went into effect pursuant to Public Law 99-335 on January 1, 1987. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired before January 1, 1984, can elect to either join FERS and Social Security or remain in CSRS. HUD expenses its contributions to the retirement plans.

A primary feature of FERS is that it offers a savings plan whereby HUD automatically contributes 1 percent of pay and matches any employee contribution up to an additional 4 percent of pay. Under CSRS, employees can contribute up to 5 percent of their pay to the savings plan, but there is no corresponding matching by HUD. Although HUD funds a portion of the benefits under FERS relating to its employees and makes the necessary withholdings from them, it has no liability for future payments to employees under these plans, nor does it report CSRS, FERS, or FECA assets, accumulated plan benefits, or unfunded liabilities applicable to its employees. These amounts are reported by the Office of Personnel Management (OPM) and are not allocated to the individual employers. HUD's matching contributions to these retirement plans during fiscal 1997 and 1996 were $53 million and $55 million, respectively.

M. Pension and Other Retirement Benefits

The Department's pension and other retirement benefit expenses totaled approximately $100 million for fiscal 1997. This amount includes $11.4 million to be funded by the OPM. Pursuant to the requirements of SFFAS Number 5, adopted during fiscal 1997, amounts funded by OPM are to be charged to expense with a corresponding amount considered as an imputed financing source. This imputed financing source is included as "Other Revenue and Financing Sources" in the statement of operations.

N. Reclassifications

Reclassifications were made to the FHA's fiscal 1996 financial statements to conform with the presentation used in 1997. The changes in classifications have no effect on the previously reported net income.

Note 3 – Commitments Under HUD's Grant, Subsidy, and Loan Programs

HUD has entered into extensive long-term contractual commitments under its various grant, subsidy and loan programs. These commitments consist of legally binding agreements the Department has entered into to provide grants, subsidies, or loans. Commitments become liabilities when all actions required for payment under an agreement have occurred. The mechanism for funding for these commitments generally differs, depending on whether the agreements were entered into before or after 1988.

Prior to fiscal 1988, HUD's subsidy programs, including the Section 8 program, HUD's largest, operated under contract authority. Each year, Congress provided HUD the authority to enter into multiyear contracts within annual and entire contract limitation ceilings. HUD then drew on and continues to draw on permanent indefinite appropriations to fund the current year's portion of those multiyear contracts. Because of the duration of these contracts (up to 40 years), significant authority exists to draw on the permanent indefinite appropriations. Beginning in fiscal 1988, the Section 8 program began operating under multiyear budget authority whereby the Congress appropriates the funds "up front" for the entire contract term in the initial year, the effect of which substantially increases HUD's net position.

As shown below, appropriations to fund a substantial portion of these commitments will be provided through permanent indefinite authority. These commitments relate primarily to the Section 8 program, and the Section 235/236 rental assistance and interest reduction programs, and are explained in greater detail below.

HUD's commitment balances are based on the amount of unliquidated obligations recorded in HUD's accounting records with no provision for changes in future eligibility, and thus are equal to the maximum amounts available under existing agreements and contracts. Unexpended appropriations shown in the Consolidated Statement of Financial Position comprise funds in the U.S. Treasury available to fund existing commitments that were provided through "up- front" appropriations, and also include permanent indefinite appropriations received in excess of amounts used to fund the pre-1988 subsidy contracts.

HUD's obligations and contractual commitments under its grant, subsidy, and loan programs as of September 30, 1997, and 1996 were as follows (dollars in millions):

	1997			1996		
	Commitments Funded Through			Commitments Funded Through		
Programs	Unexpended Appropriations	Permanent Indefinite Appropriations	Total Contracted Commitments	Unexpended Appropriations	Permanent Indefinite Appropriations	Total Contracted Commitments
Section 8 Rental Assistance	$19,468	$47,479	$ 66,947	$38,557	$47,590	$ 86,147
Community Development Block Grants	8,796	–	8,796	8,490	–	8,490
HOME Investment Partnership Program	3,506	–	3,506	3,345	–	3,345
Low Rent Public Housing Grants and Loans	8,460	–	8,460	9,663	–	9,663
Operating Subsidies	1,524	–	1,524	1,549	–	1,549
Section 202/811	3,210	–	3,210	2,759	–	2,759
Section 235/236	130	12,210	12,340	147	13,070	13,217
All Other	5,736	160	5,896	5,991	206	6,197
Total	$50,830	$59,849	$110,679	$70,501	$60,866	$131,367

With the exception of the Section 202 and Low Rent Public Housing Loan Programs, which have been converted to a grant program and Section 235/236, and a portion of "all other" program HUD management expects all of the above programs to continue to incur new commitments under authority granted by Congress in future years. However, estimated future commitments under such new authority are not included in the amounts above.

In addition to contractual commitments, HUD has entered into administrative commitments which are reservations of funds for specific projects (including those for which a contract has not yet been executed) to obligate all or part of those funds. At the time of contract execution, the administrative commitments become contractual commitments.

HUD's reservation balance as of September 30, 1997, and 1996, were as follows (dollars in millions):

	1997			1996		
	Reservations Funded Through			Reservations Funded Through		
Programs	Unexpended Appropriations	Permanent Indefinite Appropriations	Total Reservations	Unexpended Appropriations	Permanent Indefinite Appropriations	Total Reservations
Section 8 Rental Assistance	$2,656	–	$2,656	$3,679	–	$3,679
Low Rent Public Housing Grants and Loans	1,697	–	1,697	1,662	–	1,662
Section 202/811	2,414	$ 73	2,487	2,673	$73	
2,746						
All Other	1,393	35	1,428	1,420	16	1,436
Total	$8,160	$108	$8,268	$9,434	$89	$9,523

The amount required to fund each of the Department's Section 8 contracts is based on estimated information such as the number of rental units, household income, inflation, and unit rent. This estimated information will differ from actual information over the term of the contract. Accordingly, the actual amounts to be paid over the remaining terms of each Section 8 contract may be more or less than the remaining funds available under each contract. During fiscal 1997, the Department estimated that there was approximately $9.9 billion of excess commitments (budget authority originally received which will not be needed to fund the related contracts to their expiration) relating to the Section 8 Rental Voucher and Rental Certificate programs. Of this amount, approximately $7.7 billion was subsequently recaptured of which $3.65 billion was rescinded and the remaining amount was transferred to the "Section 8 Reserve Preservation Account." The fiscal 1997 Section 8 contractual commitments included in the chart above reflects the amount of the recapture and rescission.

Where HUD has estimated that the funds provided in the Section 8 contracts will not be sufficient to fully fund the contracts over their remaining terms, additional amendment funds are requested from Congress. HUD is currently in the process of estimating the amount of these amendment funds that will be needed over the remaining terms of contracts relating to project based Section 8 programs.

