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24 CFR Parts 903, 905, 941, *et al.*
Public Housing Capital Fund Program; Final Rule

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**24 CFR Parts 903, 905, 941, 968, and 969**

[Docket No. FR-5236-F-02]

RIN-2577-AC50

Public Housing Capital Fund Program**AGENCY:** Office of the Assistant Secretary for Public and Indian Housing, HUD.**ACTION:** Final rule.

SUMMARY: This final rule combines and streamlines the former legacy public housing modernization programs, including the Comprehensive Grant Program (CGP), the Comprehensive Improvement Assistance Program (CIAP), and the Public Housing Development Program (which encompasses mixed-finance development), into the Capital Fund Program (CFP). This rule defines qualified PHAs, which are not required to file annual plans. The rule expands HUD's current requirement that a Public Housing Authority (PHA) submit a physical needs assessment (PNA) to include small PHAs as well as large PHAs, but provides small PHAs additional time to plan for and implement this requirement. The rule allows PHAs to request a total development cost (TDC) exception for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency, including green construction and retrofits, which include windows; heating system replacements; wall insulation; site-based generation; advanced energy savings technologies, including renewable energy generation; and other such retrofits. The rule also makes changes to replacement housing factor funds and the threshold for management improvements. Because this rule streamlines programs, several formerly separate regulations are eliminated with the implementation of this rule.

DATES: Effective date: November 25, 2013. The incorporation by reference of certain publications listed in the rule is approved by the Director of the Federal Register as of November 25, 2013.

FOR FURTHER INFORMATION CONTACT: Jeffrey Riddel, Director, Office of Capital Improvements, Office of Public and Indian Housing, Department of Housing and Urban Development, 451 7th Street SW., Washington, DC 20410-8000; telephone number 202-708-1640 (this is not a toll-free number). Hearing- or

speech-impaired individuals may access this number through TTY by calling the toll-free Federal Relay Service at 800-877-8339.

SUPPLEMENTARY INFORMATION: This final rule follows a February 7, 2011, proposed rule and makes changes in response to public comment on the proposed rule and further consideration of issues by HUD.

I. Executive Summary*A. Purpose of the Regulatory Action*

This final rule implements section 9 of the United States Housing Act of 1937 (the 1937 Act), which created the CFP as part of the Quality Housing and Work Responsibility Act of 1998 (title V, Pub. L. 105-276, approved October 21, 1998). The Capital Fund consolidated the former public housing modernization programs, including the Comprehensive Grant Program (CGP), the Comprehensive Improvement Assistance Program (CIAP), and the Public Housing Development Program (which encompasses mixed-finance development). In 2008, the Housing and Economic Responsibility Act (HERA) (Pub. L. 110-289, approved July 30, 2008) made changes to the CFP, namely the removal of the former emergency set-aside for natural disasters and emergencies, and the creation of a category of "qualified PHAs," smaller PHAs that are relieved from certain paperwork submission requirements. To date, there has been no comprehensive regulation implementing these statutory requirements and updates. Thus, rather than a comprehensive, user friendly regulation, PHAs have been required to use annual processing notices to supplement outdated regulations in various parts of title 24 of the Code of Federal Regulations (CFR), including parts 905, 941, and 965.

This regulation is necessary to consolidate the legacy modernization programs in one part of the CFR and to update the regulations in accordance with current law. An updated regulation with current program requirements is needed to provide new staff members with the knowledge necessary to manage the Capital Fund and Mixed Finance Development programs proficiently. In addition, the regulated community needs a single, clear, updated regulation in order to have complete and current information.

The Capital Fund formula itself, currently codified at 24 CFR 905.10, is reorganized at § 905.400. This formula includes a number of coefficients that are to be inserted into the equation. These coefficients are unchanged by this rule. The coefficients were defined as

part of a negotiated rulemaking that occurred in 1999 and 2000. The proposed rule can be found at 64 FR 49924 (September 14, 1999) and the final rule can be found at 65 FR 14426 (March 16, 2000).

B. Summary of the Major Provisions of the Regulatory Action

This rulemaking: Establishes a new definition section and proposes several new definitions to be included in the section; clarifies Capital Fund eligible and ineligible activities, and incorporates energy efficiency standards; incorporates into part 905 of public housing modernization the regulations at 24 CFR part 968, which part is removed by this final rule; incorporates the development and mixed-finance development requirements of part 941, which also is removed; expands the requirement for a PNA to include small, as well as large, PHAs (specific requirements pertaining to the PNA will be addressed in a separate rulemaking), but delays the applicability of this provision for small PHAs until 30 days after the end of a federal fiscal year quarter following HUD's publication of a notice in the **Federal Register** announcing application of the provision.

The rulemaking also incorporates by reference the 2009 International Energy Conservation Code (IECC) and American Society of Heating, Refrigerating, and Air-Conditioning Engineers (ASHRAE) standard 90.1-2010, "Energy Standard for Buildings Except Low-Rise Residential Buildings." The ASHRAE standard can be found at <http://www.ashrae.org/standards-research-technology/standards-guidelines>. The 2009 IECC can be purchased at <http://shop.iccsafe.org/>.

This rulemaking also: Clarifies the calculation of TDC limits and establishes the ability for PHAs to request a TDC exception for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency; establishes 5 years of a Demolition or Disposition Transitional Funding (DDTF) grant that will be included in the regular Capital Fund formula grant, to replace the Replacement Housing Factor (RHF) grant of up to 10 years; provides for a DDTF transition period; clarifies at § 905.202(b) that because of their emergent nature, emergencies that are not identified in the 5-year action plan (statutorily required by section 5A of the 1937 Act) are eligible costs; revises the description of eligible amenities at § 905.202(c); phases in over 5 years a cap of 10 percent of a PHA's Capital

Fund that the PHA may expend on management improvements; and revises the identity of interest regulations in accordance with HUD's actual practice to provide PHAs with the flexibility to use an instrumentality as a general contractor in mixed-finance projects, as long as cost requirements are met, without having to request a waiver.

C. Costs and Benefits

This rule does not have any direct financial impact on the level of funding for the CFP, but has the potential to create some financial transfers among program participants of less than \$100 million annually. The rule will cap management improvement expenditures from the Capital Fund at 10 percent, phasing in the cap over 5 years. On average, PHAs use approximately 8 percent of their Capital Fund grants on management improvements, with many PHAs using considerably less, and larger PHAs of more than 250 units using 9 percent. The 10 percent cap would not cause significant transfers outside of the CFP, though the 10 percent cap would require significant expenditure changes for some PHAs that spend a high percentage of their Capital Fund grants on management improvements.

This final rule will also have significant benefits. This rule updates and consolidates the CFP regulations and related regulations having to do with the use of Capital Funds for development and modernization, as well as regulations for continuing operation of low-income housing after completion of debt service. In addition, the rule codifies recent statutory requirements enacted in HERA. The benefits of the rule such as regulatory consolidation, program clarification, removal of obsolete references, and enhanced efficiencies justify the promulgation of this rule.

II. Background

Section 9 of the U.S. Housing Act of 1937 (1937 Act) (42 U.S.C. 1437g) is the statutory basis for the Public Housing Capital Fund (Capital Fund) and the Public Housing Operating Fund (Operating Fund). The Operating Fund is established by Section 9(e) of the 1937 Act, and the Capital Fund, which is the focus of this rule, is established by section 9(d) of the 1937 Act (42 U.S.C. 1437g(d)). Section 9(d) lists the various items for which the Capital Fund may be used, including development, modernization, maintenance, vacancy reduction, code compliance, demolition and replacement, homeownership activities, and energy efficiency, among others.

Other important provisions found in section 9(d) of the 1937 Act are: The requirement for HUD to develop a formula to determine the amount of Capital Funds that are allocated to PHAs in each fiscal year (42 U.S.C. 1437g(d)(2)); flexibility for a small PHA to use up to 100 percent of its Capital Fund grant and for a large PHA to use up to 20 percent of its Capital Fund grant for purposes ordinarily pertaining to the Operating Fund (section 9(g) of the 1937 Act pertaining to limitation on use of funds; 42 U.S.C. 1437g(g)); and penalties for the slow obligation and expenditure of Capital Funds (section 9(j) of the 1937 Act, 42 U.S.C. 1437g(j)). All of these requirements based in statute and others added by regulation constitute the CFP. Additionally, due to changes made to the annual plan statutorily required of PHAs (PHA Annual Plan) by section 5A of the 1937 Act, and the need to have grant reporting in compliance with the requirements of the CFP, and other federal reporting requirements, the CFP informational requirements will be decoupled from the PHA Annual Plan requirements. HUD will make necessary changes to the HUD forms involving the CFP budget and reporting requirements.

Section 2702 of the HERA amended section 5A of the 1937 Act (42 U.S.C. 1437c-1) to provide that certain PHAs, called "qualified PHAs," are not required to file the PHA Annual Plan called for in section 5A(b)(1) of the 1937 Act (42 U.S.C. 1437c-1(b)(1)), although these PHAs, along with nonqualified PHAs, must file the 5-year plan and a civil rights certification required under section 5A(d)(16) of the 1937 Act, 42 U.S.C. 1437c-1(d)(16). Qualified PHAs under section 2702 are those that administer 550 or fewer units—considered as the sum of all the public housing units and vouchers under section 8(o) of the 1937 Act (42 U.S.C. 1437f(o)) (section 8) administered by a PHA—and which are not designated as a troubled PHA under section 6(j)(2), and which do not have a failing score under the Section 8 Management Assessment Program (SEMAP) during the prior 12 months. Please see the preamble to the proposed rule of February 7, 2011 (76 FR 6654–6682), for further discussion of the statutory background.

III. The Proposed Rule

Significant changes to the CFP regulations that were proposed by the February 7, 2011, rule included the following:

- Establishment of a new definition section and proposing several new

definitions to be included in this section.

- Clarification of Capital Fund eligible and ineligible activities and incorporating energy efficiency standards.

- Incorporation into part 905 of public housing modernization the regulations at 24 CFR part 968, which part is removed by this final rule.
- Establishment of annual plan submission requirements for nonqualified PHAs as defined in section 2702 of HERA and Capital Fund submission requirements for qualified and nonqualified PHAs.

- Expansion of the requirement for a PNA to include small, as well as large, PHAs. The requirements pertaining to PNA may be addressed in a separate rulemaking.¹

- Clarification that Energy Star appliances and systems, and cost-effective energy measures, are eligible costs.

- Incorporation of the IECC and American Society of Heating, Refrigerating, and ASHRAE standard 90.1–2010, "Energy Standard for Buildings Except Low-Rise Residential Buildings." The ASHRAE standard can be found at <http://www.ashrae.org/standards-research-technology/standards—guidelines>. The 2009 IECC can be purchased at <http://shop.iccsafe.org/>

- Clarification of the calculation of TDC limits and establishment of the ability for PHAs to request a TDC exception for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency.

- Limitations on the number of years that PHAs will receive RHF grants.

- Provision for RHF transition funding for PHAs that have already begun receiving RHF funding grants at the time the new 5-year program comes

¹ Part 968 promulgated December 21, 1989, instituted a requirement for large (Comprehensive Grant) PHAs to complete a PNA as a part of the Comprehensive Plan (see 968.315(e)(2)). This rule does not add new PNA requirements for large PHAs but rather continues the current requirements with the only change being that small PHAs will also have to comply with those requirements. The current PNA requirements include completion of a brief summary of the physical improvements needed to bring each development to HUD standards for modernization, energy conservation life-cycle cost effective performance standards, and lead-based paint testing and abatement standards; the replacement needs of equipment and structural elements during the period covered; a preliminary estimate of cost; any physical disparities between buildings occupied predominantly by one racial or ethnic group and the physical improvements required to correct the disparity; and the number of units the PHA is proposing for substantial rehabilitation and subsequent sale, if any.

into effect. Those PHAs would receive 10 full years of replacement funding.

- Setting of costs limits for the CFP fee at 10 percent of the annual Capital Fund grant.
- Reduction of the amount of the grant that may be spent on management improvements from 20 percent to 10 percent over a 3-year period.
- Revisions to the requirements for timely obligation and expenditure of Capital Funds currently found at 24 CFR 905.120.
- Incorporation of the design and construction requirements currently found in 24 CFR 941.203 into part 905.
- Establishment of requirements for funding Resident Management Corporation (RMC) activities.
- Establishment of rules on contracting requirements and the use of force account labor.
- Incorporation of development requirements, including those pertaining to mixed-finance projects.
- Implementation of section 35(h) of the 1937 Act, 42 U.S.C. 1437z-7(h), allowing for deviations from Public Housing Requirements, under specified conditions, to ensure the long-term feasibility of mixed-finance projects, while still ensuring certain tenant protections.
- Prohibition on a PHA pledging its assets without written HUD approval.
- Establishment of sanctions for noncompliance with HUD contracts and regulations.

IV. Summary of Significant Changes in This Final Rule

The following changes were made to the proposed rule at this final rule stage:

- Revises the definitions of Capital Fund Annual Contributions Contract (CF ACC); Public Housing Requirements; Qualified PHA; and public housing funds. This final rule adds a definition of Declaration of Trust (DOT) and of Declaration of Restrictive Covenant.
- Clarifies that the provisions of direct social services and the costs for security guards or ongoing security services are not eligible management improvements.
- Provides, as one option to the guaranty of irrevocability of funding, that the required letter of credit is to be valued at 10 percent of the contract price (the proposed rule would have required a letter of credit to be valued at 25 percent of the contract price).
- Clarifies at § 905.202(b) that because of their emergent nature, emergencies that are not identified in the 5-year action plan (statutorily required by section 5A of the 1937 Act) are eligible costs.

- Revises the description of eligible amenities at § 905.202(c).

- Implements, over a 5-year time period, a 10 percent cap on the amount of Capital Funds that a PHA may spend on management improvements. (In contrast, the proposed rule would have implemented this cap over 3 years.)
- Establishes 5 years of a DDTF grant that will be included in the regular Capital Fund formula grant. Since DDTF will be included in the formula grant, the DDTF grant will not be subject to the same requirements as the RHF grants and will be usable for modernization as well as development. PHAs will be able to use the DDTF for any eligible activity under the CFP and this funding will not be subject to accumulation, although the DDTF grant will be subject to the same statutory requirements as any Capital Fund grant and the terms of the appropriation of Capital Funds from Congress.

In addition to the above listed changes, the following changes are also made via the final rule.

The final rule delays the applicability of § 905.300(a) for small PHAs. HUD is taking this action to provide small PHAs additional time to prepare for the implementation of the requirement to submit a PNA. Specifically, small PHAs will be subject to this provision 30 days following the end of a federal fiscal year quarter following HUD's publication of a notice in the **Federal Register** announcing application of the provision. Moreover, HUD plans to delineate a time frame for submission of a PNA such that the first submission by a small PHA would not be sooner than 6 months after the end of the federal fiscal quarter.

The final rule gives PHAs more time to prepare for the change to DDTF. Starting in Fiscal Year (FY) 2014, PHAs that would be newly eligible for RHF funding will receive instead 5 years of DDTF. In FY 2014, if a PHA has one or more years of first-increment RHF funding, the PHA will receive the remaining years of first-increment RHF and an additional 5 years of DDTF. If, in FY 2014, a PHA has already started receiving second increment RHF funding, the PHA will receive the remaining years of second increment RHF funding. An Excel spreadsheet that describes the impact of HUD's changes to DDTF is available at http://portal.hud.gov/hudportal/HUD?src=/program_offices/public_indian_housing/programs/ph/capfund.

The final rule provides that PHAs that remove units because of homeownership are not eligible for replacement funding under an RHF.

This final rule corrects an error in proposed § 905.602(b), that addressed limitations on new construction. In the proposed rule, acquisition was improperly excluded from the limitations. HUD's interpretation of construction in this context, as including acquisition, was properly reflected in the regulatory preamble of the February 7, 2011, proposed rule at 76 FR 6654, third column, which stated as follows:

Section 9(g)(3) of the 1937 Act (42 U.S.C. 1437g(g)(3)) imposes limitations on the use of the Capital Fund or Operating Fund for new construction. Generally, the CF formula shall not provide PHAs funding for the purpose of constructing public housing units (which includes acquisition), if the construction would result in a net increase from the number of housing units owned, operated, or assisted by the PHA on October 1, 1999. . . ."

However, the rule text at proposed § 905.602 did not correctly reflect this interpretation. This error is corrected in final rule § 905.602(b).

The final rule makes changes to proposed § 905.604(n), which addressed deviations from HUD requirements under 35(h) of the 1937 Act (see 42 U.S.C. 1437z-7(h)). The proposed rule would have required that to allow for deviations in a mixed-finance project because of a change in appropriations or other change in law preventing a PHA from providing Operating Funds, at least 20 percent of the units must be nonpublic housing rental units. In addition, the proposed rule would have predetermined specific allowable deviations. Some commenters objected to the 20 percent threshold and the limited allowable deviations. This final rule allows for more flexibility. As the statute provides, there must be a "significant number" of units that are not public housing. Rather than specific allowable deviations, the PHA, on behalf of the mixed-finance owner entity (Owner Entity) would submit an Alternative Management Plan to HUD, which would explain the reasons for the deviation and the proposed changes, among other details (see § 905.604(k) of this final rule).

This final rule revises the identity of interest regulations in accordance with HUD's actual practice. This revision provides PHAs with the flexibility to use an instrumentality as a general contractor in mixed-finance projects, as long as cost requirements are met, without having to request a waiver. The identity of interest general contractor must have submitted the lowest bid in response to a request for bids, or, in the alternative, the PHA must submit a written justification to HUD, including

an independent cost estimate, that demonstrates that the identity of interest general contractor's costs are less than or equal to the independent third party cost estimate. Identity of interest contractors will be considered by HUD as part of the development proposal approval. Since 2008, HUD has consistently granted waivers to allow this procedure to be followed; 45 waiver requests have been granted, and no waiver request was denied in that period. Additionally, HUD previously published this provision for comment (see HUD's proposed rule entitled "Streamlining Public Housing Programs" (FR-4990-P-01), published on August 8, 2008, at 73 FR 45373 and, generally, received supportive comments. The comments on the 2008 proposed rule can be found at <http://www.regulations.gov>.

V. The Public Comments

The public comment period on the proposed rule closed on April 8, 2011, and 45 public comments were received. Comments were received from a variety of stakeholders, including PHAs, trade associations, housing advocates, and individuals.

Definitions (§ 905.108)

Issue: The proposed definition of "Capital Fund Annual Contributions Contract (CF ACC)" appears to conflate the definition of the entire ACC (which is a contract addressing the operation of public housing) with that of a Capital Funds amendment (presumably limited to the special terms applicable to the provision of Capital Funds).

HUD Response: To avoid possible ambiguity, this final rule modifies the proposed definition of CF ACC to more clearly indicate that this is an amendment to the Consolidated Annual Contributions Contract (Consolidated ACC). It should also be noted that the ACC is a grant agreement that addresses not only the operation of public housing but also the development and modernization of public housing.

Issue: The definition of "development" in § 905.200(b)(2) appears to be limited to activities to add units to inventory; notwithstanding the reference to nondwelling facilities, it is unclear what else might be covered given the limiting phrase. Also, the definition of "development" should include a facility that is being modernized.

HUD Response: The reference to "development" in this paragraph is in the context of eligible housing, not a general definition of development, and is part of a larger list of eligible activities. The paragraph states that the

eligible activities under the rubric of development include "construction and acquisition with or without rehabilitation; and any all undertakings necessary for planning, design, financing, land acquisition, demolition, construction, or equipment, including development of public housing units, and buildings, facilities, and/or related appurtenances (i.e., nondwelling facilities/spaces). Development of mixed-finance projects includes the provision of public housing through a regulatory and operating agreement, master contract, individual lease, condominium or cooperative agreement, or equity interest."

Issue: The definition of "Community Renewal Costs" in § 905.108 states that Capital Funds may be used for community renewal costs, but not what those costs are, which makes it difficult to apply the TDC formula at § 905.314(e). The commenter states that this term should be defined.

HUD Response: Community Renewal costs consist of the sum of the following HUD-approved costs related to the development of a public housing project: planning (including proposal preparation), administration, site acquisition, relocation, demolition, and site remediation of environmental hazards associated with public housing units that will be replaced on the project site, interest and carrying charges, off-site facilities, community buildings and nondwelling facilities, contingency allowance, insurance premiums, any initial operating deficit, on-site streets, on-site utilities, and other costs necessary to develop the project that are not covered under the ACC. This final rule adds this information to the definition.

Issue: The definition of "Public Housing Requirements" should be revised to specifically reference the Consolidated ACC and all amendments, rather than referring to the CF ACC Amendment without the underlying document. If there is intended to be a split between the CF ACC Amendment and the Mixed-Finance ACC Amendment, references to the CF ACC should be corrected accordingly. The definition should read:

Public Housing Requirements. All requirements applicable to public housing including, but not limited to, the 1937 Act; HUD regulations; the Consolidated Annual Contributions Contract, including amendments; HUD notices; and all applicable federal statutes, executive orders, and regulatory requirements, as these requirements may be amended from time to time.

HUD Response: HUD accepts this recommendation and the change is

incorporated into the definition at § 905.108.

Issue: HUD's regulation at § 903.3 does not directly define the term "qualified" PHA. The commenter recommends that to make the final rule transparent and conducive to public understanding, it should list the 3 factors necessary for a small PHA to be "qualified" in order to avoid having a PHA Annual Plan. The commenter additionally notes that while the proposed rule's summary and overview declare that the proposed PHA Annual Plan change would merely incorporate the definition of "qualified PHA" in the PHA Annual Plan regulation at § 903.3, the actual proposed rule text removes the current subsection explaining the purpose of the PHA Annual Plan.

HUD Response: For ease of use and transparency, this final rule incorporates the definition of "qualified PHA" that is provided in § 903.3, which, in turn, adopts the statutory definition for this term in section 2702 of HERA (codified at 42 U.S.C. 1437c-1(b)(3)(C)), rather than relying on a cross-reference:

The term "qualified PHA" means a public housing agency that meets the following requirements:

(1) The sum of the number of public housing dwelling units administered by the agency, and the number of vouchers under section 8(o) of the United States Housing Act of 1937 (42 U.S.C. 1437f(o)) administered by the agency, is 550 or fewer; and

(2) The agency is not designated under section 42 U.S.C. 1437d(j)(2) as a troubled public housing agency and does not have a failing score under SEMAP during the prior 12 months.

Issue: The definition of "Owner Entity" requires that the rule make clear, either in the definition or elsewhere, that a mixed-finance development can be owned by an Owner Entity, a PHA, or, alternatively, an instrumentality.

HUD Response: HUD has clarified the definition of Owner Entity as it relates to mixed-finance in §§ 905.108 and 905.604(a)(1).

Issue: In proposed § 906.604(b)(4), the definition of "participating party" is overbroad.

HUD Response: This term is no longer used this final rule.

Issue: The rule should include a definition of "partners," used in § 905.108; a definition of "declaration of trust"; a definition of "modernization"; and a definition of "mixed-finance modernization."

HUD Response: "Partner" was proposed to be defined in § 905.604(b); however, because the term applies

elsewhere, this final rule moves the definition to § 905.108. “Mixed-finance modernization” is defined at § 905.108, 905.200 and 905.604. Definitions of “Declaration of Trust” and “modernization” are added to this final rule at § 905.108.

Issue: The definition of “public housing” excludes HOPE VI and other non-Capital Fund assistance that HUD regulates.

HUD Response: To capture the Public Housing Funding that HUD regulates, this final rule defines “public housing funds” in a more inclusive manner at § 905.108 to include HOPE VI and other funds appropriated for public housing uses, including development, rehabilitation, and operations.

Total Development Cost (TDC)

Issue: Several commenters expressed support for limiting modernization costs to 90 percent of TDC as well as for the TDC exception in § 905.314(c) for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency, including green construction and retrofits.

One commenter, however, stated that there is a lack of clarity in the language of § 905.314(c) because the terminology varies between “exception” and “waiver,” where a waiver is normally a more formalized process than a simple regulatory exception.

HUD Response: This final rule retains the 90 percent of TDC threshold for modernization. On the issue of exception or waiver, the commenter is correct, “exception” is the correct term and is used in § 905.314(c) of this final rule.

Issue: One commenter states that while the rule deals with Capital Funds, it should also include other sources of funding for public housing such as HOPE VI, Choice Neighborhoods, “Development funds,” and any other sources that may become available in the future. The commenter states, for example, § 905.314(c), on TDC, currently covers only development with Capital Funds and that this section should be revised to include all public housing funding sources.

HUD Response: HUD agrees that, because of the federal interest in maximizing the use of funds, TDC applies to all public housing funds and revises § 905.314(c)(1) of this final rule accordingly.

Issue: Heating-and-cooling-degree-days should continue to be an essential factor when considering exceptions to TDC. The unique expenses associated with implementing energy-saving and

green features that represent high front-end costs, which may or may not be “cost saving sensitive” but are highly sensitive to depleting energy sources, should be treated similarly. The commenter states that the rule should directly and specifically address the eligible high front-end expenses when green features emphasize renewable energy sources that far exceed TDC, in exchange for preserving the other energy sources that are depleting.

HUD Response: This final rule provides for a TDC exception for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency. HUD believes that, rather than trying to address each possible special case in the rule, this exception preserves PHA discretion to address the commenter’s concern as well as other similar concerns that may arise in individual cases.

Contracts and Contracting

Issue: This commenter states that the proposed rule should subordinate its terms for a covenant to the terms of the financing deal for development. As for the covenant for modernization, it should subordinate such terms only when Capital Fund financing is involved in the modernization of the property. The commenter states that for all other cases it would appear that the 20-year covenant for modernization could then be a reasonable provision for inclusion in a final rule.

HUD Response: Section 9(d)(3)(B) of the 1937 Act (42 U.S.C. 1437g(d)(3)(B)) requires use restrictions to remain on the property for 20 years from the date that modernization is completed with Capital Funds on any public housing or portion thereof. HUD retaining a priority position as to HUD’s financing ensures that the low-income use requirements will continue to be met. HUD has interpreted the 1937 Act to allow appurtenances to be excepted from the definition of public housing (e.g., nondwelling properties such as administrative buildings) which, if included in public housing, would have had to remain under the Declaration of Trust for 20 years from the latest date on which modernization is completed, but may have liens prior to the Declaration of Trust.

Issue: The proposed regulation at § 905.316(a), which provides that PHA procurement must comply with 24 CFR part 85, should be limited to activities funded with Capital Funds.

HUD Response: Section 905.31(a) explicitly refers to public housing

capital activities; no further clarification is necessary.

Issue: A commenter stated that § 905.316(d)(2)(iv), which refers to irrevocable letters of credit as an assurance of completion, is insufficient because the specific terms are not stated. The rule should require that, before accepting a letter of credit, the PHA have its counsel review the proposal form and opine that the PHA and HUD are fully protected under its terms. Another commenter stated that the 25 percent requirement is inconsistent with modern private sector practice and imposes extra costs that do not materially increase the PHA’s security, and, in the context of mixed finance, is unnecessary because the tax credit investors have a strong monetary interest in completion.

HUD Response: The main condition that HUD is concerned about, as stated in the rule, is irrevocability. The letter of credit is only one option for the assurance, and the PHA may select one of the other options. Therefore, HUD does not believe a change is necessary regarding further specificity of the terms. However, HUD agrees to lower the percentage requirement to reflect modern practice, and this final rule now requires a 10 percent irrevocable letter of credit at § 905.316(d)(iv).

Issue: Proposed § 905.308(b)(4) appears to be an incredible expansion of prevailing wage rate requirements, since it appears to apply to third party contracts and to professionals. The commenter requests clarification as to whether, under this section, architects, engineers and technicians must be paid the prevailing wage rates and questioned how to find those rates.

HUD Response: The commenter is incorrect; HUD is not expanding the Davis-Bacon wage rate requirements in this rule. These are standard Davis-Bacon provisions and are required by statute; specifically, as Davis-Bacon requirements related to HUD-funded projects under the 1937 Act (42 U.S.C. 1437j(a)). Guidance can be found at the Department of Labor’s wage rate site, <http://www.wdol.gov/>. HUD also has a Web page with Davis-Bacon information at http://portal.hud.gov/hudportal/HUD?src=/program_offices/labor_relations.

Issue: One commenter asked whether § 905.326, which imposes a 5-year time frame for record retention, intends to add an additional 2 years to the record retention required under 24 CFR 85.36(i)(11) and 85.42(b).

HUD Response: Yes, based on the life cycle of Capital Funds, this rule adds 2 years to the 3 years required under 24 CFR part 85, for a total of 5 years.

Issue: As to § 905.318, a commenter states that a title insurance policy is not available before a PHA takes title.

HUD Response: Title insurance is required at the time the property is acquired by the PHA. This final rule makes this clarification.

Forms

Issue: The definition of “Cooperation Agreement” references a form prescribed by HUD, form HUD–52481, which is available in HUDClips (http://portal.hud.gov/hudportal/HUD?src=/program_offices/administration/hudclips/forms/), but one commenter stated that the form states that it is a drafting guide.

HUD Response: This form has always been a guide because State and local law must be considered as well. Many PHAs have used this form “as is” and that is acceptable as long as it conforms to State and local law.

Issue: One commenter stated that there should be an exception for the use of American Institute of Architects forms, such as AIA–B108–2009 under § 905.316(b)(use of HUD-prescribed contract forms).

A commenter stated that one of HUD’s proposed changes to part 905 would require that PHAs nationwide use standard mandated contract forms. The commenter states that while PHAs should be required to incorporate certain terms and conditions in their contract, they must also have flexibility to address local legal requirements, which may vary from state to state.

HUD Response: HUD-prescribed contract forms include necessary federal and Public Housing Requirements. HUD intends to limit the use of contract forms to HUD forms, because nonstandard and local forms do not reflect the appropriate federal limitations. Therefore, HUD has not changed the form requirements.

Issue: The rule is inconsistent with respect to references to ACC forms. The rule refers variously to a mixed-finance ACC Amendment (§ 905.604(k)(2)), ACC Amendment (throughout § 905.604(k)), and CF Amendment (§ 905.612(b)) in closely related provisions. The rule seems to suggest that it intends to replace 3 ACC forms currently in use with a single CF ACC amendment, but is inconsistent in this respect.

HUD Response: It is not the intention of this rule to replace the 3 ACC forms with a single ACC Amendment. There is one consolidated ACC, and separate ACC Amendments for different sections of the program. A definition of ACC Amendment has been added to § 905.108. There are separate ACC Amendments for the various areas of the

Capital Fund Program (CFP), including but not limited to the CFP annual formula grant, CFP annual RHF grants, the Capital Fund Education and Training Community Facility Program grants that were awarded, and mixed-finance grants.

Replacement Housing Factor (RHF)

Issue: Reduction in RHF grant. PHAs that have a reduction in units due to demolition and disposition have been eligible for an additional grant, the RHF grant. PHAs have been entitled to an initial 5 years of RHF funding and an additional 5 years of RHF funding if certain conditions are met. The rule proposed, for units demolished or disposed of on or after the effective date of this rule, to reduce the RHF to 5 years of funding, in total.

One commenter observed that this change would have a positive impact on the availability of Capital Funds. Several other commenters, however, objected to this change and stated that RHF funding should be standardized to 10 years because RHF funding is the best approach for developing replacement housing, and many PHAs have compelling reasons for demolishing or disposing of public housing property and need this resource, which is one of the few resources remaining to assist with new public housing. There are still thousands of distressed housing units, and until these can be improved, RHF funding should continue at 10 years. PHAs have a capital backlog of an estimated \$32 billion and an average of 10,000 units are lost each year. RHF funding adds up to a vital resource over the course of 10 years, especially given the uncertainty of funding from year to year. PHAs cannot count on an award of HOPE VI or Choice Neighborhood grants, because they are scarce and directed to certain types of projects. The RHF constitutes the only resource available that is dedicated to replacement public housing, and is an important resource for PHAs that do not have HOPE VI funds.

One commenter stated that because the funding is only paid to PHAs that have removed units, without HUD development funds it can take years to develop a viable, fundable plan to for replacement housing. One commenter stated that a PHA cannot count on other resources, and that RHF “constitutes the only resource available that is dedicated to replacement public housing. HUD has not done a study of RHF, including its leveraging effectiveness, and has not established a sound basis for dramatically cutting this much-needed resource.” Even with 10 years’ worth of

funding, agencies must look for other resources, and thus it is not sensible to reduce the amount provided by the RHF even more.

HUD Response: While the RHF is an important tool for development of replacement housing, in the current limited funding environment, the need for replacement housing for a few PHAs has to be balanced with the needs of the majority of PHAs whose Capital Funds modernize existing public housing. These needs are quantified in a study released in June 2011 on modernization needs, “Capital Needs in the Public Housing Program,” prepared by Abt Associates, available at http://portal.hud.gov/hudportal/documents/huddoc?id=PH_Capital_Needs.pdf. The study found that the Nation’s 1.2 million public housing units have an estimated total of \$25.6 billion in existing capital needs. Regarding demolition and disposition needs, the Capital Fund and other sources of funding, such as section 8 funding for replacement housing, can be used to meet these needs. The change in the RHF will result in an increase in Capital Funds, which is a more flexible resource.

However, given the significance of the change, this final rule allows for a longer transition period than proposed. PHAs that would be newly eligible for RHF funding in Federal Fiscal Year (FFY) 2014 will instead receive 5 years of DDTF from the Capital Fund. The Federal Fiscal Year is defined in § 905.108 of this rule as the fiscal year that begins each year on October 1 and ends on September 30 of the following year (PHA fiscal years can have different beginning and ending dates). PHAs that have already begun receiving first-increment RHF funding by FFY 2014 will receive the remainder of their first increment and 5 years of DDTF. If a PHA is already receiving second-increment RHF funding by FFY 2014, it will receive the remainder of its second-increment RHF funding. DDTF funding would have fewer limitations than RHF funding, in that it could be used for modernization needs (of which there is a substantial backlog) as well as development; at the same time, statutory requirements applicable to the Capital Fund, such as the requirements for expenditure and obligation in section 9(j) of the 1937 Act (42 U.S.C. 1437g(j)), will apply. This is a generous transition and should ameliorate the issues discussed by the commenters.

Issue: Scattered site replacement housing. One commenter stated that eliminating 5 years of RHF funds would tie the hands of PHAs that replace older public housing units with new

scattered-site units. Such units may take years to come online and that the local housing opportunities commission is inclined to pass over units in areas with a high affordable housing concentration in favor of units in wealthier areas. The commenter also stated that reducing the time frame for RHF funding may restrict efforts to develop mixed-finance developments that include some public housing because such deals and regulatory regimes are complex.

HUD Response: Firstly, if the PHA in question has already received at least one year of RHF funding as of the effective date of this final rule, the PHA will be eligible under § 905.400(k) for an additional 5 years of RHF funding. Secondly, the change in RHF grant funding will increase the amount of Capital Funds, which is a more flexible resource that, unlike RHF funds, can be used for any Capital Fund purpose, be it development or modernization. This flexibility is particularly important in the case of smaller PHAs whose RHF funds typically are not enough at any one time to engage in development activities. In many cases, by the time these unused funds are recaptured by HUD, they are lost to their intended use for assisted housing because the life cycle of the funding has expired and the funds must be returned to the Department of the Treasury as general revenues. Under DDTF, PHAs in this situation will be able to use the funds for modernization needs, thus assuring that funds intended for housing needs actually go to that purpose. Also, because these funds are, in fact, Capital Funds and not part of a separate appropriation, the phased-in decrease to 5 years means that there will be more Capital Funds available to all PHAs receiving Capital Fund grants.

Issue: Grandfathering. Commenters stated that PHAs currently receiving RHF grants should retain their full 10 years of eligibility.

HUD Response: Under this final rule, PHAs that have received at least one year of RHF funding as of the effective date of this rule will be eligible for 10 years of RHF grants if they meet the regulatory requirements of this rule, including leveraging (see § 905.400(i)).

Issue: Accumulation of RHF funds. Commenters stated that 10 years of RHF grants should be “banked” or accumulated on a PHA’s behalf, and paid out if the PHA meets obligations to develop one or more HUD-approved mixed-finance projects.

HUD Response: Appropriations statutes, not regulations, control the period of availability of federal funds, including Capital Funds; in the case of FY 2010, FY 2011, and FY 2012 Capital

Funds, the funds are available only until September 30, 2013; September 30, 2014; and September 30, 2015, respectively (see, respectively, div. A, tit. II, Pub. L. 111–117 (approved December 16, 2009); div. B, tit. I, section 1103, Public Law 112–10 (approved April 15, 2011); and div. C, tit. II, Public Law 112–55 (approved November 18, 2011)). This limitation prevents lengthy multiyear accumulations as suggested. Even were the funds involved to be appropriated as no-year funds, as a general matter, HUD finds that it is not appropriate for public funds to remain unobligated and unexpended for long periods of time, a policy also expressed in section 9(j) of the 1937 Act (42 U.S.C. 1437g(j)), which penalizes PHAs for delayed obligation and expenditure of funds.

Issue: Reduce administrative costs rather than eliminating RHF grants. Commenters stated that while administering the RHF grants can be cumbersome for HUD, the administration of the program should be simplified rather than HUD reducing the amount made available to the program. The commenters suggested that if the number of units receiving RHF grants is relatively stable from year to year, then after an initial cost, 5 years of RHF funding may not reduce the remaining money in the Capital Fund, while alleviating some of HUD’s administrative burden.

HUD Response: Administrative costs are not the major contributor to the need to reduce the total number of years of RHF funding. RHF funds and traditional Capital Fund grants are both funded from the same appropriation, which was \$2.044 billion in FFY 2011. While RHF is an important tool for development of replacement housing, the need for replacement housing for a few PHAs has to be balanced with the needs of the majority of PHAs whose Capital Funds modernize existing public housing. Reducing RHF grants from 10 years to 5 years will make more funds available for modernization. It is also common for PHAs to accumulate 5 years of funding and then realize there are insufficient funds to develop units and, subsequently, reject the funding, or allow the funding to be recaptured. When this occurs, most of the funding that is returned to HUD must be transferred to the Treasury, and cannot be redistributed because, during the accumulation, the life cycle of the funds from the first and seconds years of second-increment funding will have expired.

Regarding administrative costs, the replacement housing policy that is presented in this final rule has been

revised from the policy presented in the proposed rule, based on public comment. The revised policy simplifies the administration of the program for both HUD staff and PHAs. While the revised policy will still only provide 5 years of additional funding for units removed from inventory due to demolition or disposition, the limitations on the current RHF funding will be eliminated, allowing PHAs to use the funding for any eligible costs under the Capital Fund program, including development.