Note 4 – Investments in U.S. Government Securities

The U.S. Government securities are non-marketable securities. Interest rates are established by the U.S. Treasury and during fiscal 1997 ranged from 5.2 percent to 6.1 percent annually. During fiscal 1996 interest rates ranged from 4.7 percent to 8.5 percent annually. The amortized cost and estimated market value of investments in debt securities as of September 30, 1997 and 1996, were as follows (dollars in millions):

Fiscal Year	Cost	Amortized (Premium) Discount	Net Investments	Unrealized Gain	Unrealized Loss	Required Market Value Disclosure
FY 1997	$19,017	$(247)	$18,770	$380	$ (33)	$19,117
FY 1996	$12,660	$ (56)	$12,604	$240	$(151)	$12,693

Note 5 – Foreclosed Property Held for Sale

Foreclosed property held by HUD is principally obtained by FHA via claims settlement. Properties may also be acquired through foreclosure on direct loans under the Section 202 Program and the Section 312 Rehabilitation Loan Program. These result from financial default or non-compliance with other terms of the loan agreements, and through foreclosures on properties out of defaulted issuer pools serviced by Ginnie Mae. Foreclosed properties consisted of the following classes of property as of September 30, 1997, (dollars in millions):

Description	FHA	Ginnie Mae	All Other	Total
Single Family	$2,435	$1	$2	$2,438
Multifamily	355	–	1	356
Title I	–	4	–	4
Total Property	2,790	5	3	2,798
Allowance for Losses	(1,319)	(2)	(1)	(1,322)
Property Net	$1,471	$3	$2	$1,476

Foreclosed properties consisted of the following classes of property as of September 30, 1996, (dollars in millions):

Description	FHA	Ginnie Mae	All Other	Total
Single Family	$1,860	–	–	$1,860
Multifamily	490	–	$3	493
Title I	–	$8	–	8
Total Property	2,350	8	3	2,361
Allowance for Losses	(1,188)	(2)	(2)	(1,192)
Property Net	$1,162	$6	$1	$1,169

The allowance for losses is recorded to reduce the property carrying value to the amount HUD expects to receive in cash when properties are sold. The allowance is necessary because historically HUD has not recovered the full cost of its foreclosed property.

Note 6 – Mortgage Notes and Loans Receivable

HUD's mortgage notes and loans receivable as of September 30, 1997, were as follows (dollars in millions):

Description	FHA	Ginnie Mae	Low Rent Loans	Section 202 Loans	All Other Loan Programs	Total
Single Family	$ 677	$7	–	–	$ 137	$ 821
Title I	356	–	–	–	–	356
Multifamily	2,256	–	$45	$8,228	914	11,443
Total Mortgages and Loans	3,289	7	45	8,228	1,051	12,620
Unearned Discounts and Allowances for Losses	(2,117)	(3)	(10)	(21)	(626)	(2,777)
Mortgages and Loans, Net	$1,172	$4	$35	$8,207	$ 425	$ 9,843

HUD's mortgage notes and loans receivable as of September 30, 1996, were as follows (dollars in millions):

Description	FHA	Ginnie Mae	Low Rent Loans	Section 202 Loans	All Other Loan Programs	Total
Single Family	$3,023	$2	–	–	–	$ 3,025
Title I	294	–	–	–	–	294
Multifamily	3,259	–	$45	$8,307	$1,044	$12,655
Total Mortgages and Loans	6,576	2	45	8,307	1,044	15,974
Unearned Discounts and Allowances for Losses	(2,605)	(1)	(10)	(21)	(556)	(3,193)
Mortgages and Loans, Net	$3,971	$1	$35	$8,286	$ 488	$12,781

Interest income for the year ended September 30, 1997, was $253 million on FHA notes, $2 million on Low Rent Public Housing loans, $698 million on Section 202 loans and $18 million on all other loans. For the year ended September 30, 1996, interest income was $271million on FHA notes, $3 million on Low Rent Public Housing Loans, $763 million on Section 202 loans and $21.3 million on all other loans.

FHA mortgages and loans on which the accrual of interest has been discontinued or reduced are estimated at September 30, 1997 and 1996, to be $1.89 billion and $4.35 billion, respectively. If interest on those mortgages and notes had been accrued for the years ended September 30, 1997 and 1996, that interest income would have approximated $228 million and $491 million, respectively.

Changes in the allowance for losses and unearned discounts on mortgage notes and loans for the year ended September 30, 1997, were (dollars in millions):

Description	FHA	Ginnie Mae	Low Rent Loans	Section 202 Loans	All Other Loan Programs	Total
Balance, Beginning of Year	$2,605	$1	$10	$21	$556	$3,193
Provision for Losses Charged to Operations	308	2	79	–	74	463
Loans Written Off	–	–	(79)	–	(4)	(83)
Amortization of Discount	–	–	–	–	–	–
Realized Losses & Write-Offs Net of Recoveries	(796)	–	–	–	–	(796)
Balance, End of Year	$2,117	$3	$10	$21	$626	$2,777

Changes in the allowance for losses and unearned discounts on mortgage notes and loans for the year ended September 30, 1996, were (dollars in millions):

Description	FHA	Ginnie Mae	Low Rent Loans	Section 202 Loans	All Other Loan Programs	Total
Balance, Beginning of Year	$4,963	–	$10	$19	$508	$5,500
Provision for Losses Charged to Operations	(819)	$1	39	2	66	(711)
Loans Written Off	–	–	(39)	–	(18)	(57)
Amortization of Discount	–	–	–	–	–	–
Realized Losses & Write-Offs Net of Recoveries	(1,539)	–	–	–	–	(1,539)
Balance, End of Year	$2,605	$1	$10	$21	$556	$3,193

Where mortgage notes are acquired at interest rates below the market interest rate in the year acquired, the notes are discounted. This discount reduces the fair value of the notes such that the effective interest rate approximates the market rate in the year acquired. For fiscal 1997, the weighted average nominal interest rates were 7.2 percent on FHA notes and 8.3 percent on non-FHA loans. The effective interest rates after discounting were 9.2 percent on FHA notes and 8.4 percent on non-FHA loans. FHA mortgages and loans which were considered current but which were under forbearance agreements comprise approximately $278 million of the entire single family portfolio. For fiscal 1996, the weighted average nominal interest rates were 8.3 percent on FHA notes and 8.2 percent on non-FHA loans. The effective interest rates after discounting were 8.8 percent on FHA notes and 8.4 percent on non-FHA loans. FHA mortgages and loans which were considered current but which were under forbearance agreements comprise approximately $1.1 billion of the entire single family portfolio. Section 202 and Low Rent Public Housing loans are made at market rates.

Note 7 – FHA and GINNIE MAE Loss Reserves

For fiscal 1997 loss reserves established in the consolidated financial statements amounted to approximately $13.65 billion. These reserves relate to FHA operations – $13.14 billion and Ginnie Mae operations – $508 million. Loss reserves for fiscal 1996 amounted to approximately $13.45 billion and consisted of $12.98 billion relating to FHA and $472 million relating to Ginnie Mae. All loss reserves are covered by budgetary resources.