Issue: Plans for future disposition activities rely upon RHF grants to fund the development of new rental and homeownership units. With the elimination of the one-for-one replacement statutory requirement the need for RHF grants has become greater over time because it provides critical financing to demolish outdated properties. Additionally, the proposed change would make it more difficult to maintain significant numbers of highly subsidized units in mixed-finance properties.

HUD Response: Capital Funds and section 8 funds are available for these purposes. Furthermore, this final rule provides for a lengthier transition period and, beginning in FY 2014, DDTF funds that can be used on the same basis as Capital Funds.

Issue: RHF grants should not be available for units lost to homeownership, but only for units lost because of demolition or disposition, and should be limited to highly leveraged replacement rental transactions using only HUD’s mixed-finance methodology.

HUD Response: In this final rule, RHF grants eligibility is based on units lost as a result of demolition and disposition, but not homeownership. In addition, there is a leveraging requirement for PHAs that have already received some RHF funding as of the effective date of this rule and wish to receive an additional 5 years. HUD does not agree that RHF grants should be restricted to mixed-finance as that is overly inflexible.

Issue: Second-increment RHF funds continue to be needed to replace housing losses resulting from ongoing, necessary demolition and disposition. PHAs state that they made demolition and disposition plans based on RHF funding being available.

HUD Response: As originally designed, the RHF grants were never intended to fund the cost of replacement of every unit demolished or disposed of from the PHA’s inventory. However, in order to ease the transition for PHAs that have already demolished or

disposed of units that are relying in part on RHF grants, the proposed RHF regulation has been modified in this final rule at § 905.400(j) and § 905.400(k). PHAs that have received at least one year of first increment RHF funding prior to FFY 2014, the proposed effective date of the DDTF, will be eligible to receive up to 10 years of funding for units removed from inventory as a result of demolition or disposition. The additional 5 years of DDTF funding will not be subject to the same restrictions as RHF grants because it will be included in the Capital Fund grant (although it will be subject to the same legal requirements as any Capital Fund grant, including the obligation and expenditure requirements of section 9(j) of the 1937 Act (42 U.S.C. 1437g(j)), and any time limit placed on the appropriation by the applicable appropriations act). It should be noted that the PHA always has the option to use additional Capital Fund formula grant funds as a resource in a mixed-finance transaction.

Issue: The change to RHF grants will severely impact bond funding, where the 10 years of RHF grants were a major determinant to the amount of bonds issued. The commenter cites an example in which a “vast majority” of units slated for demolition were demolished well before FY 2010, but, because a few units were not demolished until 2010, the units remained in the Public Housing Information Center (PIC) database in FFY 2010 and would apparently be subject to the proposed rule limiting RHF grants to a single 5-year increment even though 10 years of RHF grants from the demolition of these units had been pledged to an outstanding bond issue. HUD should use the date of the demolition or disposition application, not the date of removal from the PIC system, to determine the applicability of new RHF grant rules.

HUD Response: Under this final rule, the postponement of the RHF transition to FY 2014, along with the future provision of DDTF funding, should allow for bond funding to continue. As to the issue of using the date of the application to determine the applicability of new RHF grant rules, the mere existence of an application is far too preliminary a step. First of all, a given application may or may not be approved. Secondly, even if approved, there are cases when demolition does not occur for a considerable period of time, even years. Despite the single example cited by the commenter, the approach that will generally help ensure the best use of public housing funds, and which is the most verifiable, is to

base the payment of RHF or DDTF funds on removal of the units from the PIC system.

Issue: Due to the federal budget crisis, RHF funding should be eliminated altogether. Since PHAs also receive tenant protection vouchers, the government is “paying double” for each unit removed.

HUD Response: Removing RHF funding altogether would have negative consequences for PHAs that have planned demolitions and dispositions based on future availability of RHF grant increments for replacement housing. On the other hand, to the extent possible, in today’s funding environment, PHAs must use federal funds to leverage other sources of funding. HUD believes that the RHF transition provisions in this final rule for PHAs already receiving, and relying on, RHF grants offer the best balance between the need to maximize sources of funding and the need to fund adequate replacement housing. PHAs newly coming into the RHF program as of FY 2014 will receive 5 years of more flexible DDTF funds. It should be noted that in order to prevent duplicative funding, RHF and DDTF funding is prohibited for a PHA that will replace units using another source of federal funding (see § 905.400(i)(5)(iii) of this final rule).

Issue: HUD has not undertaken a study of the RHF grant program, including its leveraging effectiveness, and has not established a sound basis for dramatically cutting this much-needed resource.

HUD Response: HUD has many years of experience with RHF grants and leveraging, which has shown that without leverage it is quite difficult to achieve unit replacement. HUD is not dramatically cutting a much needed resource. Not only will all activities that are currently eligible under the RHF grant program still be eligible under DDTF, but the DDTF will also allow PHAs to use this funding on any eligible activity under the Capital Fund Program. Further, HUD is providing a lengthier transition to DDTF to accommodate PHAs’ concerns. It should be noted that the funding for the RHF and DDTF grants is taken out of the general Capital Fund Appropriation. In limiting the DDTF funding to 5 years, the funding that would have gone to only specific PHAs receiving 10 years of RHF funding, will now be distributed among all of the PHAs receiving a Capital Fund formula grant.

Issue: Several commenters objected to the apparent retroactive date of the change to RHF.

HUD Response: The changes to the RHF grant program will not be

retroactive, but will be implemented starting in FFY 2014, which should ameliorate the impact.

Issue: In order to compensate for RHF grants that will be “lost” under this provision, PHAs should have the freedom to select higher-income applicants.

HUD Response: Under this final rule, PHAs that have demolished or disposed of units, and have begun to receive first-increment RHF funding as of FFY 2014, will be eligible for an additional 5 years of DDTF. Other PHAs will have significant advance notice that they will be eligible for only 5 years of DDTF and can do their financial planning accordingly. Finally, there is no direct nexus between funding for replacement housing and admission of higher-income residents.

Issue: The change to RHF funding is contrary to the statutory requirement that the Capital Fund formula be developed by negotiated rulemaking.

HUD Response: The statutory requirement of section 9(f) of the 1937 Act (42 U.S.C. 1437g(f)), is that “the formulas . . . shall be developed according to procedures for issuance of regulations under the negotiated rulemaking procedure. . . .” HUD interprets this to mean that the formulas are initially developed by negotiated rulemaking, not that each subsequent revision requires negotiated rulemaking. HUD previously fulfilled this statutory obligation to this regulation (see HUD’s final rule published on September 14, 1999 at 64 FR 49924).

Issue: Funding for small numbers of units. Some PHAs disposed of or demolished small numbers of units at various times, which resulted in RHF allocations too small to acquire or develop any replacement units. PHAs should be allowed to use funds that fall below certain thresholds for other public housing uses, such as modernization. One commenter stated that HUD should consider setting a minimum threshold for RHF funding, below which a PHA may elect to use it for general Capital Fund purposes and not replacement housing.

HUD Response: The final rule addresses these issues by providing that the 5-year DDTF be given to PHAs in their Capital Fund formula grant. The formula grant, along with the increment that has been added, can be used for any Capital Fund eligible purpose, including development of replacement housing or modernization.

Issue: The rule should include an exception where PHAs that demonstrate hardship will be eligible for a second increment of RHF funding. Hardship could include, but not be limited to, in-

process development projects that anticipated second-increment RHF funding and localities with critical shortages of affordable housing.

HUD Response: The final rule addresses the issue of in-process development by extending the transition and providing for DDTF. As for other forms of “hardship,” such as shortages of affordable housing, HUD already provides funds for housing development and for vouchers, among other forms of funding.

Eligible Activities and Costs

Issue: Is the phrase “public housing capital assistance” in § 905.314(b) intended to be broader than “Capital Funds?” If so, other included funding sources should be specified.

HUD Response: HUD has added a definition of “public housing funds” in § 905.108 that encompasses a broader source of funds.

Issue: A commenter stated that the language in proposed § 905.202 designating those items that are “not modest in design and cost,” or not “customary for the locality” as ineligible is overly broad and could disqualify many green and energy conservation measures and complicate the use of Capital Funds for all but the simplest of projects.

HUD Response: Green and energy conservation measures that do not otherwise qualify as eligible activities will be covered by the TDC exception found in § 905.314(c) of this final rule. Further, it has been long-standing regulatory description and PHA practice to design, construct, and equip public housing units to improve substandard conditions and to harmonize with the neighborhoods they occupy, meet building standards, and achieve modest levels of comfort and liveability for the low-income public housing residents to be served, and all at a reasonable cost as defined under TDC. See e.g., former 24 CFR 941.203 and 968.112(b) and (o).

Issue: Add “except for emergencies” to proposed § 905.202(b), which identifies activities and costs not identified in the 5-year action plan as ineligible costs.

HUD Response: This final rule clarifies that emergencies that are not identified in the 5-year action plan are eligible costs.

Issue: The proposed regulation at § 905.202(g) uses a test for ineligible costs (“in excess of the amount directly attributable to the public housing units”) that may be read more literally than is appropriate. In a mixed-finance project, for instance, are the common areas “directly attributable” to the public housing units? Costs should be

deemed ineligible when they are disproportionate to the benefit received by the public housing program in relation to other programs, or similar standard. The commenter also states that in § 905.314(a), the concept of “costs directly attributable to the public housing program” should be replaced with a reasonability or proportionality concept. The commenter also states that it is inappropriate for HUD to reserve the right in § 905.202(i) to retroactively find costs ineligible, when such costs otherwise came within the definition of eligibility and did not violate some standard set forth in the rulemaking provisions of the Administrative Procedure Act (APA) (5 U.S.C. 501 *et seq.*).

Another commenter stated that the “directly attributable” standard does not provide a standard by which a PHA can justify a cost’s eligibility. This commenter states that the principles for cost allocation in OMB Circular A–87 (Cost Principles for State, Local, and Indian Tribal Governments) should be the basis for the eligibility determination.

HUD Response: HUD disagrees. While concepts such as proportionality and reasonability are subjective, direct attribution to the intended purpose of the funds is objective. In general practice, the objective measures would not exclude eligible costs along the lines of what the commenter claimed. By requiring direct attribution to public housing, HUD is ensuring responsible use of government funds, and acting in accordance with 2 CFR Part 225. As to the APA issue, the APA requires public notice and an opportunity to comment on the rule itself, which the public has received regarding this rule. Each individual decision that may be made under this rule is not subject to additional notice and comment. On the contrary, it is entirely lawful for federal agencies to reserve discretion over managing their own programs.

As to OMB Circular A–87, Cost Principles for State, Local, Indian, and Tribal Governments, now codified at 2 CFR part 225 (part 225), the final rule cites part 225 in relation to reasonable costs, and as one test for ineligible costs under § 905.202(d). However, by suggesting that 2 CFR part 225 be the sole test for the connection between the costs and the public housing program, the comment misunderstands the nature of the circular. Part 225 is designed to identify basic principles, not to take the place of specific program regulations. Part 225 states, *inter alia*, “The principles are for the purpose of cost determination and are not intended to identify the circumstances or dictate the

extent of Federal or governmental unit participation in the financing of a particular program or project.” (See 2 CFR part 225, Appendix A, General Principles for Determining Allowable Costs, at § A.1). Also, part 225 states that allowable costs must conform to “governing regulations as to the types or amounts of cost items.” (See *Id.* at § C.1.d). By requiring direct attribution to public housing, HUD is acting well within the scope of 2 CFR part 225, its statutory authority, and APA principles.

Issue: While § 905.200(b)(12) makes approved homeownership activities eligible, some activities—such as relocation assistance, mobility counseling, and homeownership counseling—may appropriately occur prior to the approval of a specific homeownership plan. After the introductory phrase “activities associated with approved homeownership,” the rule should add “provided, however, that activities under sections C and D may occur prior to approval of the homeownership plan.”

HUD Response: Resident relocation and mobility counseling, which includes those items mentioned in the comment, are separately eligible under § 905.200(b)(10) of this final rule. While the physical relocation has to be after the approval of the homeownership plan, the mobility counseling and surveying of the tenants can be done at any time. However, as the section in question does not specify the need for a homeownership plan or timing in relation to it, no rule revision is required.

Issue: Under § 905.312(a), are amenities such as air conditioners, dishwashers, washing machines and dryers eligible costs, or prohibited luxuries?

HUD Response: HUD agrees that some further clarification may be helpful with respect to amenities. This final rule clarifies that air conditioning is an eligible modest amenity. Further clarification on luxury items and modest amenities will be provided in future guidance.

Issue: Are Capital Funds eligible to be used to construct office, resident service, or maintenance facilities?

HUD Response: Yes.

Issue: How does § 905.202(f), on direct provision of social services, relate to management improvements, and could HUD provide some examples?

HUD Response: Section 905.202(f) provides that direct provision of social services is not an eligible Capital Fund expense. Examples of such ineligible expenses, provided in the rule, are salaries for social workers or General

Educational Developmental (GED) teachers, and this prohibition would apply to other benefits for such workers as well. Statutorily, under 42 U.S.C. 1437g(d), services simply are not Capital Fund eligible costs; rather, the costs of the provision of services may be an operating cost under the Operating Fund as provided in 42 U.S.C. 1437g(e)(1)(D). While it is not entirely clear what the commenter means by “relate to management improvements,” the commenter appears to be asking whether these types of costs may nonetheless be permitted under the Capital Fund as management improvements. Eligible management improvements under § 905.200(b)(7) of this rule include activities that have a linkage between the management improvement and the correction of an identified management deficiency. Generally, the ineligible social services expenses about which the commenter asks would not be tied to management in such a way as to make them eligible as management improvements. HUD may issue further guidance on this subject in the future.

Issue: One commenter states that, in § 905.200(b)(8), the discussion of eligible resident self-sufficiency activities refers to funding from the Operating Fund for \$25 per-unit, per-month, for resident participation. The commenter states that Operating Fund rule at 24 CFR 990.190(e) references only \$25 per annum.

HUD Response: This statement is corrected in this final rule.

Issue: The examples of Capital Fund-related legal costs at § 905.200(b)(13) are too limited and should be expanded. Costs that specifically should be mentioned include: negotiating and drafting mixed-finance arrangements; negotiating and reviewing property descriptions; title policies, regulatory interpretation, opinions, drafting, reviewing, and negotiating evidentiary documents for mixed-finance development, the Capital Fund financing program, conventional development, and acquisition transactions.

HUD Response: Unfortunately, existing funding does not allow every potential legal cost that one can envision to be expressly included. All of the legal costs mentioned in the comment would be eligible if they were reasonable in cost and related to the Capital Fund development activities. However, this rule is not intended to be an exclusive list of eligible and Capital Fund-related legal costs.

Issue: Section 905.200(b)(7)(iii) (“Activities that include or foster equal opportunity”) should be revised to

include Limited English Proficiency (LEP), Reasonable Accommodation, and Violence against Women Act (VAWA) policies and their implementation as part of equal opportunity requirements.

HUD Response: Housing counseling for residents and prospective residents, as well as the design and construction of accessibility improvements, are eligible under the Capital Fund. (See §§ 905.200(b), 905.200(b)(7)(i) and (iv) and 905.200 (b)(10) of the rule.) Generally, a PHA would use operating subsidy or other noncapital resources for staffing and program materials for LEP or VAWA, rather than management improvements under the Capital Fund.

Issue: Proposed § 905.200(b)(4) states that vacancy reduction may be an eligible activity. It would be helpful for the rule to be more explicit about what is expected, either in the rule itself or in guidance. Also, compliance with accessibility requirements should be explicitly mentioned under proposed § 905.200(b)(6) and should be more specific.

HUD Response: HUD is making no change to the final rule text, but may issue future guidance on this and other issues. As to accessibility specifically, § 905.312 addresses accessibility requirements.

Issue: The rule should allow set-asides of capital replacement reserves for future modernization as an eligible activity. The inclusion of “modernization” as an eligible activity in section 9(d)(1)(A) of the 1937 Act (42 U.S.C. 1437g(d)(1)(A))—coupled with the authorization to accumulate funds to undertake modernization, substantial rehabilitation, or new construction of units in section 9(j)(1)(B) of the 1937 Act (42 U.S.C. 1437g(j)(1)(B))—should be sufficient legal basis to allow for such capital replacement reserves.

HUD Response: Replacement reserves as such are not an authorized use of Capital Funds under section 9 of the 1937 Act (42 U.S.C. 1437g). Under section 9(j)(1)(B) of the 1937 Act (42 U.S.C. 1437g(j)(1)(B)), accumulated funds for modernization are required to be expended within 24 months once sufficient funds are accumulated to undertake an activity.

Issue: Subpart B, starting at § 905.200, should have more precise language describing what is covered by the subpart.

HUD Response: HUD agrees and has made the suggested revision at § 905.200(a) of this final rule.

Issue: The term “significant” in the phrase “. . . PHA must have determine that there is no debt service payments, significant Capital Fund needs, or

emergency needs that must be met prior to transferring 100 percent of its funds to operating expenses” in 24 CFR 905.314(1)(2) should be clarified.

HUD Response: HUD is considering issuing guidance to assist HUD field offices and PHAs with what information should be evaluated prior to allowing a small PHA to transfer all of its Capital Funds to Operations.

Federalization and Federalism

Issue: The rule should clarify the meaning of § 905.602(c) of the proposed rule, prohibiting federalization of certain projects. One commenter stated that the rule should provide that federalization is prohibited except as otherwise approved by HUD. Another commenter stated that there is no authority for prohibiting nonfederal public housing owned by a PHA from being federalized as provided in that section and that such policy is not in the interest of preserving affordable housing. Another commenter noted that the only authority for allowing federalization is found in section 9(n) of the 1937 Act (42 U.S.C. 1437g(n)), and that any such language should be carefully limited to apply only to “covered locally developed public housing units” as defined in section 9(n). This commenter stated that there is no other statutory authority to limit a PHA’s decision to bring PHA-owned properties into the public housing program, subject to the HUD approvals generally required for public housing development. In some instances, such units may provide the most economical and best opportunities for the production of replacement public housing.

HUD Response: This final rule revises proposed § 905.602(c) titled “Federalization,” to make a more general statement that nonpublic housing properties may be used in the development of public housing units provided all requirements of the 1937 Act and the development requirements of this part are met. For historical reference, former section 9(n) of the 1937 Act was never used by HUD to federalize projects. Former section 9(n) was repealed by the Consolidated Appropriations Resolution, 2003 (Pub. L. 108–7, 117 Stat. 1, approved February 20, 2003; see 117 Stat. 502) with additional directions applicable to “covered locally developed public housing units” in the states of New York and Massachusetts. HUD’s regulation at § 905.602(c) is neither a development exception nor a new development method relying on any form of prior authority relating to Federalization. Instead, HUD may consider any

property presented for development of public housing units under all of the existing requirements of the 1937 Act and 24 CFR part 905.

Issue: HUD's proposed regulation at § 905.602(c) should be revised to provide that a PHA may acquire and modernize a building that it already owns outside the public housing system, if that same modernization would be permitted for new construction under § 905.602(b).

HUD Response: Section 905.602(c), both as proposed and in this final rule, allows this activity to occur.

Issue: This rule triggers Executive Order 13132 on Federalism. This rule opens the public housing market to private partnerships with restrictions on the public on obtaining information and attending meetings, and without the accountability required for use of public funds. The commenter states that planning issues are under the jurisdiction of local municipalities under state requirements.

HUD Response: Executive Order 13132 on Federalism concerns regulations and proposed legislation that have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. This regulation does not have these direct effects on states or on the relationship between the Federal Government and the states. This rule, which is authorized by statute, establishes substantive regulations and procedures for the use of federal funds by PHAs, as directed by statute, and does not preempt state law. Therefore, this rule does not trigger the Executive Order.

Conversion of Units

Issue: A commenter states that § 905.10(f)(3) as codified prior to the effective date of this final rule indicates that the total estimated need of the development is unchanged by conversion of units. The commenter states, however, that the preamble to the final rule adopting the existing regulation explains that "reduction of units is not based only on demolition or disposition." If the intention of the new Capital Fund rule is not to change the formula, the language of the current rule regarding conversions should remain. The commenter expressed concern about the impact of this rule, considering the unit conversion it must undertake at one of its developments. HUD's policy, as stated in the proposed rule, would result in a permanent loss that is difficult for a housing agency of a small size to absorb. If a small PHA

has an outstanding Capital Fund Financing Program loan, the terms of which require maintaining its public housing stock to generate sufficient Capital Fund grants to sustain three-to-one debt service coverage, HUD's proposed rule also may mean that it cannot undertake the necessary reconfiguration without partial prepayment of the loan.

The commenter further states that HUD's funding policy should encourage rather than discourage PHA action to convert efficiencies to one-bedroom units. Because PHAs have the same square footage to manage and renovate, it would be reasonable for the Capital Fund to build in the proper incentive by not taking away funds when conversions occur.

HUD Response: The Capital Fund formula is based on a complex calculation with a variety of characteristics including, but not limited to, the number of units in the development, the average number of bedrooms, and the location and age of the development. Based on the way the formula is calculated, if one PHA has a larger formula share it reduces the formula share for other PHAs. It was never the intent of the Capital Fund formula to result in HUD continuing to pay the modernization needs or the administrative costs of units that no longer exist at one housing authority while making other housing authorities with modernization needs pay for them, which would be the result if the Capital Fund were used to pay for units lost to conversion. The incentive for reconfiguration or conversion for the PHA is to better serve the needs of the low-income families in the community. Furthermore, funding for reconfiguration or preparing units for conversion, and any necessary relocation, are eligible Capital Fund expenses.

Issue: A commenter states that while the new rule specifically states that reconfiguration of units will alter Capital Fund formula funding allocations, this policy was not articulated in the Capital Fund rule prior to the proposed rule and may have unintended consequences, such as a decrease of subsidy to the agency.

A commenter states that § 905.400(f)(3) differs from the current regulation, which is that conversion of public housing units does not change the Capital Fund formula shares. This proposed policy will discourage, for example, combining of unmarketable efficiency units into one-bedroom units.

HUD Response: HUD is aware that some PHAs have been confused about the intent of the proposed provision,

§ 905.400(f)(3), as well as the current provision, 24 CFR 905.10. The purpose of this provision is to clarify HUD's policy as it has consistently been implemented.

Issue: How does the limit on new units found at § 905.602(b)(1) apply to merged units? May a PHA replace merged units, and will the new units be eligible for Capital Fund and operating subsidy?

HUD Response: This limit based on the number of units in management as of October 1, 1999, would remain the same. Thus, for example, if a PHA had a unit count of 100 as of 1999 and in FY 2005 the PHA decided to merge 6 efficiency units into 3 one-bedroom units, the PHA's unit count would be reduced to 97, and the PHA would be allowed to build 3 additional units.

Separating CFP Informational Requirements From PHA Annual Plan Requirements

Issue: Small PHAs should not have the same reporting requirements as large authorities and should operate as stated in HERA. Removing some reporting requirements from the annual plan and making their submission separate would result in small housing authorities being obligated to submit forms from which they are currently exempt. Even with the passage of HERA, small housing authorities continue to suffer from an excessive regulatory structure. HUD should not reestablish a regulatory burden that has been lifted by HERA. HUD should find a less burdensome method of receiving any necessary information, such as through an annual audit.

HUD Response: These commenters appear to be referring to qualified PHAs, a category established under HERA as "a public housing agency meeting the following requirements: (1) the sum of public housing dwelling units administered by the public housing agency and the number of vouchers under section 8(o) of the 1937 Act is 550 or fewer, and (2) the public housing agency is not designated as a troubled PHA under section 6(j)(2) and does not have a failing score under SEMAP during the prior 12 months." While qualified PHAs are exempt from submitting a PHA Annual Plan, they are not exempt from the requirement to hold an annual public hearing or to submit a 5-Year Plan. Further, HUD has authority under section 9 of the 1937 Act (42 U.S.C. 1437g) to obtain information needed to calculate the Capital Fund formula and monitor the implementation of the CFP.

Issue: Large PHAs (over 550 units) that are required to submit both a PHA

Annual Plan and a Capital Fund program submission should be able to submit those documents at the same time as permitted under current rules. A key goal of the PHA planning process under section 5A of the 1937 Act (42 U.S.C. 1437c-1) is to unify and consolidate PHA planning and reporting requirements from the various programs that PHAs administer in order to create efficiencies for PHAs and HUD, and also to provide residents and the community with an opportunity to review the PHA's plans holistically. The changes included in this proposed rule may have the impact of requiring a second public process, reducing efficiency, and creating confusion in the community about the opportunities for input. If a PHA submits their annual plan, and then subsequently submits a Capital Fund budget that alters the annual plan, the PHA will be required to hold a second public hearing process, unnecessarily burdening PHAs.

A commenter states that a separate public process from developing the agency plan should not be required. Combining these processes has worked well. The commenter also stated that it is difficult to get resident participation and that all parts of a PHA are tied together and should be discussed in total, rather than the context of individual meetings. The commenter concluded that combining this public consultation has worked well for over 10 years. Decoupling the capital planning from the overall agency planning will make it more difficult to see the big picture of the PHA, require more administrative time and expense for the PHA with separate resident advisory board actions, and make it more challenging for the PHA Board to pass an agency budget that contains both operating and capital expenditures. Furthermore, it may not be feasible to schedule a resident meeting and a Board of Directors meeting in time to comply with HUD deadlines for submission of the ACC Amendment. This commenter suggests HUD extend the deadlines.

HUD Response: HUD's regulations at § 905.300(b)(3)-(4) are revised in this final rule to clarify that the PHA is to present the Capital Fund submission to the public and its residents and Resident Association Board (RAB) concurrent with the public hearing being held on the PHA Annual Plan. By making these submissions concurrent, the PHA will be able to present an integrated plan for public housing to the community and to the RAB. The PHA must consider the recommendations of the RAB concerning both the PHA Annual Plan (under current 24 CFR part 903) and the Capital Fund submission,

and these submissions must be consistent with any applicable Consolidated Plan. This final rule further clarifies that the required forms and information on the Capital Fund submission will be submitted along with the Annual Contributions Contract Amendment submitted to HUD when the annual Capital Fund awards are made.

Issue: How does HUD have the discretion to require separate reporting requirements for the Capital Fund activities, considering that certain items, such as capital improvements and asset management, are required to be in the PHA Plan?

HUD Response: The PHA Annual Plan requirements are satisfied with general information, as opposed to the more specific information required for Capital Fund formula purposes. They are not the same requirements.

Issue: The language regarding budget submission requires clarification. According to a commenter, the proposed rule states that: "The PHA's budget must be approved by the PHA's Board of Commissioners, but does not require HUD approval (see § 905.300(b)(1))." If that in fact is the case, why require the budget to be submitted to HUD when the CFP ACC is submitted to HUD? The proposed rule should state that the budget must be approved and therefore gets submitted to HUD for review and approval, or that the PHA's budget must be approved by the PHA's Board of Commissioners, and does not need to be submitted to HUD for its review and approval. One commenter states that PHA Board approval only should be required.

HUD Response: This final rule revises § 905.300(b)(1)(iv) to state that the PHA's 5-Year Action Plan and budget must have been approved by the PHA's Board of Commissioners before it is submitted to HUD for review and approval. Under the current process for Qualified PHAs HUD reviews the PHA's budget for eligible activities and compliance with cost limits and other requirements. The HUD review is tantamount to HUD approval. Therefore, the language has been changed to signify that HUD approval is required.

Issue: HUD should provide additional funding to defray the cost of the PNA inspection. Another commenter questioned whether PNA inspections would be conducted by PHA staff or outside firms, thus resulting in additional costs. Another commenter stated that the rule should provide more details about the PNA. Another commenter stated that the PNA should be a flexible planning tool and not impose requirements.

HUD Response: The PNA is currently addressed in a separate rulemaking (see HUD's proposed rule published on July 20, 2011, at 76 FR 43219), which provides details on the PNA. Unfortunately, due to constraints on funding, HUD cannot provide extra funds for this purpose.²

Issue: A commenter stated that in § 905.300(b)(3) the reference relating to the PHA Annual Plan is confusing as the CFP is being decoupled from the PHA Annual Plan process. The commenter questioned whether HUD is requiring a separate consultation via the processing of the PHA Annual Plan or it can be a stand-alone process. Another commenter states that decoupling CFP requirements from the PHA annual plan is "essential to guaranteeing resident input"; however, it may also be beneficial to maintain explicit requirements for resident meetings and input.

HUD Response: In this final rule, most cross references in § 905.300(b) to 24 CFR part 903 are removed and § 905.300 is expanded to include sections on resident and RAB participation, public hearings, definition of significant amendment, criteria for plan revision, and procedures for HUD review and approval. These changes should ensure that the decoupling is complete.

Development, Redevelopment, and Modernization

Issue: Since this regulation replaces part 941 in full, whenever the rule regulates the development process, it should refer not only to Capital Funds, but also HOPE VI, Choice Neighborhoods, development funds, and other sources appropriated by Congress for the development of public housing.

HUD Response: This final rule includes a definition of "public housing funds" at § 905.108 to provide this broader definition.

Issue: Proposed § 905.314(g) provides that the modernization cost limit is 90 percent of TDC. One commenter suggests that the rule allow determination for redevelopment to be made when modernization costs reach a lower threshold such as 70 or 80 percent. In such cases, when the community believes such modernization expenditures would not be prudent use of federal financial assistance, such a community or PHA should be able to decide instead to demolish and develop new affordable housing.

HUD Response: Demolition of public housing is governed by section 18 of the

² Please see footnote #1 for more information.

1937 Act (42 U.S.C. 1437p) and is beyond the scope of this rulemaking.

Issue: The reference to Capital Fund financing in proposed § 905.600(c) is unclear.

HUD Response: Proposed § 905.600(c) on Capital Fund financing is revised in this final rule. HUD's final rule on Capital Fund financing (see final rule published on October 21, 2010, at 75 FR 65208) is incorporated in subpart E of this final rule.

Issue: Proposed § 905.600(d) suggests that a PHA or a PHA's partner would solicit construction bids after approval of a development proposal. At least in the mixed-finance environment, a final development proposal cannot be submitted without a firm construction price.

HUD Response: In this final rule, HUD's regulation at § 905.600(c) on the development process is revised. HUD does not dictate when a PHA or a PHA's partner solicits construction bids.

However, the PHA must submit, as part of its Development Proposal (§ 905.606), an independent construction cost estimate or actual executed construction contract that supports the permanent and construction budgets for the project.

Issue: Proposed § 905.600(e)(7) should refer to "proceeds" of an Operating Fund Financing Program (OFFP).

HUD Response: This final rule makes this revision at § 905.600(d)(8).

Issue: Proposed § 905.202(h) is overbroad and could be read to prohibit temporary or bridge funding.

HUD Response: This section, at § 905.202(i) of this final rule, refers to costs that are actually funded by a duplicate source and temporary or bridge financing does not result in duplicate funding.

Issue: Section 9(l) of the 1937 Act (42 U.S.C. 1437g(l)) allows for capital- and operating-fund-only transactions, and permits HUD to reduce the period during which the property must be operated according to Public Housing Requirements. However, the proposed rule does not reflect this flexibility. Also, following the statute, the rule should allow PHAs to make section 8 assistance available in cases where there is operating assistance but not Capital Fund assistance.

HUD Response: Generally, the reference in § 905.304(a)(3) to "such shorter period as permitted by HUD by an exception" implements the flexibility under 42 U.S.C. 1437g(l).

In the case of mixed-finance specifically, § 905.604(j)(3)(ii) states that the term of the ACC Amendment will be determined based on the assistance provided under § 905.304, "unless reduced by the Secretary." Also, if the

PHA is no longer able to provide operating subsidy, final rule § 905.604(j)(3)(iii) permits early termination of the DOT or Declaration of Restrictive Covenants and provides public housing residents with a relocation option, which may be a unit in another project or a Housing Choice Voucher.

Issue: A commenter stated that the proposed regulation at § 905.312(c)(1) should not refer to outdated Handbook 7485.2 REV.

HUD Response: This handbook is not referenced in the rule.

Mixed Finance

Issue: All provisions of this rule should be premised on the belief that the interests of all participants are advanced if the regulations permit a predictable and efficient restructuring such that a project can be operated on a stable basis with whatever level of federal subsidy is reliably available.

HUD Response: Along with statutory compliance, this rule also provides for sufficient flexibility to meet project goals.

Issue: The rule should provide more extensive standards. The articulated standards in the proposed rule bridge the gap about halfway—they include some substantive standards, yet do not include some of the fundamental "rules" that have developed over the years regarding, for example, funding and replenishing of reserves and required segregation of public housing funds (both direct subsidy and tenant rents) from attachment in the case of foreclosure or loan acceleration.

HUD Response: The types of issues to which the commenter refers are matters of policy and procedure that are best stated in guidance, such as PIH Notices and policy statements.

Issue: HUD's regulation at § 905.600(d) should be revised to take into account that, in mixed-finance, the construction contract is virtually always signed before proposal approval. Accordingly, the second sentence of § 905.600(d)(3) should be revised to remove the phrase, "After HUD approval of the development proposal. . . ."

HUD Response: This final rule adopts, at § 905.600(c)(3), this revision to accord with general industry practice.

Issue: Commenters questioned language suggesting why the mixed-finance category includes projects funded entirely with Capital Funds.

HUD Response: If there is an Owner Entity other than the PHA, the project is considered mixed-finance even if 100 percent of the funding is public housing Capital Funding. However, if the PHA

holds a 100 percent interest in the project, it is not a mixed-finance project.

Issue: The rule is overbroad in requiring the formation of an "Owner Entity" in situations where nonpublic housing sources are being utilized, but no third-party participation in the ownership is required. There are instances, where state or local resources may be used, where the rule would seem to require another entity, but the transaction should not require the PHA to go to the expense of establishing and maintaining a separate Owner Entity.

HUD Response: This final rule revises § 905.604 to clarify this role of the Owner Entity. The partnership arrangement to which the commenter refers applies in mixed-finance situations; where the PHA owns 100 percent of the units, mixed-finance development would not apply.

Issue: Proposed § 905.604(a) should be revised to reflect that in some cases, such as meeting Davis-Bacon requirements, only the mixed-finance owner can comply; the PHA can require compliance, but cannot directly comply itself.

HUD Response: HUD agrees, and this final rule incorporates the suggested change at § 905.600(a).

Issue: HUD's regulation at § 905.604(h), "Irrevocability of financial commitment," should allow alternatives to the opinion of counsel. The opinion of counsel will not always be feasible to obtain.

HUD Response: The opinion of counsel as to irrevocability is an option, not a requirement. Please note that this final rule places this material at §§ 905.606(a)(6)(iii)(A) through (D).

Issue: HUD's regulation at § 905.604(h)(1) states that, to ensure the irrevocability of funds, that the PHA or the Owner Entity be "ready willing, and able" to attain milestones. Also, the conditions in the legal documents must be "commercially reasonable." These terms are vague and could lead to a finding of noncompliance if an auditor applies a different definition of commercial reasonableness.

HUD Response: This final rule, in § 905.606(a)(6)(iii)(A), revises this terminology to avoid ambiguity. The contractual conditions must be "generally consistent with similar affordable housing transactions," and the PHA or Owner Entity must know of no "impediments that would prevent the project from moving forward consistent with" the project milestones.

Issue: The requirement in proposed § 905.604(h)(3), that counsel has examined the availability of financing, seems to mean that counsel will examine the funding for the funding

source, which may be feasible in some cases, such as funds received from a city, but not in the case of bank or Assisted Housing Program (AHP) funds, because those entities will not reveal their funding sources.

HUD Response: This proposed section (now at § 905.606(a)(6)(iii)(D)) is revised in this final rule to clarify that it is the participating parties' financing that is examined.

Issue: In the case of operating-fund-only assistance under proposed § 905.604(k), one commenter stated that the provisions that require use restrictions to continue for a substantial and virtually indefinite period, whether or not there is operating subsidy to support them, are highly problematic for mixed-finance deals. The full flexibility permitted by 42 U.S.C. 1437g(l) should be utilized in order to give lenders and investors assurance that if sufficient subsidy ceases to be available, they will be promptly released from the obligation to house people who require such subsidy. In operating-fund-only projects, in such cases, section 8 assistance should be used to allow residents to remain if they wish.

HUD Response: This final rule implements the ability for HUD to reduce the use restriction period found in 42 U.S.C. 1437g(l) (see § 905.604(j)(2)(ii) and (iii)). If the use restrictions are terminated, the PHA must provide residents with a decent, safe, sanitary, and affordable unit to which they can relocate, which may include a public housing unit in another development or a Housing Choice voucher.

Issue: Proposed § 905.608, which covers the site acquisition proposal, only applies to acquisition with Capital Funds and should include acquisition with all available sources, including HOPE VI and other funds.

HUD Response: This final rule adds a definition of "public housing funds" to include not only Capital Funds, but also HOPE VI, Choice Neighborhoods, development funds, or any other funds appropriated by Congress for public housing development.

Issue: There is no justification in § 905.608(f) for stating that, absent HUD approval, the purchase price may not exceed the appraised value, because the federal interest in cost reasonableness is generally accomplished by TDC rules.

HUD Response: TDC is applicable to new development and acquisition of existing housing. The TDC operates as a constraint on excessive payments of public funds in the context of § 905.608 along with HUD's requirement for a PHA to provide an appraisal of the property.

Issue: Proposed § 905.612(b)(2) on mixed-finance drawdown ratios is unclear as to whether the requirement applies only to the final drawdown ratio or to interim ratios as well.

HUD Response: This final rule clarifies this paragraph to refer to the overall drawdown ratio.

Issue: While the rule requires that HUD funds be drawn down in the same ratio as other funding sources, projects are more economically feasible when interest-free HUD funds can be drawn first.

HUD Response: HUD's regulation at § 905.612(b)(2) clarifies that upon completion of the project, the ratio of public housing funds to non-public housing funds for the overall project must remain as reflected in the executed documents. The ratio does not apply to the construction period.

Issue: HUD's proposed regulation at § 905.604(b)(6) should be revised to acknowledge that Public Housing Requirements do not apply to non-mixed-finance development.

HUD Response: This section is clarified in the final rule. Public Housing Requirements apply to public housing-related work or mixed-finance development as meant in this subpart.

Issue: Proposed §§ 905.316, 905.318, and 905.320(b) and (c) appear to apply to both mixed-finance and conventional development, yet this is not clear from their language.

HUD Response: This final rule clarifies these sections.

Issue: HUD's proposed regulation at § 905.604(a) is unclear as to whether it applies only to the PHA, mixed-finance owner, or both.

HUD Response: This final rule revises this section. Final § 905.604(a)(1) explains the possible ownership structures under mixed-finance.