Federal Housing Administration

FHA loss reserves for claims and loss adjustment expenses (LAE), were as follows as of September 30, 1997 and 1996, (dollars in millions):

	1997			1996		
Fund	Claims Loss Reserve	LAE Reserve	Total	Claims Loss Reserve	LAE Reserve	Total
MMI	$ 2,452	$121	$ 2,573	$ 2,132	$103	$ 2,235
CMHI	27	–	27	6	–	6
GI	8,222	214	8,436	9,198	228	9,426
SRI	2,069	44	2,113	1,292	27	1,319
Total	$12,770	$379	$13,149	$12,628	$358	$12,986

The LAE reserve is provided for estimated administrative expenses of settling anticipated claims and reported defaults. The MMI Fund records an undiscounted claims loss reserve to provide for estimated losses incurred by FHA to pay claims on insured mortgages where defaults have taken place, but where claims have not yet been filed. The reserve is estimated based on historical claim and loss experience data, adjusted for judgments concerning current economic factors.

Discounted loss reserves for claims in the GI and SRI Funds are recorded when loan defaults are considered probable but have not yet been reported as such to FHA. Special projects are conducted to assess the credit risk of FHA's insured multifamily portfolio and calculate a loss reserve. Based on these reviews, multifamily loss reserves were decreased by approximately $306 million for fiscal 1997 and increased by approximately $1.9 billion for fiscal 1996 through a credit to operations.

Aggregate premiums generated by the GI and SRI Funds' various programs will not be sufficient to cover the Funds' losses nor to sustain their operations. The severity of the losses in these funds and the insufficiency of their premiums leave the Funds dependent on budget appropriations to sustain their operations as originally intended under statutes. Although activity in all of the SRI Fund's major programs has decreased substantially in recent years, activity in the GI Fund continues to be significant.

Government National Mortgage Association

Ginnie Mae establishes a reserve for loss through a provision charged to operations when defaults of issuers of mortgage-backed securities become probable. The reserve is relieved as losses are realized from the disposal of the defaulted issuers' portfolios. As of September 30, 1997 and 1996, the reserves are comprised of the following (dollars in millions):

Description	1997	1996
Single Family	$196	$150
Multifamily	57	57
Title I	255	265
Total	$508	$472

Ginnie Mae incurs losses when Federal insurance and guarantees do not cover expenses that result from issuer defaults, including such expenses as: (1) unrecoverable losses on individual mortgage defaults because of coverage limitations on federal mortgage insurance or federal mortgage guarantees; (2) ineligible mortgages included in defaulted Ginnie Mae-pools; (3) improper use of proceeds by an issuer; and (4) nonreimbursable administrative expenses and costs incurred to service and liquidate portfolios of defaulted issuers.

Note 8 – Borrowings

Several HUD programs have the authority to borrow funds from the U.S. Treasury for program operations. Additionally, FHA in certain cases is authorized by the National Housing Act to issue debentures in lieu of cash to pay claims. Funds were also borrowed by PHAs and IHAs from the private sector and from the Federal Financing Bank (FFB) to finance construction and rehabilitation of low rent housing; these borrowings are being repaid by HUD on behalf of the PHAs and IHAs. HUD borrowings, and borrowings by PHAs/IHAs for which HUD is responsible for repayment, were as follows as of September 30, 1997 (dollars in millions):

Liabilities Not Covered by Budgetary Resources:

Description	Beginning Balance	New Borrowings	Repayments	Ending Balance	Current Liabilities	Non-Current Liabilities
Agency Borrowings:						
Held by Public	$ 3,861	$ –	$ (275)	$ 3,586	$ 281	$ 3,305
Total Agency Borrowings	$ 3,861	$ –	$ (275)	$ 3,586	$ 281	$ 3,305
Other Borrowings:						
From the U.S. Treasury	$10,032	$677	$ (896)*	$ 9,813	$ 972	$ 8,841
From the Federal Financing Bank	1,627	–	(66)	1,561	70	1,491
Total Other Borrowings	$11,659	$677	$ (962)*	$11,374	$1,042	$10,332
Total Borrowings	$15,520	$677	$(1,237)*	$14,960	$1,323	$13,637
Classification of Borrowings:						
Governmental Borrowings				3,586		
Intragovernmental Borrowings				$11,374		
Total Borrowings				$14,960		

** $85 million of this balance is forgiven borrowings*

Other Liabilities Covered by Budgetary Resources:

Description	Beginning Balance	New Borrowings	Repayments	Ending Balance	Current Liabilities	Non-Current Liabilities
Intragovernmental Borrowings:						
From the Federal Financing Bank	$ 39	$ –	$ (4)	$ 36	$ 4	$ 32
Total Borrowings	$ 39	$ –	$ (4)	$ 36	$ 4	$ 32

HUD borrowings, and borrowings by PHAs/IHAs for which HUD is responsible for repayment, were as follows as of September 30, 1996 (dollars in millions):

Liabilities Not Covered by Budgetary Resources:

Description	Beginning Balance	New Borrowings	Repayments	Ending Balance	Current Liabilities	Non-Current Liabilities
Agency Borrowings:						
Held by Public	$ 4,132	$ –	$ (271)	$ 3,861	$ 275	$ 3,586
Total Agency Borrowings	$ 4,132	$ –	$ (271)	$ 3,861	$ 275	$ 3,586
Other Borrowings:						
From the U.S. Treasury	$ 9,361	$1,636	$ (965)*	$10,032	$ 812	$ 9,220
From the Federal Financing Bank	1,689	–	(62)	1,627	65	1,562
Total Other Borrowings	$11,050	$1,636	$(1,027)*	$11,659	$ 877	$10,782
Total Borrowings	$15,182	$1,636	$(1,298)*	$15,520	$1,152	$14,368
Classification of Borrowings:						
Governmental Borrowings				3,861		
Intragovernmental Borrowings				$11,659		
Total Borrowings				$15,520		

** $20 million of this balance is forgiven borrowings*

Other Liabilities Covered by Budgetary Resources:

Description	Beginning Balance	New Borrowings	Repayments	Ending Balance	Current Liabilities	Non-Current Liabilities
Intragovernmental Borrowings:						
From the Federal Financing Bank	$ 89	$ –	$ (50)	$ 39	$ 4	$ 35
Total Borrowings	$ 89	$ –	$ (50)	$ 39	$ 4	$ 35

Total HUD projected principal payments for the next 5 years and thereafter are (dollars in millions):

	Governmental	Intragovernmental
FY 1997	$ 281	$1,046
FY 1998	$ 285	$ 836
FY 1999	$ 281	$ 889
FY 2000	$ 274	$ 635
FY 2001	$ 275	$ 637
FY 2002 and thereafter	$2,190	$7,367

Interest paid during the years ended September 30, 1997 and 1996, on borrowings were $924 million and $988 million, respectively. The purposes of these borrowings are discussed in the following paragraphs.

Borrowings from the U.S. Treasury

HUD is authorized to borrow from the U.S. Treasury to finance Section 202 loans. The Treasury borrowings typically have a 15-year term, but may be repaid prior to maturity at the discretion of HUD. However, such borrowings must be repaid in the sequence in which they were borrowed from Treasury. The interest rates on the borrowings are based on Treasury's 30-year bond yield at the time the notes are issued. Interest is payable on April 30 and October 31. Interest rates are 11 percent for fiscal 1997 and 9.0 percent for fiscal 1996.

In fiscal 1997 and 1996, FHA MMI and GI/SRI funds borrowed $592 million and $1.6 billion respectively from the U.S. Treasury to cover cash shortfalls.

Borrowings from the Federal Financing Bank and the Public

During the 1960s, 1970s, and 1980s, PHAs and IHAs obtained loans from the private sector and from the FFB to finance development and rehabilitation of low rent housing projects. These borrowings are being repaid by HUD on behalf of the PHAs and IHAs, through the Low Rent Public Housing program. For borrowings from the Public, interest is payable throughout the year. Interest rates range from 2.25 percent to 6 percent for both fiscal 1997 and 1996. The borrowings from the FFB have terms up to 40 years; the borrowings from the private sector have terms up to 30 years. FFB interest is payable annually on November 1. Interest rates range from 10.6 percent to 16.1 percent for both fiscal 1997 and 1996.

Before July 1, 1986, notes issued by units of general local government and guaranteed by HUD under Section 108 were purchased by the FFB. These notes had various maturities and carried interest rates that were one-eighth of one percent above rates on comparable Treasury obligations. No note purchased by the FFB has ever been declared in default. Substantially all outstanding notes are still held by the FFB.

Note 9 – Net Position

A. Cumulative Results of Operations

HUD's Cumulative Results of Operations represent the cumulative deficit or surplus from HUD's revolving funds operations, excluding activity relating to FHA's mutual funds which are reported separately. Cumulative losses of FHA's GI and SRI funds and of HUD's Section 202 loan program are financed with appropriated capital. Such appropriated capital is reported as a separate component of HUD's net position.

The net position activity for fiscal 1997 and 1996 is presented below (dollars in millions):

	1997				
Description	Beginning Balance	Activity Net Results	Dividends Paid to Treasury	Other	Ending Balance
FHA, GI and SRI Funds	$(21,043)	$ (154)	–	–	$(21,197)
Ginnie Mae	4,533	601	$ –	–	5,134
Low Rent Public Housing Grants and Loans	49	9	–	$(15)	43
Section 202 Loans	45	259	–	–	304
All other	417	1	$ –	–	418
Total	$(15,999)	$ 716	$ –	$(15)	$(15,298)

	1996				
Description	Beginning Balance	Activity Net Results	Dividends Paid to Treasury	Other	Ending Balance
FHA, GI and SRI Funds	$(19,769)	$(1,274)	–	–	$(21,043)
Ginnie Mae	4,033	515	$(15)	–	4,533
Low Rent Public Housing Grants and Loans	65	(16)	–	–	49
Section 202 Loans	(143)	153	–	$ 35	45
All other	434	17	$(34)	–	417
Total	$(15,380)	$ (605)	$(49)	$ 35	$(15,999)

The FHA cumulative losses in its GI and SRI mortgage insurance funds exceed appropriated capital, even though the National Housing Act, as amended, and the Federal Credit Reform Act authorize appropriations to restore losses in these funds. This is because, under generally accepted accounting principles, losses are recognized when the default of insured mortgages becomes probable, while for budgetary purposes, related appropriated capital will be received as defaulted loans are liquidated.

The cumulative results of operations for Ginnie Mae are derived from collection of commitment fees, guarantee fees, and investment income in excess of expenses.

B. Unexpended Appropriations

HUD receives appropriations on both an annual and multiyear basis for all non-revolving fund activity. Unexpended appropriations are amounts not yet expended, which have not lapsed, been rescinded, or been withdrawn.

Unexpended appropriations consists of obligated, committed, reserved, and available funds as presented below (dollars in millions):

	1997				
Description	Beginning Balance	Operating Appropriations Received, Net	Appropriated Capital Used	Other	Ending Balance
Section 8 Rental Assistance	$43,417	$ 1,974	$(15,149)	$(780)*	$29,462
CDBG	9,217	4,877	(4,518)	–	9,576
HOME	3,527	1,408	(1,219)	–	3,716
Operating Subsidies	1,570	2,911	(2,823)	(4)	1,654
Low Rent Public Housing Grants and Loans	12,758	3,390	(4,297)	(272)	11,579
Section 202/811	6,245	865	(845)	–	6,265
All Other	7,647	2,868	(2,737)	235*	8,013
Total	$84,381	$18,293	$(31,588)	$(821)	$70,265

** Includes transfer between HUD programs*

	1996				
Description	Beginning Balance	Operating Appropriations Received, Net	Appropriated Capital Used	Other	Ending Balance
Section 8 Rental Assistance	$53,053	$ 5,880	$(16,384)	$ 868*	$43,417
CDBG	9,097	4,667	(4,547)	–	9,217
HOME	3,329	1,405	(1,207)	–	3,527
Operating Subsidies	1,559	2,822	(2,811)	–	1,570
Low Rent Public Housing Grants and Loans	14,063	3,291	(4,251)	(345)	12,758
Section 202/811	6,797	1,107	(745)	(914)	6,245
All Other	6,530	3,051	(2,446)	512*	7,647
Total	$94,428	$22,223	$(32,391)	$ 121	$84,381

** Includes transfer between HUD programs*

Unexpended Obligational Authority for Budgetary Reporting

Unexpended obligational authority is a budgetary term consisting of budget authority provided which has not been obligated. Unexpended appropriations for financial statement purposes will not agree with unexpended obligational authority, for the following reasons:

a) unlike unexpended obligational authority, unexpended appropriations do not include contractual commitments and reservations for which appropriations have not yet been received. As explained in Note 3, unfunded contractual commitments and unfunded reservations relate primarily to the Section 8 and Section 235/236 programs, resulting from contract authority provided prior to FY 1988 (contract authority is not an appropriation);

b) unexpended obligational authority includes FHA and GNMA activity. To the extent this activity is recorded for financial statement purposes, it is included in other net position accounts;

c) commitments to fund future interest payments relating to loans made to PHAs and IHAs for which repayment was subsequently assumed by HUD, are included in unexpended obligational authority, but are not considered commitments for financial statement purposes.