Issue: Rather than stating that mixed-finance contracts should "specify that they comply" with listed requirements, mixed-finance contracts should be required simply to contain no provisions inconsistent with the applicable regulations.

HUD Response: An affirmative statement of compliance provides a basis for HUD to take enforcement action if the statement is untrue, which is an assurance that HUD requires when committing public funds.

Issue: The rule should codify the authority to retain the original DOFA that existed prior to a mixed-finance transaction.

HUD Response: The rule codifies the current practice. In § 905.604(a)(4) of this final rule, the Department will retain the date of full availability

(DOFA) if a PHA is doing mixed-finance modernization.

Issue: The rule should be more specific as to the minimum information required by a PHA for the release funds for predevelopment assistance under proposed § 905.612(a)(3).

Response: HUD reviews each mixed-finance project separately, as the structure and financing of each project is unique. HUD has issued "Cost Control and Safe Harbor Standards for Rental Mixed-Finance Development," which contains provisions related to predevelopment expenses. Further, HUD has internal mechanisms for evaluating each mixed-finance project and issues that arise within the context of mixed-finance development. These mechanisms are the best way to manage mixed-finance projects, including the use of public housing funds for predevelopment purposes. Therefore, to date, there has been no need to issue generally applicable guidance on the use of public housing funds for predevelopment expenses related to mixed-finance development.

Issue: A commenter asked under what circumstance HUD would approve a PHA to exceed the 5 percent limit for predevelopment costs under § 905.612(a)(2).

HUD Response: As the rule states, this will be determined on a case by case basis. HUD declines to speculate about the circumstances under which this may occur.

Deviations Under Section 35(h) of the 1937 Act, 42 U.S.C. 1437z-7(h)

Issue: A commenter stated that additional flexibility for mixed-finance projects is considered helpful, for instance flexibility with rent and income eligibility requirements for projects with 20 percent or more nonpublic housing units. Another commenter stated that the threshold should be the lesser of 10 percent or 10 units. Another commenter stated that such flexibility should be granted for all public housing stock.

HUD Response: HUD's regulation at § 905.604(k) of this final rule provides flexibility where a PHA has a project in which a "significant number" of units are other than public housing units, following the statutory language under section 35(h) of the 1937 Act (42 U.S.C. 1437z-7(h)), which addresses mixed-finance development. The statute allows deviations under the specific statutory conditions stated, which do not apply to all public housing stock.

Issue: The standard for allowing "restructuring" is too limiting and "HUD should expand it to the extent interpretation permits, and should

generally recognize the ability of parties to make restructuring decision outside this standard where the standard need not be applied.” This commenter states that the phrase “reduction in appropriations” is meaningless without a recognized starting point, and suggests that the per-unit appropriations in 1998 would be a reasonable starting point for interpretation. In addition, any definition should recognize the likelihood of continuing inflation; a flat appropriation over 10 years would be the equivalent of a 50 percent effective reduction in funding at an inflation rate of 7 percent. This commenter states that HUD may interpret “reduction in appropriations” to be a reduction in the present value of the per-unit appropriation available. This commenter also states that HUD should recognize that many Regulatory and Operating (R&O) Agreements, for good reason, limit the operating-subsidy pass-through obligation of the PHA with reference to what the PHA is receiving from HUD. For instance, an R&O Agreement might provide for the PHA to pass through 90 percent of what it actually receives for that project. In literal terms, such a PHA is never prevented by a funding reduction from meeting its obligations, because its obligations automatically decrease, yet clearly a project receiving 50 percent of its intended subsidy would be in deep trouble and require deviation under section 35(h) of the 1937 Act. The commenter states that skilled drafters could provide alternate 35(h) triggers, such as a PHA failure to provide alternate non-operating subsidy funding in specified circumstances. This commenter states that “HUD needs to take care that it does not carelessly eliminate these triggers.” This commenter states that the rule eliminates these triggers by replacing the statutory phrase “from meeting its contractual obligations” with “from providing Operating Funds as provided in its contractual agreement.”

HUD Response: This final rule implements the statutory authority correctly, and the statute is unambiguous in referring to “a reduction in appropriations under section 1437g,” meaning an actual reduction in appropriations from Congress, not a change as a by-product of inflation. HUD recognizes that projects are structured differently. For this reason, this final rule removes the proposed section on “Allowable Deviations.” HUD encourages PHAs to draft R&O agreements that clearly address the issue of reduction in appropriation and clearly identify a

“starting point,” or baseline amount, from which a reduction in operating subsidy caused by a reduction in appropriation can be calculated. In addition, as requested by the commenter, to avoid unintended impacts, HUD has revised the language in the final rule concerning a public housing agency’s inability to meet its contractual obligations to mirror the phrasing in the statute.

Issue: HUD should propose to Congress legislation allowing deviations from Public Housing Requirements that do not rely on section 35 of the 1937 Act (42 U.S.C. 1437z–7).

HUD Response: HUD, through rulemaking, interprets and implements enacted legislation. The subject of proposing additional legislation is beyond the scope of this rulemaking process.

Issue: A commenter stated that the allowable deviations in the proposed rule are too limiting and unclear. For example, it is not clear if the “increased public housing rents” contemplated by proposed § 905.604(n)(2)(i) are different from those contemplated by proposed § 905.604(n)(2)(iii). More generally, HUD should not require a complicated sequencing of remedies; each situation will be different, and the paramount requirement for this rule is that it gives the PHA and owner the ability to design a restructuring plan appropriate to their circumstances.

Commenters objected to specific allowable deviations in the proposed rule. A commenter stated that limiting a rent increase under proposed § 905.604(n)(2)(iii) to the “amount strictly needed” is too inflexible. One commenter stated that the rule should not allow PHAs to eliminate eligibility restrictions altogether as contemplated in § 905.604(n)(2)(ii).

HUD Response: The allowable deviations are removed in this final rule in favor of a case-by-case approach, under which the Owner Entity will submit an Alternative Management Plan, which HUD will review.

Issue: HUD’s annual reevaluation and approval of the transformation plan under proposed § 905.604(n)(5) should provide that, once the annual update is properly submitted, the existing plan remains in effect pending HUD action.

HUD Response: The intent is for the existing plan to remain in effect until HUD disapproves it or approves a change. This final rule revises § 905.604(k)(4) accordingly.

Issue: One commenter stated that the tenant protections in § 905.604(n)(2)(iv) should be limited to 2 years; otherwise, if a PHA has limited resources to relocate tenants, it may be unwilling to

act and leave the mixed-finance owner without a remedy.

HUD Response: The proposed regulation at § 905.604(n)(2) is removed in this final rule. The regulation at § 905.604(k)(2)(ii)(C) addresses tenant protections and states that the responsibility for relocation is with the PHA or as included in the agreement between a PHA and the Owner Entity. The PHA should address this issue when negotiating its Regulatory and Operating Agreement with an Owner Entity.

Issue: The requirement in proposed § 905.604(n)(3)(iii)(D) that Public Housing Requirements be reinstated once the PHA restores operating subsidies to their normal level could be subject to misinterpretation, and deviations switch on and off from year to year.

HUD Response: HUD will consider providing additional guidance on the timing of reinstatement in the future, based on experience with this issue.

Issue: Proposed § 905.604(n)(3)(iv)(A) does not specify whether the reference to “reduced allocation of operating subsidy” refers to the subsidy provided by HUD or the subsidy passed through by the PHA.

HUD Response: The statute on which this section is based refers to reduced appropriations; what is meant is a reduction in appropriations resulting in a reduction of subsidy allocation. This final rule clarifies this point at § 905.604(k)(2)(iv)(B).

Issue: To ensure that project owners have pursued available alternative remedies prior to undertaking an Alternative Management Plan, the rule should require that project owners demonstrate that available development resources are being utilized to offset deficits with the public housing units.

HUD Response: Along with eliminating the allowed deviations and requiring the PHA to submit an Alternative Management Plan, this final rule includes such a provision as part of the supporting documentation that a PHA will submit with its an Alternative Management Plan (§ 905.604(k)(2)(iv)(D)).

Issue: One commenter states that proposed § 905.604(n)(3)(iv)(E), which requires prior expenditure of 50 percent of a named reserve, seems to contradict § 905.604(n)(2)(ii), which states that deviations from Public Housing Requirements are permitted only if the owner has expended all operating subsidy reserve funds put aside for this eventuality. A commenter states that this section should be eliminated, as requirements for operating reserves vary

greatly in mixed-finance projects, and may not be appropriate for this use.

HUD Response: This final rule, at § 905.604(k)(2)(iv)(D), removes an expenditure of reserve requirement and states more generally that the owner entity must use “all available means” to offset the reduction in appropriation or change in applicable law, including the use of other public and private development resources, the use of cash flow from any nonpublic housing units, funds from other operating deficit reserves, and so forth.

Issue: A commenter states that to ensure that project owners have pursued available alternative remedies prior to undertaking an Alternative Management Plan, the rule should require that project owners demonstrate that available development resources are being utilized to offset deficits with the public housing units.

HUD Response: This final rule at § 905.604(k)(2)(iv)(D) requires the PHA to provide documentation that the Owner Entity has used all available means to offset the impact of reduced operating subsidy.

Issue: Commenter states that HUD’s regulations implementing 35(h) of the 1937 Act (42 U.S.C. 1437z–7(h)) should take care to state that they do not affect, one way or the other, the ability of PHAs and their partners to restructure a project consistent with standard Public Housing Requirements.

HUD Response: That section only applies to deviations from statutory requirements under the conditions specified. It does not affect mixed-finance arrangements consistent with statute and regulation.

Issue: The word “solely” in proposed § 905.604(n)(3)(iv)(B)(“The deficit in operating revenues is attributable solely to the reduction in operating subsidy”), as such situations are likely to have multiple causes.

HUD Response: This final rule uses the term “primarily” instead of “solely” (§ 904.604(k)(2)(iv)(B)).

Issue: Deviations should be allowed for changes in law other than appropriations.

HUD Response: The statute allows for deviations in the case of a reduction in appropriations or other change in law that makes a PHA unable to fulfill its contractual obligations with respect to a specific number of public housing units. This final rule implements this statutory authority at § 905.604(k).

Issue: The reference to “contractual agreement” in § 905.604(n)(1) should be changed to “Regulatory and Operating Agreement (R&O),” which is more specific.

HUD Response: There may be instances where an agreement is not through an R&O.

Issue: A commenter states that implementation of “transformation remedies” (42 U.S.C. 1437z–7(h)) should be postponed until HUD has had broad discussions with stakeholders to ensure that appropriate protections remain in place for PHAs and residents. This commenter is particularly concerned about the potentially serious consequences of implementing a regulation that facilitates the loss of public housing units in the current political and economic environment.

HUD Response: HUD, at this time, cannot predict how many or which projects will require such deviations, and views that the greater risk is that, without an Alternative Management Plan under the statute and regulations, units will be permanently lost, where under transformation the deviation may be temporary. By removing in this final rule the proposed paragraph allowing deviations automatically under certain conditions, HUD will review each request and apply oversight to the process. HUD submits that this is the best choice under current conditions.

Issue: The proposed regulation at § 905.604(n) places the risk on PHAs regardless of the contractually agreed upon structure of a mixed-finance deal or the underlying business arrangement between a public housing authority and, for example, its private developer partner. The commenter states that one example is making the PHA responsible for tenant relocation, including moving costs (§ 905.604(n)(2)(iv)). This commenter states that in many mixed-finance transactions, investors require reserves to be sized, in part, to pay for relocation costs. Shifting responsibility to PHAs for such costs may not be part of existing deal structures and would result in a substantial realignment of risk in a mixed-finance transaction.

HUD Response: This final rule provides for required relocation according to the contractual agreement between the PHA and the Owner Entity (see § 905.604(k)(2)(ii)(C)).

Issue: The phrase “in HUD’s sole discretion” should be removed from proposed § 905.604(n)(4). The commenter states that this phrase removes the issue from judicial review.

HUD Response: While HUD does not agree with the commenter regarding judicial review, this final rule clarifies the review of an Alternative Management Plan, in § 905.604(k)(3), by providing examples of some, but not all, of the reasons why HUD might disapprove an Alternative Management Plan.

Energy Conservation Requirements

Issue: Many PHA commenters stated that HUD should not mandate energy conservation measures without giving PHAs the flexibility to determine their own priorities. The rule should make it clear that PHAs are not required to implement everything recommended in an energy audit, but that energy needs must be balanced against other PHA needs. Many of these PHAs supported energy conservation, generally.

One commenter stated that if energy audits and their corresponding recommended energy conservation measures are to be relied upon clearly, established and standardized measurement systems should be established so that uniformity of results is achieved. If measurement standards and recommendations vary from audit to audit, Capital Funds could be continuously wasted from year to year based on the new and/or conflicting recommendations.

One commenter stated that HUD and industry would benefit from more research and discussion on this topic.

Other commenters stated that not all energy audits produce savings or are reliable and there could be burdens on PHAs. Some commenters stated that they are skeptical of a cost-effectiveness approach to spend Capital Funds.

Other commenters suggested use of a 20-year, voluntary rolling base freeze on public housing utility consumption levels.

One commenter questioned the cost effectiveness of energy conservation measures (ECMs), and also stated that there could be situations where an audit may find an ECM not to be cost effective, when in fact it is an improvement that the PHA should implement as part of a modernization. This commenter stated that return on investment (ROI) should always be a factor in determining whether or not it makes sense to implement a recommendation. Another commenter stated that in addition to ROI, health and safety, conflicting modernization schedules, and the validity of energy audit results need to be considered.

One commenter stated that it should be determined whether using the funds for the energy conservation measures now would take away from future development needs or be premature.

One commenter stated that energy trade-offs need to be easy to plan and implement, not burdensome and complicated.

One commenter stated that in determining which energy conservation measures should be implemented, it is important whether the item is

something that would have been replaced anyway.

HUD Response: HUD is handling the energy audit process, ECMs, and ROI issues under a separate rulemaking (see the proposed rule of 76 FR 71287 *et seq.*). The 20-year rolling base freeze relates to the current Operating Fund rule at 24 CFR part 990 and is outside the scope of this rulemaking.

Issue: One commenter endorsed incorporating the International Energy Conservation Code (IECC) in various subsections of the proposed rule related to what types of projects are eligible for Capital Funds. The commenter suggested that HUD reference the 2009 IECC to promote energy efficiency over the life of those projects. One commenter stated that because the section specifies the required design and construction requirements for affected building projects, the International Building Code (IBC) and the IECC will also provide compliance with several other requirements listed in this section, including compliance with ASHRAE standard 90.1–2010, “Energy Standard for Buildings Except Low-Rise Residential Buildings,” an accepted alternative means of compliance with chapter 5 of the IECC.

HUD Response: This final rule references the 2009 edition of the IECC, in §§ 905.200 and 905.312, rather than the 2006 IECC, and references the ASHRAE standard.

Reductions in the Amount of Capital Funds for Management Improvements

Issue: Commenters expressed concern about limiting the amount of Capital Fund budget that can be used for management improvements to 10 percent. Although PHA’s on average only use 8 percent, the flexibility to go up to 20 percent is important and has a significant upside without a corresponding downside; for instance where PHAs need multiple infusions of capital for management improvement purposes at the same time, which may occur when a PHA becomes near-troubled or troubled. Also, such flexibility might be needed in an emergency. PHAs rarely use too much of their Capital Fund for management improvement, and HUD provides a solution to a problem that does not exist. Often there are statutory restrictions that prevent overly high usage, such as using 50 percent. HUD has not provided evidence that PHAs are mismanaging their Capital Fund for nonconstruction activities. It is counterintuitive that in a period of underfunding of PHAs, HUD would introduce a proposal that limits flexibility, authorized under statute, for

PHAs to administer their CFP to meet local needs.

PHAs need the flexibility to use limited funds to address the ever-growing capital improvements necessary to ensure continued assisted housing for low-income residents; therefore, the current rule should be kept as is.

A PHA may need additional assistance for training, consulting, information technology upgrades, or security services and, with the prospect of being forced to use reserves for operational expenses during the next fiscal year, the use of CFP for management improvements will be crucial. One PHA commenter cited the need to pay a resident coordinator.

Another commenter cited a possible need to upgrade computer systems and train users. Another commenter referenced “investments in technology,” community policing, and security measures. Another commenter cited the Americans with Disabilities Act (42 U.S.C. 12101 *et seq.*) compliance, the Violence Against Women Act (VAWA) (Pub. L. 109–162, approved January 5, 2006), and the Limited English Proficiency programs.

Another commenter cited the funding environment and projections of flat or declining funding. Another commenter cited resident training and service goals, and suggested a 15 percent limit as more reasonable.

HUD Response: In a limited funding environment, HUD has the obligation to ensure that PHAs expend their funds to maintain their properties in good physical condition. HUD agrees that resident training and service are important goals. Capital Funds may be used for capital expenditures (hard costs) to facilitate programs to improve the empowerment and economic self-sufficiency of public housing residents, as well as for resident-related management improvements. It is important to mention this not only with respect to capital and management improvement funding, but also that, generally, Section 3 of the Housing and Community Development Act of 1968 (12 U.S.C. 1701u) requires, to the greatest extent feasible, that PHAs make their best efforts to ensure that employment and other economic opportunities generated by certain of HUD’s Capital Fund- assisted activities are directed to low- and very-low-income persons, in accordance with 12 U.S.C. 1701u and HUD’s Section 3 regulations at 24 CFR part 135.³

³ While 12 U.S.C. 1701u uses “best efforts” with respect to the efforts required of PHAs, their contractors and subcontractors and uses “to the

Examples of such resident training and economic opportunities would be job training (e.g., painting and carpentry or computer skills and data entry) for residents and resident business development (e.g., painting contracting business or jobs in the PHA’s offices, related to management assistance) for the purposes of carrying out activities related to the Capital Fund management or physical improvements. In addition, HUD has taken the public comments into consideration and revises the Management Improvements Policy in this final rule in order to allow PHAs more time for making any necessary adjustments. This final rule reduces the standard allowable percentage for management improvements from up to 20 percent to up to 10 percent for all PHAs over a 5-year period, rather than the 3 years proposed.

It should be noted that while some items mentioned by commenters are eligible expenses under the Capital Fund Program (CFP)—such as compliance with section 504 of the Rehabilitation Act of 1973 (29 U.S.C. 701 *et seq.*), housing counseling for residents and prospective residents, and the design and construction of accessibility improvements—others such as staffing for security services, VAWA, and Limited English Proficiency, are not. Based on the responses to the proposed changes to the Management Improvements Policy, it has become evident that there is confusion over what items are eligible management improvement activities; therefore, eligible and ineligible activities under management improvements have been clarified at §§ 905.200(b)(7) and 905.202(h), respectively.

It should also be noted that the commenter misunderstands HUD’s policy to conserve scarce resources as a statement that PHAs are mismanaging their Capital Funds, which HUD has never contended. However, as a recent modernization study entitled “Capital Needs in the Public Housing Program (available at http://portal.hud.gov/hudportal/documents/huddoc?id=PH_Capital_Needs.pdf) has shown, there are huge outstanding modernization needs (over \$25 billion in 2010 dollars), and there has been insufficient regulation of the allocation of management funds.

greatest extent feasible” with respect to the efforts required of program assistance programs (e.g., housing and community development programs), HUD has determined that there is very little difference between these terms, and that the same level of effort is to be undertaken by HUD and all recipients and contractors regardless of the source of HUD financial assistance. That level of effort is “to the greatest extent feasible.” (See, 59 FR 33866, 33877, June 30, 1994).