Unexpended appropriations can be reconciled to unexpended obligational authority as of September 30, 1997, as follows (dollars in millions):

Appropriations recorded in accounting and budgetary records:	
Contractual commitments funded through unexpended Appropriations (Note 3)	$50,830
Reservations Funded through unexpended appropriations (Note 3)	8,160
Appropriations received, unreserved	11,275
Unexpended appropriations for Financial Statement Reporting	70,265
Non-accounting transactions recorded in budgetary records only:	
Pre-1988 contract authority reflected in Note 3 as:	
Contractual commitments funded through permanent indefinite appropriations	59,849
Reservations funded through permanent indefinite appropriations	108
FHA unexpended balances, not included in unexpended appropriations	17,452
GNMA unexpended balances, not included in unexpended appropriations	5,525
Public and Indian Housing Loan future interest payments assumed by HUD, not included in unexpended appropriations	1,237
Non-accounting transactions	84,171
Unexpended Obligational Authority for Budgetary Reporting	$154,436

C. Mutual Insurance Funds Equity

The mutual funds equity consists of the net results to date of the operations of the MMI and CMHI mutual mortgage insurance funds of the FHA. Operating activity relating to these mutual funds is recorded separately and is not included in cumulative results of operations as discussed in Note 9A. Mutual fund equity is either held to meet capital ratio requirements or distributed to eligible policyholders.

Under the National Affordable Housing Act of 1990 (Affordable Housing Act), the MMI Fund must attain a capital ratio of 2.0 percent by fiscal 2000. The Affordable Housing Act defines the capital ratio as the ratio of the economic net worth of the MMI Fund to unamoritized insurance in force.

Unamoritized insurance in force is defined by the Affordable Housing Act to be the remaining obligation on outstanding mortgages and is, therefore, the same as the MMI Fund's insurance in force. The economic net worth, as defined by the Affordable Housing Act, is the current cash available to the MMI Fund, plus the present value of all future cash inflows and outflows expected to result from the outstanding mortgages insured by the MMI Fund. The MMI Fund's economic net worth differs from the MMI Fund's equity determined in accordance with generally accepted accounting principles (GAAP), because GAAP-determined equity is not based on the net present value of future cash flows.

Since fiscal 1989, FHA has commissioned independent annual studies of the actuarial soundness of the MMI Fund. These studies may be used, in part, to estimate the economic net worth of the MMI Fund. The results of the most recent study indicate that the MMI Fund has an economic value of approximately $11.3 billion and a capital ratio of 2.81 percent as of September 30, 1997, based on unamortized insurance in force. The results of the fiscal 1996 study indicated an economic value of approximately $9.4 billion and a capital ratio of 2.54 percent as of September 30, 1996, based on unamoritized insurance in force.

Whereas the Affordable Housing Act defines unamoritized insurance in force as "the remaining obligation on outstanding mortgages", this definition is more commonly understood to be the amortized insurance in force. Use of amortized insurance in force increases the capital ratio as of September 30, 1997 and 1996 to 3.02 percent and 2.71 percent, respectively.

Changes in the FHA's Mutual Funds Equity balance during the year ended September 30, 1997 were as follows (dollars in millions):

	1997		
Description	MMI Fund	CMHI Fund	Total
Beginning Balance	$2,508	$18	$2,526
FY Activity:			
Net Results	156	(19)	137
Distributive Shares Paid	–	(1)	(1)
Distributive Shares Canceled	–	–	–
Ending Balance	$2,664	$(2)	$2,662

Changes in the FHA's Mutual Funds Equity balance during the year ended September 30, 1996 were as follows (dollars in millions):

	1996		
Description	MMI Fund	CMHI Fund	Total
Beginning Balance	$1,854	$17	$1871
FY Activity:			
Net Results	654	2	656
Distributive Shares Paid	–	(2)	(2)
Distributive Shares Canceled	–	1	1
Ending Balance	$2,508	$18	$2,526

D. Appropriated Capital

Appropriated Capital primarily represents the amounts Congress has appropriated as permanent operating capital for HUD's loan and loan insurance programs operated as revolving funds. The appropriations given to FHA to offset losses in its subsidized funds (GI and SRI) represent the majority of the balance. Appropriations receivable that were canceled as a result of Federal Credit Reform were charged against appropriated capital.

The appropriated capital activity for fiscal 1997 is as follows (dollars in millions):

	1997			
Description	FHA GI and SRI Funds	Section 202/811 Housing for the Elderly & Disabled	All Other	Total
Approriated Capital, Beginning of Year	$14,674	$2,811	$454	$17,939
Credit Subsidy Appropriations Received:				
On Insured 1997 Mortgages	95	–	–	95
As a Result of Asset Sales	–	–	–	–
For Administrative Expenses	207	–	–	207
Appropriations Returned to Treasury				
Relating to Negative Subsidies:				
On Insured 1997 Mortgages	(142)	–	–	(142)
As a Result of Re-estimates	(25)	–	–	(25)
As a Result of Modification	(80)	–	–	(80)
As a Result of Modifications Due to Asset Sales	(384)	–	–	(384)
As a Result of Budget Rescission	–	–	–	–
Other Appropriations	–	735	(64)	671
Appropriated Capital, End of Year	$14,345	$3,546	$390	$18,281

The appropriated capital activity for fiscal 1996 is as follows (dollars in millions):

	1996			
Description	FHA GI and SRI Funds	Section 202/811 Housing for the Elderly & Disabled	All Other	Total
Appropriated Capital, Beginning of Year	$14,613	$2,006	$528	$17,147
Credit Subsidy Appropriations Received:				
On Insured 1996 Mortgages	152	–	–	152
As a Result of Asset Sales	533	–	–	533
For Administrative Expenses	202	–	–	202
Appropriations Returned to Treasury				
Relating to Negative Subsidies:				
On Insured 1996 Mortgages	(142)	–	–	(142)
As a Result of Re-estimates	(110)	–	–	(110)
As a Result of Modification	(40)	–	–	(40)
As a Result of Modifications Due to Asset Sales	(533)	–	–	(533)
As a Result of Budget Rescission	(1)	–	–	(1)
Other Appropriations	–	805	(74)	671
Appropriated Capital, End of Year	$14,674	$2,811	$454	$17,939

E. Invested Capital

Invested capital represents the book value, net of amortization and depreciation, of HUD resources invested in property and equipment. HUD had a balance of $15.1 million in Invested Capital as of September 30, 1997 and $10.1 million as of September 30, 1996.

F. Future Funding Commitments

Future funding commitments are appropriations anticipated in future years to cover expenses incurred as of September 30, 1997 and 1996, for which HUD has not yet received appropriations. As of September 30, 1997 and 1996, future funding commitments consist of the following (dollars in millions):

	1997	1996
Low Rent Public Housing Loans	$(5,147)	$(5,488)
Section 202 Loans	(807)	(807)
Annual Leave and FECA	(138)	(134)
Total	$(6,092)	$(6,429)

The future funding commitments for the Low Rent Public Housing Loan program are to offset the liabilities assumed by HUD in repaying borrowings on behalf of PHAs and IHAs. HUD receives an annual appropriation covering yearly payment of principal and interest. A future funding commitment is recorded in the amount of the outstanding principal on these borrowings as of year end.

The Section 202 program was revised by the Housing and Community Development Act of 1987. This Act provided for a transfer of funds from the loan to the new capital grant program. A portion of these funds were borrowed from the U.S. Treasury. The repayment of these borrowings will be from future years' appropriations. A future funding commitment was recorded in the amount of $806 million and $807 million for September 30, 1997 and 1996.

Note 10 – Financial Instruments With Off-Balance Sheet Risk

Some of HUD's programs, principally those operated through FHA and Ginnie Mae, enter into financial arrangements with off-balance sheet risk in the normal course of their operations.

A. FHA Mortgage Insurance

Unamortized insurance in force outstanding for FHA's mortgage insurance programs as of September 30, 1997, and 1996 were as follows (dollars in millions):

Fund	1997	1996
MMI	$360,289	$337,449
CMHI	247	271
GI	84,205	78,753
SRI	8,860	9,560
Total	$453,601	$426,033

FHA's mortgage insurance covers losses that result when borrowers default on their mortgage payments. FHA mortgage insurance covers only default risk, and thus FHA is not exposed to losses resulting from interest rate fluctuations, except in the case of mortgages insured pursuant to Section 221(g)(4) of the National Affordable Housing Act. In most cases FHA insures 100 percent of the mortgage principal. However, when FHA pays claims resulting from mortgage defaults, a portion of the claim can normally be recovered through foreclosure and subsequent sale of the mortgaged property. In recent years, FHA has also recovered a portion of claims paid through public sale of the mortgage notes received at claim settlement.

FHA's MMI Fund provides mortgage insurance principally for 30-year fixed rate home mortgages. By law the MMI Fund must be operated in accordance with "sound actuarial and accounting practice." Borrowers should be charged a premium that will cover default losses and administrative expenses, and provide equity. Like all FHA activities, the MMI Fund suffers losses when premium income is insufficient to cover default losses and administrative costs. The magnitude of these losses is greater when there is either an increase in the number of mortgage defaults or a decrease in amounts recovered from the sale of foreclosed properties or mortgage notes sold. Since the MMI Fund primarily insures low down-payment mortgages, it is more susceptible to losses resulting from economic downturns. Such downturns may increase the number of defaults and result in lower claim recoveries when foreclosed properties are sold. Either situation could result in the MMI Fund experiencing greater losses than have been provided for in the accompanying consolidated financial statements.

The GI Fund provides mortgage insurance for loans involving cooperatives, condominiums, nursing homes, hospitals, and for low and moderate income multifamily loans involving construction, rehabilitation and refinancing. While the GI Fund's insurance in force is much less than that of the MMI Fund, its exposure to loss may be much greater. Unlike the MMI Fund, the GI Fund has no statutory requirement to be actuarially sound. In carrying out its mission, the GI Fund assumes levels of default risk not generally borne by commercial insurers or lenders. Furthermore, the GI Fund is susceptible to losses resulting from weaknesses in commercial and residential real estate markets at both the regional and national levels. Aggregate premiums charged by the GI Fund have not been sufficient to cover default losses and administrative costs. As a result, the GI Fund is dependent on appropriations to sustain its operations.

Activity for FHA's other two funds, SRI and Cooperative Management Housing Insurance (CMHI), has been minimal in recent years. Since these funds have very little activity, FHA's exposure to additional loss from these funds is comparatively small.

The significant geographical concentrations of both FHA's single and multifamily insurance risk are as follows. The significant geographic concentration for the single family unpaid principal insurance balance at September 30, 1997 is located in California (14 percent), Texas (8 percent), and Florida (6 percent). No other state equals 5 percent or more of the unpaid single family insurance principle balance. The concentration of risk is geographically dispersed for multifamily, except for the Hospital Program. The insurance in force for the Hospital Program is located primarily in the Northeast, with over 92 percent of the $4.8 billion unpaid principal balance of the insurance in force attributed to the New York/New Jersey HUD Regions. New York state constitutes over 88 percent of the insurance in force for hospitals. The highest geographic concentration of risk for the remaining multifamily programs is in New York (13 percent), California (9 percent), Maryland (6 percent), Illinois (5 percent), and Ohio (5 percent). No other state equals 5 percent or more of the unpaid multifamily insurance principal balance.

B. Ginnie Mae Mortgage-Backed Securities

Ginnie Mae financial instruments with off-balance sheet risk include guarantees of Mortgage Backed Securities (MBS) and commitments to guaranty MBS. The securities are backed by pools of FHA-insured, RHS-insured, and VA-guaranteed mortgage loans. Ginnie Mae is exposed to credit loss in the event of non-performance by other parties to the financial instruments. The total amount of Ginnie Mae guaranteed securities outstanding at September 30, 1997, and 1996 was approximately $531 billion and $497 billion, respectively. However, Ginnie Mae's potential loss is considerably less because the FHA and RHS insurance and VA guaranty serve to indemnify Ginnie Mae for most losses. Also, as a result of the structure of the security, Ginnie Mae bears no interest rate or liquidity risk.

During the mortgage closing period and prior to granting its guaranty, Ginnie Mae enters into commitments to guarantee MBS. The commitment ends when the mortgage-backed securities are issued or when the commitment period expires. Ginnie Mae's risks related to outstanding commitments is much less than for outstanding securities due, in part, to GNMA's ability to limit commitment authority granted to individual issuers of MBS. Outstanding commitments as of September 30, 1997 and 1996, were $31 billion and $33 billion, respectively.

Generally, Ginnie Mae's MBS pools are diversified among issuers and geographic areas. No significant geographic concentrations of credit risk exist; however, to a limited extent, securities are concentrated among issuers.

During fiscal 1997, Ginnie Mae acquired four single family issuer portfolios with a remaining principle balance of $351 million.

In fiscal 1997, Ginnie Mae issued a total of $28 billion in its multiclass securities program.. The outstanding balance at September 30, 1997 was $52 billion. These guaranteed securities do not subject Ginnie Mae to additional credit risk beyond that assumed under the MBS program.

C. Section 108 Loan Guarantees

Under HUD's Section 108 Loan Guarantee program, recipients of CDBG Entitlement Grant program funds may pledge future grant funds as collateral for loans guaranteed by HUD (these loans were provided from private lenders since July 1, 1986). This Loan Guarantee Program provides entitlement communities with a source of financing for projects which are too large to be financed from annual grants. The amount of loan guarantees outstanding as of September 30, 1997 and 1996 was $1.16 billion and $1.03 billion, respectively. In prior years the amount of loans guaranteed under this program were presented as of six months prior to the end of the fiscal year, since that was the most current information available. HUD is now able to provide this information as of the end of the fiscal year, and fiscal 1996 information has been restated to reflect this information. HUD management believes its exposure in providing these loan guarantees is limited, since loan repayments can be offset from future CDBG Entitlement Program Funds and, if necessary, other funds provided to the recipient by HUD. HUD has never had a loss under this program since its inception in 1974.

Note 11 – Contingencies

A. Section 221(g)(4) Contingent Liability

Prior to the passage of the Cranston-Gonzalez National Affordable Housing Act of 1990, single family and multifamily mortgages insured under Section 221 of the National Housing Act that were neither delinquent nor in default could be assigned to FHA pursuant to Section 221(g)(4) by lenders in exchange for FHA debentures bearing current interest rates. Eligible mortgagees could elect to assign their current mortgages to FHA during the year following the twentieth anniversary after final endorsement of the mortgage. The assignment of these mortgages resulted in an additional cost to FHA to the extent that Treasury debenture rates exceeded the mortgage interest rates.