One result has been that large amounts of management funds have been used to, for example, fund and operate security staff, which should be an operating expense. HUD's regulation in this area intends to ensure that in this difficult fiscal environment sufficient modernization funds are allocated for modernization needs.

Issue: The reduction of the amount for management improvements will cause an "undue financial burden to PHAs." Resident Opportunities and Self Sufficiency (ROSS), Community Supportive Services, and HOPE VI are not formula grants, and there is no guarantee a PHA would be successful in its grant application to receive such funding. Without the full 20 percent management improvement funding, PHAs that do not receive Public Housing Drug Elimination Program (PHDEP) funds might have to cancel security and drug elimination programs. While the current Capital Fund formula does allow for the potential use an additional 20 percent of appropriated Capital Funds to be used for operations, not all PHA's elect to or are eligible to utilize this funding mechanism. Reducing the management improvement amount by 50 percent would be penalizing those PHAs that are not utilizing this option.

Another commenter stated that the ROSS program has become politically disfavored, and that HOPE VI funding will be eliminated. The commenter was skeptical of HUD equating the 20-percent use of Capital Funds for operations with the 20 percent use of Capital Funds for management improvements, while housing authorities cannot use 20 percent of Capital Funds for management improvements as they can for operations. The commenter also stated that the proposed rule ignores that public housing programs are underfunded and housing authorities will not benefit from further restrictions on funding that limits how they operate.

HUD Response: The purpose of limiting the management improvement percentage is to help ensure that the PHAs spend appropriate amounts on the basic task of providing decent, safe, and sanitary housing. HUD is aware that this change may require a period of time of adjustment for PHAs. Therefore, HUD is phasing in the 10 percent cap over 5 years rather than the 3 years proposed.

HUD agrees that funding for operations does not necessarily equate to funding for management improvements, although there may be some overlap and all large PHAs (250 units or greater) are eligible under the statute to use up to 20 percent of their

annual Capital Fund grant for operations, as long as it is in the PHA Plan and the PHA does not have emergency conditions that need to be corrected immediately. However, generally, all PHAs are working under a limited funding environment under which they have a legal obligation to provide decent, safe, and sanitary housing. HUD believes that the course it has chosen—to limit the amount that can be taken from the Capital Fund and to provide flexibility for those PHAs that are clearly spending enough Capital Fund to maintain the physical condition of their property—is the best use of limited funding.

Issue: There should be a direct correlation of management improvements to improved program performance.

HUD Response: HUD believes as a general matter that the issue is not performance, but the proper allocation of limited Capital Funds. HUD believes that the bulk of those funds should go to capital needs, and that the vast majority of PHAs are not using and do not need to use, more than 10 percent for eligible management improvements.

Issue: Larger PHAs, in particular, may have higher management costs that require flexibility in their use of their grant, and so those PHAs with 250 or more units should be allowed to continue using 20 percent of the Capital Fund grant for management improvements.

HUD Response: The actual usage of management improvements indicates that most PHAs use 10 percent or less of their Capital Funds for eligible management improvements. However, because some PHAs do use more, HUD is allowing more time than proposed to phase in the cap. The 10 percent overall cap will be phased in over 5 years.

Issue: One commenter stated that the proposed rule should be modified to include specific accounting instructions for the way in which to properly assign the 10 percent to the Central Office Cost Center.

HUD Response: As an administrative rather than regulatory matter, HUD may address this issue in guidance, but not in this rulemaking.

Other Issues

Issue: Resident participation. While it is commendable for the rule to include resident participation costs as eligible costs under § 905.200(b)(8)(ii), it would be helpful for HUD to take some additional action on resident participation.

HUD Response: This final rule incorporates, at § 905.300(b)(3), the resident participation and resident

advisory board requirements formerly in 24 CFR part 903.

Issue: Tenants should be able to access technical assistance to help them understand either the budget or structural issues. The commenter states that there should be support for technical assistance through a capital operating account and that technical assistance should be offered on the regional and national level.

HUD Response: Funding for additional technical assistance (there is currently limited technical assistance for RAB training) is outside the scope of this rulemaking. This is an issue of appropriations.

Issue: Commenters are concerned about the dates of implementation in the proposed rule.

HUD Response: The implementation dates for the DDTF and the RHF transition can be found in § 905.400(j)–(k) and the implementation date for management improvements will be in accordance with the effective date of the rule. The rule only applies prospectively.

Issue: Adding the Public Housing Development Program to the list of programs eligible for the Capital Fund program may have a negative effect by spreading already scarce funds to more places as this program includes mixed-finance development. The commenter stated that mixed-income finance development may not have as high a degree of need as the low-income housing and that possible renovations could be more expensive in those buildings because they are for people of higher economic standing.

HUD Response: As to the fact that development is an eligible expense under the Capital Fund, this is statutorily required under section 9(d)(1) of the 1937 Act (42 U.S.C. 1437g(d)(1)). As to the potential for higher costs of renovations in mixed-finance housing, HUD is not aware of any evidence of these higher costs, and development of public housing via mixed-finance development is subject to the same limitations on TDC and Housing Construction Costs as non-mixed-finance development of public housing.

Issue: A commenter disagreed with language under proposed § 905.400(d)(3)(ii), which stated that units with a DOFA date of October 1, 1991, or after, shall be considered to have zero existing modernization need. The commenter stated that it is more cost effective to maintain a unit than it is to renovate it to address deferred maintenance and delayed capital improvements or to replace it. The commenter stated that buildings will

have capital needs in less than 20 years and need to accrue Capital Funds. Another commenter stated that the time frame for having existing modernization needs should be changed to 10 years.

HUD Response: This calculation was determined by the original negotiated rulemaking, and will not be revised in this rulemaking. However, HUD agrees that this is one of several components of the formula that should be reevaluated. Consequently, HUD is considering initiating another proposed rule to solely address the Capital Fund formula.

Issue: A commenter stated that there is a fundamental illogic in allocating 50 percent of Capital Funds to “existing modernization needs,” as defined, and 50 percent to “accrual needs,” as defined. Under the rule, a building constructed after 1991 would be deemed to have no modernization needs. The proportion of buildings in the public housing inventory that are more than 20 years old will decrease over time. Therefore, the inventory will be divided among an ever-smaller group of buildings, even as the post-1991 buildings age and become needier.

HUD Response: Similar to HUD’s response to the preceding comment, these allocations are part of the original negotiated rulemaking and will not be revised in this rulemaking, but, as already noted, HUD is considering initiating another proposed rule on the Capital Fund formula.

Issue: A commenter stated that the proposed guidelines for site and neighborhood standards are overly rigid and unnecessarily restrictive. HUD should revise these standards to allow for PHAs to provide on-site replacement housing sufficient to meet community needs, regardless of the number of units previously existing on the site. The commenter also stated that the proposed requirement that sites used for replacement housing be accessible to necessary services through public transportation would not work in rural areas and small communities, where public transportation is limited or nonexistent.

HUD Response: It is HUD’s responsibility to help ensure that some of the public housing that is demolished or disposed of is replaced, and to help ensure that there is sufficient public housing to serve the low-income community. As a result, PHAs, when submitting site acquisition or development proposals, are required to select sites that support this responsibility. HUD recognizes that each site selected for the construction or rehabilitation of public housing presents unique circumstances that reflect the neighborhood or community slated for

the construction or rehabilitation. Consequently, HUD will balance the need for housing and the overall impact of the rehabilitation of public housing on residents when reviewing these development proposals against the site and neighborhood criteria identified in § 905.602(d). This final rule revises § 905.602(d)(9) to reflect the commenter’s concern about lack of public transportation in rural areas.

Issue: A commenter stated that the standard in § 905.602(d)(5)(ii) should be revised to insert the phrase “public housing” to read:

. . . the number of public housing units being constructed is the minimum number needed to house current residents that want to remain at the site, so long as the number of [public housing] units is significantly fewer than the number being demolished . . .

HUD Response: HUD agrees with this clarification and this final rule makes the suggested revision.

Issue: It is unclear what is meant by § 905.306(b), “Items and costs.”

HUD Response: This term refers to items and costs listed in the PHA’s budget and Capital Fund 5-Year Action Plan. To be obligated, these items and costs must meet the definition of “obligation” found in § 905.108.

Issue: HUD should include in §§ 905.306 and 905.310 the authorization found in section 35(b)(1) of the 1937 Act, 42 U.S.C. 1437z-7(b)(1) for a PHA to deposit funds in an escrow account in order to collateralize construction financing, whether through a bond issue or otherwise. The commenter states that escrow is a crucial technique for obtaining 4 percent Low Income Housing Tax Credits (LIHTC), in particular. In addition, the regulation should state explicitly that deposit into the escrow account constitutes expenditure for all deadline purposes.

HUD Response: To put this authority into effect, the statutory language requires HUD to issue regulations. HUD will consider doing so in the future.

Issue: The § 905.304(a) requirement to record a Declaration of Trust on “all public housing property” is vague. The commenter suggests reference to a Declaration of Trust recorded against real property on which a public housing project is located.

HUD Response: The phrase “all public housing property” is an appropriate phrase that accurately covers both the PHA’s land and improvements, each of which must be subject to the Declaration of Trust.

Issue: HUD’s proposed regulation at § 905.304(a)(3) requires projects receiving operating fund assistance to

operate as public housing for the following 10 years, “except as permitted by HUD by an exception.” This rule should provide operating-fund-only projects with the maximum flexibility permitted by the 1937 Act to cease public housing operations if subsidies are reduced or suspended.

HUD Response: Each situation should be evaluated and determined by its own merits. A broad exception for an entire class of projects does not sufficiently protect the public interest.

Issue: The rule should remove references to Public Housing Development and Major Reconstruction of Obsolete Projects (MROP) funding, which program no longer exists.

HUD Response: PHAs still have unobligated balances in Public Housing Development and MROP grants, and so MROP cannot yet be removed from the rule.

Issue: The rule should be revised to provide that Moving to Work (MTW) agencies shall submit plans for expenditures of their Capital Funds pursuant to the terms of their MTW agreements, and any contrary requirements in the regulations will not apply to MTW PHAs.

HUD Response: HUD’s proposed regulation at § 905.300(b)(10) has been revised at this final rule to incorporate guidance on MTW agencies providing the Capital Fund submission information through the MTW plan.

Issue: PHA performance should be rewarded with respect to timely obligation and expenditure of funds.

HUD Response: Timely obligating and expending funds simply means that a PHA is meeting the statutory legal requirements of 42 U.S.C. 1437g(j). HUD does not agree that PHAs should be rewarded for meeting basic legal requirements.

Issue: Terminology should be updated to reflect changes in asset management and project-level accounting.

HUD Response: HUD believes this final rule uses the appropriate terminology.

Issue: One commenter asked for clarification of whether § 905.312(b), on inspections of work in progress and goods delivered, applies only to mixed-income developments.

HUD Response: The section applies to both mixed-finance and public housing development.

Issue: One commenter objected to the fact that § 905.700, “Other security interests,” may be read to require HUD approval of transactions that provide recourse to nonpublic housing property of a PHA.

HUD Response: HUD’s regulation at § 905.700 implements the statutory

language at section 30 of the 1937 Act, 42 U.S.C. 1437z–2, which states that HUD, upon such terms and conditions as it may prescribe, may authorize a PHA to “mortgage or otherwise grant a security interest in any public housing project or other property of the PHA.”

VI. Incorporation by Reference

42 U.S.C. 12709 requires HUD to adopt energy efficiency standards that meet or exceed the requirements of the 2006 International Energy Conservation Code (hereafter in this section referred to as “the 2006 IECC”), or, in the case of multifamily high-rises, the requirements of the American Society of Heating, Refrigerating, and Air-Conditioning Engineers Standard 90.1–2004. This statute also provides for the updating of those standards by adopting amended standards. Accordingly, the following updated standards are incorporated by reference in § 905.110 of this final rule with the approval of the Director of the Office of the Federal Register under 5 U.S.C. 552(a) and 1 CFR part 51:

- ASHRAE 90.1–2010, “Energy Standard for Buildings Except Low-Rise Residential Buildings.”
- The 2009 International Energy Conservation Code (IECC).

All approved material may be obtained from the organization that developed the standard. These standards also are available for inspection at HUD’s Office of Policy Development and Research, Affordable Housing Research and Technology Division, Department of Housing and Urban Development, telephone number 202–708–4370 (this is not a toll-free number). In addition, the standards are available for inspection at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, call 202–741–6030 or go to http://www.archives.gov/federal_register/code_of_federal_regulations/ibr_locations.html.

Other resources are:

- ASHRAE 90.1–2010, “Energy Standard for Buildings Except Low-Rise Residential Buildings,” by the American Society of Heating, Refrigerating, and Air-Conditioning Engineers, Inc., 1791 Tulle Circle NE., Atlanta, GA 30329 (<http://www.ashrae.org/standards-research-technology/standards-guidelines>), and

- The 2009 International Energy Conservation Code (IECC) by the International Code Council, 500 New Jersey Avenue NW., 6th Floor, Washington, DC 20001 (1–888–422–7233) (<http://www.iccsafe.org/Store>).

The incorporated standards are found in this final rule at §§ 905.200(b)(6)(ii) and 905.312(b)(1).

VII. Findings and Certifications

Regulatory Review—Executive Orders 12866 and 13563

Under Executive Order 12866 (Regulatory Planning and Review), a determination must be made whether a regulatory action is significant and, therefore, subject to review by the Office of Management and Budget (OMB) in accordance with the requirements of the order. Executive Order 13563 (Improving Regulations and Regulatory Review) directs executive agencies to analyze regulations that are “outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned. Executive Order 13563 also directs that, where relevant, feasible, and consistent with regulatory objectives, and to the extent permitted by law, agencies are to identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public. This rule was determined to be a “significant regulatory action” as defined in section 3(f) of Executive Order 12866 (although not an economically significant regulatory action, as provided under section 3(f)(1) of the Executive Order).

With respect to Executive Order 12866, it is determined that this final rule would not have any impact on the level of funding for the CFP—which level is determined by annual congressional appropriations—but would potentially create some financial transfers among program participants. The total amount of transfers is estimated to be less than \$100 million annually, with most of the transfers being interagency transfers attributable to the Demolition or Disposition Transitional Funding (DDTF). However, the benefits of the rule such as regulatory consolidation, program clarification, removal of obsolete references, and enhanced efficiencies, justify the rule regardless of the transfers of funding involved.

A summary of the changes made to the proposed rule at the final rule stage can be found in the preamble of the final rule. These changes can be aggregated in two groups:

1. Revision of Definitions and Other Clarifications

The final rule accommodates changes to definitions and provides other clarifications in response to public comments on the proposed rule, and

further consideration of the issues by HUD. These actions bring much needed clarity to the Capital Fund Program.

For example, the proposed definition of “Capital Fund Annual Contributions Contract (CF ACC)” appeared to conflate the definition of the entire ACC (which is a contract addressing the operation of public housing) with that of a Capital Funds amendment (presumably limited to the special terms applicable to the provision of Capital Funds). To avoid possible ambiguity, this final rule modifies the proposed definition of CF ACC to more clearly indicate that this is an amendment to the Consolidated Annual Contributions Contract.

2. Program Requirements

A. Management Improvement

The proposed rule called for the gradual phase down of the management improvements funding limit from up to 20 percent to up to 10 percent over a period of 3 fiscal years. This final rule extends the phase-in over a 5-year time period. Following the phase down all PHAs would be limited to using up to 10 percent for management improvements. The 20 percent standard was implemented by regulation; it is not a statutory limitation.

HUD has determined, using 2008 data, that approximately 440 of the 3129 PHAs expended in excess of 10 percent of their Capital Funds for management improvements, corresponding to a total of \$28.4 million. That sum represents an approximation of the amount of funding currently allocated to management improvements that effectively would be transferred to other eligible Capital Funds activities.

HUD notes, however, that collectively and on average, PHAs expend well below the 10 percent threshold. Still using the 2008 data, \$2.14 billion was distributed by formula to PHAs under the Capital Fund Program. Of that amount, only \$99,693,783, or about 4.65 percent, was expended by PHAs for management improvements. Overall, the average amount expended by PHAs for management improvements was 8.1 percent.

These results suggest that the potential transfer of \$28.4 million would be observed at the level of each individual PHA. Collectively, and for the program as a whole, there would not be any transfers since PHAs, on an average, budget less than 10 percent for management improvements.

In reviewing the impact of HUD’s 10 percent cap on management improvements, it is important to note that the cap does not imply a cost to the PHAs or a reduction in funding. With

the limit, PHAs with a management improvements budget over 10 percent of their annual Capital Fund allocation will simply have to realign their budget over a 5 year period and transfer the excess to other eligible capital fund activities within the PHA.

There is also no cost to be borne by PHAs and there is no reduction of the annual Capital Fund allocation to the PHA when the limit becomes effective. Further, there should be no disruption of activities already planned and included in the PHA plan. In this regard, it should be noted that Capital Fund expenditures are guided by the PHA's 5-year plan and annual statement, which describe the work to be carried out in the budget year. The fact that this final rule calls for a phase-down over 5 years mitigates any adverse programmatic impact to the PHA and allows work items already budgeted to be funded using management improvements funds to be completed, if the PHA so desires.

The restriction established by this rule is that no new work items in excess of 10 percent of the PHA's annual Capital Fund allocation would be approved using management improvements funds. The limitation and the priority change will leave a larger percentage of the PHA's annual Capital Fund grant available to be used for physical improvements, and will cause a transfer from and to an economic agent outside of the PHAs. Traditionally, PHAs spend management improvement funds on management information systems equipment, resident initiatives, etc. Stakeholders in these lines of business may see a reduction of activities from PHAs that routinely budget more than 10 percent to management improvements, as a result of the 10 percent limit.

Nevertheless, the potential benefit for capping the management improvements budget to 10 percent, down from 20 percent is to target the bulk of the capital funds to other capital fund—eligible activities, such as physical improvements. Recent studies, such as the Capital Needs Assessment, have stressed an urgent need for additional funding for physical improvements.

B. Capital Fund Formula

This proposed rule proposes the phase-down of the Replacement Housing Factor (RHF) from a 10-year long RHF program to a 5-year RHF program for PHAs that remove units from the inventory based on demolition or disposition.

The final rule establishes 5 years of a DDTF grant that will be included in the regular Capital Fund formula grant. The

modification would alter the distribution of funds amongst program participants and thus create some inter-agency transfers. It should be noted that the main difference at this stage is on the way funds are distributed to eligible PHAs and the eligible use of funds. The DDTF grant will not be subject to the same requirements as the RHF grant, and it will allow PHAs to fund modernization as well as development, and fund any eligible activity under the Capital Fund Program. The need for more modernization is quantified in a study released in June 2011 on modernization needs, "Capital Needs in the Public Housing Program," prepared by Abt Associates, available at http://portal.hud.gov/hudportal/documents/huddoc?id=PH_Capital_Needs.pdf. The study found that the Nation's 1.2 million public housing units have an estimated total of \$25.6 billion in existing capital needs.

This final rule will also have significant benefits. This rule updates and consolidates the Capital Fund Program regulations and related regulations having to do with the use of Capital Funds for development and modernization, as well as regulations for continuing operation of low-income housing after completion of debt service. In addition, the rule codifies recent statutory requirements enacted in HERA. The benefits of the rule, such as regulatory consolidation, program clarification, removal of obsolete references, and enhanced efficiencies, make the rule necessary. Although HUD established the Capital Fund formula in 2000, HUD has continued to rely on Capital Fund Program requirements to the extent that these requirements were not superseded by statutory requirements.