However, under the National Affordable Housing Act, FHA was required to arrange for the sale of the beneficial interest in the multifamily mortgage in lieu of accepting assignment after the 20th anniversary. The sales price to be paid to the lenders was to be equal to the outstanding principal balance at the time of the sale plus accrued interest. To ensure this price was realized, FHA was required to make subsidy interest payments. The Affordable Housing Act, as amended, only provided for the auction of multifamily mortgages assigned through September 30, 1996. Proposed legislation is in process to extend the auction authority through December 31, 2005, the natural sunset of the assignment program based on the November 30, 1983 congressionally mandated termination date. It is unclear if and when this legislation will be approved.

However, until an approval is received, FHA will issue debentures to those eligible Section 221(g)(4) mortgagees. FHA estimates that a maximum of 3,715 mortgages with an unpaid principle balance of $8.3 billion could be assigned through 2005.

B. Termination of the Single Family Assignment Program

Historically, FHA has taken assignment of a significant number of insured single family mortgage notes which are in default rather than settle the claims through foreclosure or other alternatives. Legislation was enacted in April 1996 to eliminate the single family mortgage note assignment program. It authorized FHA to implement new loss mitigation tools and expand existing alternatives to foreclosure

C. Section 8 Subsidies

At September 30, 1997, the Department estimates that approximately 8,400 projects (with an insured mortgage value of $17 billion) were receiving rental subsidies from a variety of non-FHA Section 8 subsidy programs.

Previously, the 1997 Budget set limits on Section 8 contract terms to one year and made changes to limit the level of rental subsidies paid under new Section 8 contract renewals and amendments. Various proposals to further reduce future subsidy payments made directly to project owners either were advanced as part of the formal fiscal 1998 budget process and related legislative submissions to Congress or are expected as part of the Congressional debate about the future of public and subsidized housing in the country.

H.R. 2158 – The VA, HUD & Independent Agencies Apportion Act for fiscal year 1998, Subtitle A – FHA-Insured Multifamily Housing Mortgage and Housing Assistance Restructuring provides for a “mark to market” program to reduce the costs of over-subsidized Section 8 multifamily housing properties insured by FHA.

Under the “mark to market” program, FHA-insured Section 8 housing properties with above market rents are eligible for debt restructuring to reduce rent levels to those of comparable market rate properties or to the minimum level necessary to support proper operations and maintenance. In response to limitations with HUD capacity, the legislation shifts the administration and management of this portfolio from HUD to entities (termed participating administrative entities), charged with protecting the affordable housing stock in a fiscally responsible manner. Additionally, the legislation terminates the Government's relationship with owners who fail to comply with Federal requirements and ends the practice of subsidizing properties that are not economically viable.

While the act includes extensive guidance on the selection of participating administrative entities development and submission of portfolio restructuring agreements covering the insured and subsidized mortgages, and determination, from a number of alternatives, of the best methods to restructure the project mortgage and subsidies, the Secretary is charged to develop additional regulations, rules, and procedures to implement the program.

The impact of these proposals would vary from project to project depending on such factors as the then current financial and physical condition, size and timing of subsidy changes, and local market conditions. In addition, final costs to FHA of these additional claims would depend upon the methods used to restructure project mortgages or to minimize the actual transfer of the mortgages or properties to FHA ownership, and the methods used to dispose of any mortgages or properties assumed in a timely fashion. The claims which would result almost all relate to insurance issued prior to 1991. FHA has available a permanent indefinite appropriation authority to pay these claims.

FHA estimates that approximately $ 5.3 billion of loss reserves on subsidized projects have already been accrued, for financial reporting purposes, but not for budget purposes, as part of its estimation of potential losses on the entire insured portfolio at September 30, 1997. Loss reserves accrued for subsidized projects at September 30, 1996, were $6.2 billion. These reserves include the estimated overall financial impacts on FHA of the changes to the present rent subsidy structure. HUD believes these reserves adequately provide for estimated losses on subsidized projects.

D. Lawsuits and Other

HUD is party in various legal actions and claims brought against it. In the opinion of management and General Counsel, the ultimate resolution of these legal actions and claims will not materially affect HUD's financial position or results of operations for the fiscal year ended September 30, 1997 and 1996. Payments made out of the Claims, Judgments and Relief Acts Fund in settlement of the legal proceedings are subject to the Department of Justice's approval.

A case was filed by owners of 42 multifamily projects regarding the Emergency Low-Income Housing Preservation Act of 1987 (ELIHPA) and the Low-Income Housing Preservation and Resident Homeownership Act of 1990 (LIHPRHA). The Court of Federal Claims has ruled that the project owners' mortgage contracts had been breached by implementation of ELIHPA and LIHPRHA, and a trial was held in November 1996 to determine damages, if any, with respect to that claim as regards four model properties. The court awarded $3,061,107 in damages to the Plaintiff owners of the four model properties. An appeal has been taken by the United States from the judgment entered in this case and is presently under consideration by the United States Court of Appeals for the Federal Circuit. The ruling by the Federal Circuit on this appeal will very likely affect the outcome of all the other pending actions unless further review is done by the United States Supreme Court, in which event, the Supreme Court's decision will be determinative. To date, there are 20 other lawsuits involving approximately 656 multi-family projects, all of which allege the same cause of action as stated above. HUD intends to defend these matters vigorously. HUD is unable at this time to form a judgment about the likelihood of an unfavorable outcome, or to make an estimate of the amount or range of potential loss if the plaintiffs should prevail. Any adverse judgment would be paid out of the Claims, Judgments, and Relief Acts Fund administered by the Department of Justice.

Note 12 – Intragovernmental Financial Activities

HUD's financial activities interact with and are dependent upon those of the Federal government as a whole. Specifically, HUD is subject to financial decisions and management controls of the Office of Management and Budget (OMB). As a result of its relationship with other Federal government entities and OMB, HUD's operations may not be conducted, nor its financial position reported, as they would if HUD were a separate and unrelated entity.

HUD's consolidated financial statements are not intended to report the Department's proportionate share of the total federal deficit or of public borrowings by the Treasury, including interest thereon.

A. Claims, Judgments, and Relief Acts Fund

Most legal actions that affect HUD and involve an amount in excess of $2,500, with the exception of on-the-job injury claims as discussed in Note 2 and legal actions pertaining to the FHA and Ginnie Mae programs, are paid from the Claims, Judgments, and Relief Acts Fund maintained by the Department of the Treasury and administered by the General Accounting Office and the Department of Justice. HUD is not required to reimburse this fund for payments made on its behalf. During fiscal 1997 and 1996, no material amounts were paid to settle actions against HUD.

B. Other Interagency Transactions

HUD maintains various agreements with other federal agencies under the Economy and Efficiency Act. The revenues, expenses, receivables and payables for these agreements for fiscal 1997 and 1996 are not material. HUD's two largest federal transactions are with the General Services Administration (GSA) for the use and upkeep of HUD facilities, and the Department of Agriculture's National Finance Center, for the processing of payroll and related benefits.

HUD also manages transfer appropriations from GSA, the Appalachian Regional Commission (ARC), and the Department of Energy (DOE). The GSA funding is used to pay certain building occupancy costs for HUD's Headquarters building. The ARC funding is used to facilitate joint Federal and State efforts to provide basic facilities essential to economic growth in Appalachia. The DOE funding is used to fund loans and grants related to solar energy conservation improvements. These funds are included in the "All other" category in the consolidated financial statements.

Note 13 – Credit Reform

HUD's activities are subject to the Federal Credit Reform Act of 1990 ("Credit Reform"), which became effective on October 1, 1991. Credit Reform's effect on HUD relates primarily to how losses and costs associated with loans insured through FHA's GI and SRI funds are financed. A primary purpose of Credit Reform is to more accurately measure the "subsidy" costs of Federal credit programs. Subsidy costs generally comprise the present value of estimated disbursements for costs associated with mortgage defaults, net of the present value of estimated collections for insurance premiums and claims recoveries.

For mortgages insured on or after October 1, 1991, up-front appropriations are required to finance credit subsidy costs. Appropriations to finance subsidy costs in the GI and SRI Funds were $95 million and $152 million in fiscal 1997 and 1996, respectively. FHA's MMI Fund has not received credit subsidy appropriations because the premiums charged are estimated to exceed associated costs.

For mortgages insured prior to October 1, 1991, the effective date of Credit Reform, permanent indefinite appropriations are available to finance costs associated with such mortgages to the extent premiums, recoveries, and financing are insufficient to do so. No appropriations were drawn for pre-Credit Reform mortgages for fiscal 1997 and 1996.

In fiscal year 1997, FHA's MMI and GI/SRI Funds borrowed $592 million from the Treasury to cover re-estimates of prior years insurance and expected gains from new MMI insurance activity as required by the Credit Reform Act.

FHA also receives appropriations to finance credit-related administrative expenses of the GI/SRI funds. These annual appropriations are separate from subsidy appropriations, and are not determined on a present value basis. The GI/SRI Funds, administrative costs were $207 million and $202 million for fiscal 1997 and 1996, respectively. The MMI Fund administrative expenses are not covered by appropriations and are funded by operating revenues. For fiscal 1997 and 1996, the MMI Fund incurred administrative expenses of $351 million and $342 million, respectively.

During fiscal 1997, mortgage notes sales generated additional cash flows of $449 million and $384 million for the MMI and GI/SRI Funds, respectively. In fiscal 1996, additional cash flows of $265 million and $533 million were generated from mortgage note sales for the MMI and GI/SRI Funds, respectively. In 1996, Congress provided standing authorization to use the proceeds to help fund program operations.

Periodic subsidy re-estimates are required by Credit Reform to assure that the amount of monies necessary for credit subsidies is sufficient to cover estimated costs. Downward adjustments result from having received more subsidy than is believed needed, and the excess is deposited to a special receipt account at the Treasury. Upward adjustments result in additional monies due, which are financed by standing legislation and do not require additional Congressional action, although approval to receive and utilize the monies must be made by the OMB.

Ginnie Mae's credit activities have historically operated at a profit. Ginnie Mae has not incurred borrowings or received appropriations to finance its credit operations, nor does it anticipate the need to receive such funding. As of September 30, 1997, Ginnie Mae had an Investment in the U.S. Government balance of $5.1 billion after establishing reserves for potential losses on its credit activities. Pursuant to the statutory provisions under which Ginnie Mae operates, its net earnings are used to build sound reserves.

Note 14 – Excess Rental Subsidies

During fiscal 1997 and 1996, HUD developed statistical estimates of the extent of unreported income and excess rental subsidies based on an analysis of a sample of assisted households nationwide that received rental assistance during calendar year 1996 (the most recent year for which data is available for computer matching purposes) and 1995.

Under HUD's Section 8 and Low Rent Public Housing programs, tenants generally are required to pay 30 percent of their income towards rent, with HUD providing the balance of the rental payment. New applicants and existing tenants are to provide income information which is used in determining the amount of rent they are to pay. Tenants are also required to recertify their income on an annual basis, and in certain other circumstances, i.e., when there is a significant increase in household income. The applicants' or tenants' failure to disclose all of their income, or the housing agencies', owners', or agents' failure to timely recertify the tenants for rental assistance, may result in the Department paying a greater rental subsidy than would be required. This additional subsidy is referred to as excess rental subsidy.

During fiscal 1997 and 1996, the Department selected a sample of households from its automated databases containing tenant data, and computer matched household income shown in those databases to Social Security Administration (SSA)/Internal Revenue Service (IRS) data. HUD staff examined source documents for each case where differences in income from computer matching sources and tenant reported sources exceeded a predetermined threshold. These source documents were obtained from housing agencies, owners, and agents to determine if the income differences contributed to excess rental subsidies or were caused by other reasons that would not contribute to excess subsidies. For example, the computer matching would not identify excess subsidies if erroneous income information had been entered into the databases or SSA/IRS and tenant-reported income information were reported for different time periods.

The threshold used to determine computer matching differences was $1,000 for calendar 1996 and $3,000 for calendar 1995 data. Use of a threshold was necessary to provide a reasonable and cost effective basis for developing estimates of unreported income. The $1,000 threshold was selected to provide a more accurate estimate of the amount of excess subsidies than obtained in the prior year using the larger threshold. However, to facilitate comparability between calendar 1996 and 1995 results, the Department also compiled calendar 1996 results using the prior year $3,000 threshold.

The results of the statistical sample of computer matching results were as follows:

	Calendar 1996		Calendar 1995
	($1,000 threshold)	($3,000 threshold)	($3,000 threshold)
Excess rental subsidies for all households included in databases, based on statistical sampling, with a 95% confidence level.	$752 million, +$147 million	$644 million, +$146 million	$409 million, +$122 million
Number of housholds in databases	3.47 million	3.47 million	3.24 million
Extrapolating this information to the universe of all households would yield the following results:			
Excess rental subsidies for all households included in databases extrapolated to universe of all households	$939 million, +$184 million	$804 million, +$182 million	$538 million, +$161 million
Universe of all households receiving subsidy	4.33 million	4.33 million	4.27 million

The above extrapolation of the database information to the entire universe of households is based on the assumption that the characteristics of the households included in the databases from which the sample was selected are similar to those households not included in the databases.

The phrase "excess rental subsidies" does not necessarily equate to budgetary reductions that are realizable by eliminating the excess rental assistance. HUD's budgetary needs are affected by many variables not recognized in the above estimates.

The Department plans on conducting a similar estimate of the amount of excess subsidies on an annual basis.