The update in energy standards is made on the basis of a review of analysis prepared pursuant to the Energy Independence and Security Act (Pub. L. 110–140, approved December 19, 2007) showing that the average simple payback is 3.45 years for the energy savings resulting from implementing IECC 2009 to equal the incremental cost of the improvements.⁴ This payback period is significantly less than the useful life of affected components and as a result the benefits of compliance with IECC 2009 outweigh the costs. It is noted that regardless of HUD's determination, 37 states have adopted IECC 2009 or IECC 2012, making the current HUD IECC 2006

⁴ Zachary Pachette, John Miller, Mike DeWein, *Incremental Construction Cost Analysis for New Homes*, Building Code Assistance Project, Updated June 2011. (Retrieved from: <http://bcap-ocean.org/incremental-cost-analysis>).

standard moot in those states in addition to others, such as California, that enforce a stricter state standard than IECC. Generally, the IECC establishes baseline expectations for energy efficiency that consumers can rely upon as a matter of public policy. Without the requirement of the IECC to implement baseline energy conservation measures, real estate owners in both the public and private sectors generally would not implement energy conservation solely on the basis of energy savings. This is because the incentive for such measures in the form of cost savings often does not accrue to the entity implementing the energy conservation measure, creating a misplaced incentive. If there are market failures or barriers that are not reflected in the return of the investment, then the market penetration of energy-efficient investment will be less than optimal. Consistent with the search cost approach to imperfect information, landlords have a reduced incentive to provide energy-efficient appliances to their tenants.⁵

It is determined that this final rule is not economically significant. This final rule accommodates changes made to the proposed rule in response to public comments and other consideration of issues by HUD. Like the proposed rule, this final has the potential to generate some transfers caused by the modification of the formula grant to accommodate the introduction of the DDTF. Notwithstanding, the rule will yield some substantial benefits such as regulatory consolidation, program clarification, and removal of obsolete references.

With respect to Executive Order 13563, the preamble has demonstrated that, in response to public comment, and following further consideration of the issues by HUD, components of the Capital Fund regulations have been made more flexible and less burdensome.

The docket file is available for public inspection in the Regulations Division, Office of the General Counsel, Room 10276, 451 7th Street SW., Washington, DC 20410–0500. Due to security measures at the HUD Headquarters building, please schedule an appointment to review the docket file by calling the Regulations Division at 202–708–3055 (this is not a toll-free

⁵ Allcott, Hunt and Michael Greenstone, 2012, "Is there an Energy-Efficiency Gap?" National Bureau of Economic Research, Working Paper 17766; Gillingham, Kenneth, Matthew Harding, and David Rapson. 2012. "Split Incentives and Household Energy Consumption." *Energy Journal* 33 (2): 37–62.

number). Individuals with speech or hearing impairments may access this number via TTY by calling the Federal Relay Service, toll-free at 800-877-8339.

Paperwork Reduction Act

The information collection requirements contained in this final rule have been submitted for review and approval by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). The information collection requirements for the Capital Fund program are assigned OMB control numbers 2577-0157, 2577-0226, 2577-0265, and 2577-0275. The information collection requirements in this final rule include largely pre-existing information collection requirements. However, the

information collection requirements of some preexisting forms are being revised to reduce the paperwork burden. Specifically, the information collection requirements in this rule reflect a decrease of 32,222 burden hours from the preexisting forms. This decrease reflects statutory changes enacted by sections 2701 and 2702 of the Small PHA Paperwork Reduction Act, title VII of the Housing and Economic Recovery Act of 2008 (HERA) (Pub. L. 110-289, approved July 30, 2008). Specifically, HERA exempts qualified PHAs from the requirement of section 5A of the U.S. Housing Act of 1937 (42 U.S.C. 1437 *et seq.*) to prepare and submit an Annual PHA Plan. Qualified PHAs under HERA are defined as those PHAs with less than 550 public housing units and

Housing Choice Vouchers (HCV) combined that are not in troubled performance status. This provision significantly reduces the paperwork burdens and associated costs for qualified PHAs, which represent approximately 68 percent of the PHAs that administer public housing programs. Under HERA, qualified PHAs are exempt from preparing and submitting a PHA Annual Plan and are only required to submit the 5-Year PHA Plan once every 5 years. The sections in this rule that contain the current information collection requirements and the upcoming revisions that are awaiting OMB approval, as well as the estimated adjusted burden of the pending revisions, are set forth in the following table.

CFR Section (related forms referenced)	Number of respondents	Total annual responses	Average hours per response	Total annual burden hours
§ 905.604(k), Transition Plan, OMB Control No. 2577-0275	920	920	18.46	16,980
§ 905.300(b)(8) Annual Statement/Performance and Evaluation Report, HUD form 50075.1, OMB Control No. 2577-0265, current	3,163	3,163	8	25,304
§ 905.300(b)(8) Annual Statement/Performance and Evaluation Report, HUD form 50075.1, OMB Control No. 2577-0265, pending approval	1,551	1,551	4.18	6,488
§ 905.300(b)(1) Capital Fund 5-Year Action Plan, HUD form 50075.2, OMB Control No. 2577-0226, current	3,163	3,163	3.00	9,489
§ 905.300(b)(1) Capital Fund 5-Year Action Plan, HUD form 50075.2, OMB Control No. 2577-0226, pending approval	1,551	1,551	2.09	3,244
§ 903.3 PHA 5-Year and Annual Plan, HUD form 50075, OMB Control No. 2577-0226, current	4,139	4,139	4.28	17,719
§ 903.3 PHA 5-Year and Annual Plan, HUD form 50075, OMB Control No. 2577-0226, pending approval	4,053	4,053	2.6	10,558
<i>Total current burden hours</i>	52,512
<i>Total burden hours once pending forms are approved</i>	20,290

All estimates include the time for reviewing instructions, searching existing data sources, gathering or maintaining the needed data, and reviewing the information.

The docket file is available for public inspection. For information or a copy of the paperwork package submitted to OMB, contact: Colette Pollard at 202-708-0306 (this is not a toll free number) or via email at Colette.Pollard@hud.gov. In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531-1538) (UMRA) establishes requirements for federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and the private sector. This rule does not

impose any federal mandate on any state, local, or tribal government or the private sector within the meaning of UMRA.

Environmental Impact

A Finding of No Significant Impact with respect to the environment has been made at the proposed rule stage in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)), and remains applicable to this final rule. The Finding of No Significant Impact is available for public inspection between the hours of 8 a.m. and 5 p.m., weekdays, in the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street SW., Room 10276, Washington, DC 20410-0500. Due to security measures at the HUD Headquarters building, an advance appointment to review the docket file must be scheduled by calling the

Regulations Division at 202-708-3055 (this is not a toll-free number). Hearing- or speech-impaired individuals may access this number through TTY by calling the Federal Relay Service, at toll-free 800-877-8339.

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) (5 U.S.C. 601 *et seq.*) generally requires an agency to conduct a regulatory flexibility analysis of any rule subject to notice and comment rulemaking requirements, unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. This rule reflects the transition from PHA-wide accounting to an asset management model, and therefore changes some of the language regarding the Capital Fund formula to reflect the new accounting model. The only significant change in the Capital Fund formula calculation is a proposal to limit the number of years a PHA is eligible to receive RHF grants

to replace units removed from the inventory by demolition, disposition, or homeownership from 10 years to 5 years. The Capital Fund formula amount that is freed up because of fewer RHF grants will cause an increase in the amount of Capital Funds available to the remainder of the PHAs, which includes a large number of small PHAs. Since most small PHAs do not demolish or dispose of a significant number of public housing units, reducing RHF eligibility to 5 years should benefit small PHAs. Therefore, the undersigned certifies that this rule will not have a significant economic impact on a substantial number of small entities, and an initial regulatory flexibility analysis is not required.

Executive Order 13132, Federalism

Executive Order 13132 (entitled "Federalism") prohibits, to the extent practicable and permitted by law, an agency from promulgating a regulation that has federalism implications and either imposes substantial direct compliance costs on state and local governments and is not required by statute or preempts state law, unless the relevant requirements of section 6 of the Executive Order are met. This rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Catalog of Federal Domestic Assistance Number

The Catalog of Federal Domestic Assistance numbers for 24 CFR parts 905, 941, 968, and 969 are 14.850, 14.872, 14.882, 14.883.

List of Subjects

24 CFR Part 903

Administrative practice and procedure, Public housing, Reporting and recordkeeping requirements.

24 CFR Part 905

Grant programs—housing and community development, Incorporation by reference, Public housing, Reporting and recordkeeping requirements.

24 CFR Part 941

Grant programs—housing and community development, Loan programs—housing and community development, Public housing.

24 CFR Part 968

Grant programs—housing and community development, Loan programs—housing and community

development, Public housing, Reporting and recordkeeping requirements.

24 CFR Part 969

Grant programs—housing and community development, Low and moderate income housing, and Public housing.

Accordingly, for the reasons stated in the preamble, under the authority of 42 U.S.C. 3535(d), HUD amends 24 CFR chapter IX as follows:

PART 903—PUBLIC HOUSING AGENCY PLANS

■ 1. The authority citation for part 903 is revised to read as follows:

Authority: 42 U.S.C. 1437c; 42 U.S.C. 1437c-1; Pub. L. 110-289; 42 U.S.C. 3535d.

■ 2. Revise § 903.3 to read as follows:

§ 903.3 What is the purpose of this subpart?

(a) This subpart specifies the requirements for PHA plans, required by section 5A of the United States Housing Act of 1937 (42 U.S.C. 1437c-1) (the Act), as amended.

(b) The purpose of the plans is to provide a strategic planning framework for PHA management operations and capital planning:

- (1) Local accountability; and
- (2) An easily identifiable source by which public housing residents, participants in the tenant-based assistance program, and other members of the public may locate basic PHA policies, rules and requirements concerning the PHA's operations, programs and services.

(c) Title VII of the Housing and Economic Reform Act, Public Law 110-289, section 2702, amends 42 U.S.C. 1437c-1(b) to provide qualified PHAs an exemption from the requirement of section 5A of the Act to submit an annual PHA Plan. The term "qualified PHA" means a public housing agency that meets the following requirements:

- (1) The sum of the number of public housing dwelling units administered by the agency, and the number of vouchers under section 8(o) of the United States Housing Act of 1937 (42 U.S.C. 1437f(o)) administered by the agency, is 550 or fewer; and

(2) The agency is not designated under section 42 U.S.C. 1437d(j)(2) as a troubled public housing agency, and does not have a failing score under SEMAP during the prior 12 months.

PART 905—THE PUBLIC HOUSING CAPITAL FUND PROGRAM

■ 3. The authority citation for part 905 is revised to read as follows:

Authority: 42 U.S.C. 1437g, 42 U.S.C. 1437z-2, 42 U.S.C. 1437z-7, and 3535(d).

■ 4. Revise subpart A to read as follows:

Subpart A—General

Sec.

- 905.100 Purpose, general description, and other requirements.
905.102 Applicability.
905.104 HUD approvals.
905.106 Compliance.
905.108 Definitions.
905.110 Incorporation by reference.

Subpart A—General

§ 905.100 Purpose, general description, and other requirements.

(a) *Purpose.* The Public Housing Capital Fund Program (Capital Fund Program or CFP) provides financial assistance to public housing agencies (PHAs) and resident management corporations (RMC) (pursuant to 24 CFR 964.225) to make improvements to existing public housing. The CFP also provides financial assistance to develop public housing, including mixed-finance developments that contain public housing units.

(b) *General description.* Congress appropriates amounts for the Capital Fund in HUD's annual appropriations. In order to receive a Capital Fund grant, the PHA must:

(1) Validate project-level information in HUD's data systems, as prescribed by HUD;

(2) Have an approved CFP 5-Year Action Plan;

(3) Enter into a Capital Fund Annual Contributions Contract (CF ACC) Amendment to the PHA's Annual Contributions Contract (as defined in 24 CFR 5.403) with HUD; and

(4) Provide a written certification and counsel's opinion that all property receiving Capital Fund assistance is under a currently effective Declaration of Trust (DOT) and is in compliance with the CF ACC and the Act.

(c) *Informational requirements.* Section 905.300 of this part describes the information to be submitted to HUD for the CFP. HUD uses the CF formula set forth in § 905.400 of this part, along with data provided by the PHA and other information, including, but not limited to, the high-performance information from the Real Estate Assessment Center (REAC) and location cost indices, to determine each PHA's annual grant amount. HUD notifies each PHA of the amount of the grant and provides a CF ACC Amendment that must be signed by the PHA and executed by HUD in order for the PHA to access the grant. After HUD executes the CF ACC Amendment, the PHA may draw down funds for eligible costs that

have been described in its CFP Annual Statement/Performance and Evaluation Report or CFP 5-Year Action Plan.

(d) *Eligible activities.* Eligible Capital Fund costs and activities as further described in subpart B of this part include, but are not limited to, making physical improvements to the public housing stock and developing public housing units to be added to the existing inventory. With HUD approval, a PHA may also leverage its public housing inventory by borrowing additional capital on the private market and pledging a portion of its annual Capital Funds for debt service, in accordance with § 905.500 of this part.

(e) *Obligation and expenditure requirements.* A PHA must obligate and expend its Capital Funds in accordance with § 905.306 of this part. The PHA will directly employ labor, either temporarily or permanently, to perform work (force account) or contract for the required work in accordance with 24 CFR part 85. Upon completion of the work, the PHA must submit an Actual Modernization Cost Certificate (AMCC) or Actual Development Cost Certificate (ADCC) and a final Performance and Evaluation Report (in accordance with § 905.322 of this part) to HUD to close out each Capital Fund grant.

(f) *Financing and development.* Section 905.500 of this part regulates financing activities using Capital Funds and Operating Funds. Section 905.600 of this part contains the development requirements, including those related to mixed-finance development, formerly found in 24 CFR part 941. Section 905.700 of this part describes the criteria for the use of Capital Funds for other security interests. Section 905.800 of this part addresses PHA compliance with Capital Fund requirements and HUD capability for review and sanction for noncompliance.

§ 905.102 Applicability.

All PHAs that have public housing units under an Annual Contributions Contract (ACC), as described in 24 CFR 5.403, are eligible to receive Capital Funds.

§ 905.104 HUD approvals.

All HUD approvals required in this part must be in writing and from an official designated to grant such approval.

§ 905.106 Compliance.

PHAs or owner/management entities or their partners are required to comply with all applicable provisions of this part. Execution of the CF ACC Amendment, submissions required by this part, and disbursement of Capital

Fund grants from HUD are individually and collectively deemed to be the PHA's certification that it is in compliance with the provisions of this part and all other Public Housing Program Requirements. Noncompliance with any provision of this part or other applicable requirements may subject the PHA and/or its partners to sanctions contained in § 905.804 of this part.

§ 905.108 Definitions.

The following definitions apply to this part:

1937 Act. The term "1937 Act" is defined in 24 CFR 5.100.

Accessible. As defined in 24 CFR 8.3.

ACC. The Annual Contributions Contract between HUD and a PHA covering a public housing project or multiple public housing projects.

ACC Amendment. An Amendment to the ACC to reflect specific changes made to a PHA's public housing inventory or funding. An ACC Amendment may be a Capital Fund ACC Amendment, a Mixed-Finance ACC Amendment, a Capital Fund Financing ACC Amendment, or other form of amendment specified by HUD.

Additional Project Costs. The sum of the following HUD-approved costs related to the development of a public housing project, which are not included in the calculation of the Total Development Cost (TDC) limit, but are included in the maximum project cost as stated in § 905.314(b). Additional project costs include the following:

(1) Costs for the demolition or remediation of environmental hazards associated with public housing units that will not be rebuilt on the original site; and

(2) Extraordinary site costs that have been verified by an independent state-registered, licensed engineer (e.g., removal of underground utility systems; replacement of off-site underground utility systems; extensive rock and/or soil removal and replacement; and amelioration of unusual site conditions, such as unusual slopes, terraces, water catchments, lakes, etc.); and

(3) Cost effective energy-efficiency measures in excess of standard building codes.

Capital Fund (CF). The fund established under section 9(d) of the 1937 Act (42 U.S.C.) 1437g(d).

Capital Fund Annual Contributions Contract Amendment (CF ACC). An amendment to the Annual Contributions Contract (ACC) under the 1937 Act between HUD and the PHA containing the terms and conditions under which the Department assists the PHA in providing decent, safe, and sanitary housing for low-income families. The

CF ACC must be in a form prescribed by HUD, under which HUD agrees to provide assistance in the development, modernization, and/or operation of a low-income housing project under the 1937 Act and the PHA agrees to modernize and operate the project in compliance with all Public Housing Requirements.

Capital Fund Program Fee. A fee that may be charged to a Capital Fund grant by the PHA to cover costs associated with oversight and management of the CFP by the PHA Central Office Cost Center (COCC). These costs include duties related to general capital planning, preparation of the Annual Plan, processing of the Line of Credit Control System (LOCCS), preparation of reports, drawing of funds, budgeting, accounting, and procurement of construction and other miscellaneous contracts. The CFP fee is the administrative cost for managing a Capital Fund grant for a PHA subject to asset management.

Community Renewal Costs. Community Renewal Costs consist of the sum of the following HUD-approved costs related to the development of a public housing project: planning (including proposal preparation); administration; site acquisition; relocation; demolition of—and site remediation of environmental hazards associated with—public housing units that will be replaced on the project site; interest and carrying charges; off-site facilities; community buildings and nondwelling facilities; contingency allowance; insurance premiums; any initial operating deficit; on-site streets; on-site utilities; and other costs necessary to develop the project that are not covered under the Housing Construction Cost (HCC). Public housing capital assistance may be used to pay for Community Renewal Costs in an amount equivalent to the difference between the HCC paid for with public housing capital assistance and the TDC limit.

Cooperation agreement. An agreement, in a form prescribed by HUD, between a PHA and the applicable local governing body or bodies that assures exemption from real and personal property taxes, provides for local support and services for the development and operation of public housing, and provides for PHA payments in lieu of taxes (PILOT).

Date of Full Availability (DOFA). The last day of the month in which substantially all (95 percent or more) of the units in a public housing project are available for occupancy.

Declaration of Restrictive Covenant. The Declaration of Restrictive Covenant

is a legal instrument that binds the PHA and the Owner Entity to develop mixed-finance projects in compliance with Public Housing Requirements and restricts disposition of the property, including transferring, conveying, assigning, leasing, mortgaging, pledging or otherwise encumbering the property.

Declaration of Trust (DOT). A legal instrument that grants HUD an interest in public housing property. It provides public notice that the property must be operated in accordance with all public housing federal requirements, including the requirement not to convey or otherwise encumber the property unless expressly authorized by federal law and/or HUD.

Development. Any or all undertakings necessary for planning, land acquisition, demolition, construction, or equipment in connection with a public housing project.

Emergency work. Capital Fund related physical work items that if not done pose an immediate threat to the health or safety of residents, and which must be completed within one year of funding. Management Improvements are not eligible as emergency work and therefore must be covered by the CFP 5-Year Action Plan before the PHA may carry them out.

Energy audit. A systematic review of the energy requirements and consumption for property with the intent to identify potential opportunities for energy and water savings through improved operational efficiency or more efficient components.

Expenditure. Capital Funds disbursed by the PHA to pay for obligations incurred in connection with work included in a CFP 5-Year Action Plan that has been approved by the PHA Board of Commissioners and HUD. Total funds expended means cash actually disbursed and does not include retainage.

Federal Fiscal Year (FFY). The Federal Fiscal Year begins each year on October 1 and ends on September 30 of the following year.

Force account labor. Labor employed directly by the PHA on either a permanent or a temporary basis.

Fungibility. As it relates to the Capital Fund Program, fungibility allows the PHA to substitute work items between any of the years within the latest approved CFP 5-Year Action Plan, without prior HUD approval.

HCC. The sum of the following HUD-approved costs related to the development of a public housing project: dwelling unit hard costs (including construction and equipment), builder's overhead and profit, the cost of extending utilities from the street to the

public housing project, finish landscaping, and the payment of Davis-Bacon wage rates.

Line of Credit Control System (LOCCS). LOCCS is a HUD grant disbursement system. LOCCS currently provides disbursement controls for over 100 HUD grant programs. LOCCS-Web is an intranet version of LOCCS for HUD personnel. eLOCCS is the Internet link to LOCCS data for HUD business partners.

Mixed-finance modernization. Use of the mixed-finance method of development to modernize public housing projects described in § 905.604.

Modernization. Modernization means the activities and items listed in § 905.200(b)(4–18).

Natural disaster. An extraordinary event, such as an earthquake, flood, or hurricane, affecting only one or few PHAs, but excluding presidentially declared emergencies and major disasters under the Robert T. Stafford Disaster Relief and Emergency Assistance Act (42 U.S.C. 5121 *et seq.*).

Obligation. A binding agreement for work or financing that will result in outlays, immediately or in the future. All obligations must be incorporated within the CFP 5-Year Action Plan that has been approved by the PHA Board of Commissioners and HUD. This includes funds obligated by the PHA for work to be performed by contract labor (i.e., contract award), or by force account labor (i.e., work actually started by PHA employees). Capital Funds identified in the PHA's CFP 5-Year Action Plan to be transferred to operations are obligated by the PHA once the funds have been budgeted and drawn down by the PHA. Once these funds are drawn down they are subject to the requirements of 24 CFR part 990.

Open grant. Any grant for which a cost certificate has not been submitted and which has not reached fiscal closeout as described in § 905.322 of this part.

Operating fund. Assistance provided under 24 CFR part 990 pursuant to section 9(e) of the 1937 Act (42 U.S.C. 1437g(e)) for the purpose of operation and management of public housing.

Owner entity. An entity that owns public housing units. In mixed-finance development, the Owner Entity may be the PHA, or may be an entity in which the PHA owns a partial interest, or may be an entity in which the PHA has no ownership interest. The Owner Entity is subject to the applicable requirements of this subpart.

Partner. A third-party entity with which the PHA has entered into a partnership or other contractual arrangement to provide for the mixed-

finance development of public housing units pursuant to this subpart. The partner has primary responsibility with the PHA for the development and/or operation of the public housing units and is subject to the applicable requirements of subpart F of this part.

Physical Needs Assessment (PNA). A systematic review of all the major physical components of property to result in a long-term schedule for replacement of each component and estimated capital costs required to meet the replacement need.

PIH Information Center (PIC). PIH's current system for recording data concerning: the public housing inventory, the characteristics of public housing and Housing Choice Voucher—assisted families, the characteristics of PHAs, and performance measurement of PHAs receiving Housing Choice Voucher funding.

Public Housing Agency (PHA). Any state, county, municipality, or other governmental entity or public body or agency or instrumentality of these entities that is authorized to engage or assist in the development or operation of public housing under this part.

Public Housing Assessment System (PHAS). The assessment system under 24 CFR part 902 for measuring the properties and PHA management performance in essential housing operations, including rewards for high performers and consequences for poor performers.

Public housing capital assistance. Assistance provided by HUD under the Act in connection with the development of public housing under this part, including Capital Fund assistance provided under section 9(d) of the Act, public housing development assistance provided under section 5 of the Act, Operating Fund assistance used for capital purposes under section 9(g)(2) or 9(e)(1)(I) (with HUD's approval of such financing of rehabilitation and development of public housing units) of the Act, and HOPE VI grant assistance.

Public housing funds. Any funds provided through the Capital Fund or Other Public Housing Development Sources, such as HOPE VI, Choice Neighborhoods, Development Funds, disposition proceeds that a PHA may realize under section 18 of the 1937 Act (42 U.S.C. 1437p), or any other funds appropriated by Congress for public housing.

Public housing project. The term “public housing” means low-income housing, and all necessary appurtenances thereto, assisted under the 1937 Act, other than assistance under 42 U.S.C. 1437f of the 1937 Act (section 8). The term “public housing”

includes dwelling units in a mixed-finance project that are assisted by a public housing agency with public housing capital assistance or Operating Fund assistance. When used in reference to public housing, the term "project" means housing developed, acquired, or assisted by a PHA under the 1937 Act, and the improvement of any such housing.

Public housing requirements. All requirements applicable to public housing including, but not limited to, the 1937 Act; HUD regulations; the Consolidated Annual Contributions Contract, including amendments; HUD notices; and all applicable federal statutes, executive orders, and regulatory requirements, as these requirements may be amended from time to time.

Reasonable cost. An amount to rehabilitate or modernize an existing structure that is not greater than 90 percent of the TDC for a new development of the same structure type, number, and size of units in the same market area. Reasonable costs are also determined with consideration of HUD regulations including 24 CFR part 85, and 2 CFR part 225 (codifying OMB Circular A-87).

Reconfiguration. The altering of the interior space of buildings (e.g., moving or removing interior walls to change the design, sizes, or number of units).

Uniform Federal Accessibility Standards (UFAS). As defined in 24 CFR 8.32; see also 24 CFR part 40.

§ 905.110 Incorporation by reference.

(a) Certain material is incorporated by reference into this part, with the approval of the Director of the **Federal Register**, under 5 U.S.C. 552(a) and 1 CFR part 51. To enforce any edition other than that specified in this section, HUD must publish notice of change in the **Federal Register** and the material must be available to the public. Incorporated material is available from the sources listed below and is available for inspection at HUD's Office of Policy Development and Research, Affordable Housing Research and Technology Division, Department of Housing and Urban Development, telephone number 202-408-4370 (this is not a toll-free number). This material is also available for inspection at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, call 202-741-6030 (this is not a toll-free number) or go to http://www.archives.gov/federal_register/code_of_federal_regulations/ibr_locations.html.

(b) American Society of Heating, Refrigerating, and Air-Conditioning Engineers, Inc., 1791 Tulle Circle NE., Atlanta, GA 30329 (<http://www.ashrae.org/standards-research-technology/standards-guidelines>).

(1) ASHRAE 90.1-2010, "Energy Standard for Buildings Except Low-Rise Residential Buildings," copyright 2010, IBR approved for §§ 905.200(b) and 905.312(b) of this part.

(2) [Reserved].

(c) International Code Council, 500 New Jersey Avenue NW., 6th Floor, Washington, DC 20001.

(1) International Energy Conservation Code (IECC), January 2009, IBR approved for §§ 905.200(b) and 905.312(b).

(2) [Reserved].

■ 5. Add subparts B, C, and D to read as follows:

Subpart B—Eligible Activities

Sec.

905.200 Eligible activities.

905.202 Ineligible activities and costs.

905.204 Emergencies and natural disasters.

Subpart C—General Program Requirements

905.300 Capital fund submission requirements.

905.302 Timely submission of the CF ACC amendment by the PHA.

905.304 CF ACC term and covenant to operate.

905.306 Obligation and expenditure of Capital Fund grants.

905.308 Federal requirements applicable to all Capital Fund activities.

905.310 Disbursements from HUD.

905.312 Design and construction.

905.314 Cost and other limitations.

905.316 Procurement and contract requirements.

905.318 Title and deed.

905.320 Contract administration and acceptance of work.

905.322 Fiscal closeout.

905.324 Data reporting requirements.

905.326 Records.

Subpart D—Capital Fund Formula

905.400 Capital Fund formula (CF formula).

Subpart B—Eligible Activities

§ 905.200 Eligible activities.

(a) **General.** Activities that are eligible to be funded with Capital Funds as identified in this section include only items specified in an approved CFP 5-Year Action Plan as identified in § 905.300, or approved by HUD for emergency and natural disaster assistance, other than presidentially declared natural disasters and emergencies.

(b) **Eligible activities.** Eligible activities include the development, financing, and modernization of public housing projects, including the

redesign, reconstruction, and reconfiguration of public housing sites and buildings (including compliance with the accessible design and construction requirements contained in 24 CFR 8.32, 24 CFR part 40, 24 CFR part 100, 28 CFR 35.151, and 28 CFR part 36, as applicable) and the development of mixed-finance projects, including the following:

(1) **Modernization.** Modernization is defined in § 905.108 of this part;

(2) **Development.** Development refers to activities and related costs to add units to a PHA's public housing inventory under § 905.600 of this part, including: construction and acquisition with or without rehabilitation; any and all undertakings necessary for planning, design, financing, land acquisition, demolition, construction, or equipment, including development of public housing units, and buildings, facilities, and/or related appurtenances (i.e., nondwelling facilities/spaces).

Development of mixed-finance projects include the provision of public housing through a regulatory and operating agreement, master contract, individual lease, condominium or cooperative agreement, or equity interest.

(3) **Financing.** Debt and financing costs (e.g., origination fees, interest) incurred by PHAs for development or modernization of PHA projects that involves the use of Capital Funds, including, but not limited to:

(i) Mixed finance as described in § 905.604 of this part;

(ii) The Capital Fund Financing Program (CFFP) as described in § 905.500 of this part; and

(iii) Any other use authorized by the Secretary under section 30 of the 1937 Act (42 U.S.C. 1437).

(4) **Vacancy reduction.** Physical improvements to reduce the number of units that are vacant. Not included are costs for routine vacant unit turnaround, such as painting, cleaning, and minor repairs. Vacancy reduction activities must be remedies to a defined vacancy problem detailed in a vacancy reduction program included in the PHA's CFP 5-Year Action Plan.

(5) **Nonroutine maintenance.** Work items that ordinarily would be performed on a regular basis in the course of maintenance of property, but have become substantial in scope because they have been postponed and involve expenditures that would otherwise materially distort the level trend of maintenance expenses. These activities also include the replacement of obsolete utility systems and dwelling equipment.

(6) **Planned code compliance.** Building code compliance includes

design and physical improvement costs associated with:

(i) Correcting violations of local building code or the Uniform Physical Condition Standards (UPCS) under the Public Housing Assessment System (PHAS), and

(ii) A national building code, such as those developed by the International Code Council or the National Fire Protection Association; and the IECC or ASHRAE 90.1–2010 (both incorporated by reference, see, § 905.110 of this part), for multifamily high-rises (four stories or higher), or a successor energy code or standard that has been adopted by HUD for new construction pursuant to section 109 of the Cranston-Gonzales National Affordable Housing Act, Public Law 101–625, codified at 42 U.S.C. 12709, or other relevant authority.

(7) *Management improvements.* Noncapital activities that are project-specific or PHA-wide improvements needed to upgrade or improve the operation or maintenance of the PHA's projects, to promote energy conservation, to sustain physical improvements at those projects, or correct management deficiencies. PHAs must be able to demonstrate the linkage between the management improvement and the correction of an identified management deficiency, including sustaining the physical improvements. HUD encourages PHAs, to the greatest extent feasible, to hire residents as trainees, apprentices, or employees to carry out activities under this part, and to contract with resident owned businesses as required by section 3 of the Housing and Community Development Act of 1968, 12 U.S.C. 1701u. Management improvement costs shall be fundable only for the implementation period of the physical improvements, unless a longer period, up to a maximum of 4 years, is clearly necessary to achieve performance targets. Eligible activities include the following costs:

(i) Training for PHA personnel in operations and procedures, including resident selection, rent collection and eviction;

(ii) Improvements to management, financial, and accounting control systems of the PHA;

(iii) Improvement of resident and project security;

(iv) Activities that assure or foster equal opportunity; and

(v) Activities needed in conjunction with capital expenditures to facilitate programs to improve the empowerment and economic self-sufficiency of public housing residents, including the costs for resident job training and resident business development activities to

enable residents and their businesses to carry out Capital Fund-assisted activities.

(vi) Resident management costs not covered by the Operating Fund include:

(A) The cost of technical assistance to a resident council or RMC to assess feasibility of carrying out management functions for a specific development or developments;

(B) The cost to train residents in skills directly related to the operation and management of the development(s) for potential employment by the RMC;

(C) The cost to train RMC board members in community organization, board development, and leadership;

(D) The cost of the formation of an RMC; and

(E) Resident participation costs that promote more effective resident participation in the operation of the PHA in its Capital Fund activities, including costs for staff support, outreach, training, meeting and office space, childcare, transportation, and access to computers that are modest and reasonable.

(8) *Economic self-sufficiency.* Capital expenditures to facilitate programs to improve the empowerment and economic self-sufficiency of public housing residents.

(9) *Demolition and reconfiguration.* (i) The costs to demolish dwelling units or nondwelling facilities subject to prior approval by HUD, where required, and other related costs for activities such as relocation, clearing, and grading the site after demolition, and subsequent site improvements to benefit the remaining portion of the existing public housing property, as applicable.

(ii) The costs to develop dwelling units or nondwelling facilities approved by HUD, where required, and other related costs for activities such as relocation, clearing and grading the site prior to development.

(iii) The costs to reconfigure existing dwelling units to units with different bedroom sizes or to a nondwelling use.

(10) *Resident relocation and mobility counseling.* Relocation and other assistance (e.g., reimbursement to affected residents of reasonable out-of-pocket expenses incurred in connection with temporary relocation, including the cost of moving to and from temporary housing and any increase in monthly rent/utility costs) as may be required or permitted by applicable Public Housing Requirements for permanent or temporary relocation, as a direct result of modernization, development, rehabilitation, demolition, disposition, reconfiguration, acquisition, or an emergency or disaster.

(11) *Security and safety.* Capital expenditures designed to improve the security and safety of residents.

(12) *Homeownership.* Activities associated with public housing homeownership, as approved by HUD, such as:

(i) The cost of a study to assess the feasibility of converting rental units to homeownership units and the preparation of an application for the conversion to homeownership or for the sale of units;

(ii) Construction or acquisition of units;

(iii) Downpayment assistance;

(iv) Closing cost assistance;

(v) Subordinate mortgage loans;

(vi) Construction or permanent financing such as write downs for new construction, or acquisition with or without rehabilitation; and

(vii) Other activities in support of the primary homeownership activities above, including but not limited to:

(A) Demolition to make way for new construction;

(B) Abatement of environmentally hazardous materials;

(C) Relocation assistance and mobility counseling;

(D) Homeownership counseling;

(E) Site improvements; and

(F) Administrative and marketing costs.

(13) *Capital Fund-related legal costs* (e.g., legal costs related to preparing property descriptions for the DOT, zoning, permitting, environmental review, procurement, and contracting).

(14) *Energy efficiency.* Allowed costs include:

(i) Energy audit or updated energy audits to the extent Operating Funds are not available and the energy audit is included within a modernization program.

(ii) Integrated utility management and capital planning to promote energy conservation and efficiency measures.

(iii) Energy and water conservation measures identified in a PHA's most recently updated energy audit.

(iv) Improvement of energy and water-use efficiency by installing fixtures and fittings that conform to the American Society of Mechanical Engineers/ American National Standards Institute standards A112.19.2–1998 and A112.18.1–2000, or any revision thereto, applicable at the time of installation, and by increasing energy efficiency and water conservation by such other means as the Secretary determines are appropriate.

(v) The installation and use of Energy Star appliances whenever energy systems, devices, and appliances are replaced, unless it is not cost-effective

to do so, in accordance with Section 152 of the Energy Policy Act of 2005, 42 U.S.C. 15841.

(vi) Utility and energy management system automation, and metering activities, including changing mastermeter systems to individually metered systems if installed as a part of a modernization activity to upgrade utility systems; for example, electric, water, or gas systems of the PHA consistent with the requirements of 24 CFR part 965.

(15) *Administrative costs.* Any administrative costs, including salaries and employee benefit contributions, other than the Capital Fund Program Fee, must be related to a specific public housing development or modernization project and detailed in the CFP 5-Year Action Plan.

(16) *Audit.* Costs of the annual audit attributable to the portion of the audit covering the CFP in accordance with § 905.322(c) of this part.

(17) *Capital Fund Program Fee.* This fee covers costs associated with oversight and management of the CFP attributable to the HUD-accepted COCC as described in 24 CFR part 990 subpart H. These costs include duties related to capital planning, preparing the CFP Annual Statement/Performance and Evaluation Report, preparing the CFP 5-Year Action Plan, the monitoring of LOCCS, preparing reports, drawing funds, budgeting, accounting, and procuring construction and other miscellaneous contracts. This fee is not intended to cover costs associated with construction supervisory and inspection functions that are considered a front-line cost of the project.

(18) *Emergency activities.* Capital Fund related activities identified as emergency work, as defined in § 905.108 of this part, whether or not the need is indicated in the CFP 5-Year Action Plan.

§ 905.202 Ineligible activities and costs.

The following are ineligible activities and costs for the CFP:

(a) Costs not associated with a public housing project or development, as defined in § 905.604(b)(1);

(b) Activities and costs not included in the PHA's CFP 5-Year Action Plan, with the exception that expenditures for emergencies and disasters, as defined in § 905.204 of this subpart, that are not identified in the 5-year Action Plan because of their emergent nature are eligible costs;

(c) Improvements or purchases that are not modest in design and cost because they include amenities, materials, and design in excess of what is customary for the locality. Air

conditioning is an eligible modest amenity;

(d) Any costs not authorized as outlined in 2 CFR part 225 (codifying OMB Circular A-87), including, but not limited to, indirect administrative costs and indemnification;

(e) Public housing operating assistance, except as provided in § 905.314(l) of this part;

(f) Direct provision of social services through either force account or contract labor. Examples of ineligible direct social services include, but are not limited to, salaries for social workers or GED teachers;

(g) Eligible costs that are in excess of the amount directly attributable to the public housing units when the physical or management improvements, including salaries and employee benefits and contributions, will benefit programs other than public housing, such as section 8 Housing Choice Voucher or local revitalization programs;

(h) Ineligible management improvements include:

(1) Costs for security guards or ongoing security services (Capital Funds may only be used for the initial capital (e.g., fencing, lights, and cameras) or noncapital (e.g., training of in-house security staff) management improvements but may not be used for the ongoing costs, such as security guards after the end of the implementation period of the physical improvements);

(2) General remedial education; and

(3) Job counseling, job development and placement, supportive services during training, and the hiring of a resident coordinator. No continued Capital Funds will be provided after the end of the implementation period of the management improvements. The PHA shall be responsible for finding other funding sources, reducing its ongoing management costs, or terminating the management activities;

(i) Eligible cost that is funded by another source and would result in duplicate funding; and

(j) Any other activities and costs that HUD may determine on a case-by-case basis.

§ 905.204 Emergencies and natural disasters.

(a) *General.* PHAs are required by the CF ACC to carry various types of insurance to protect it from loss. In most cases, insurance coverage will be the primary source of funding to pay repair or replacement costs associated with emergencies and natural disasters. Where the Department's Annual Appropriations Act establishes a set-

aside from the Capital Fund appropriation for emergencies and natural disasters, the procedures in this section apply.

(b) *Emergencies and natural disasters.* An emergency is an unforeseen or unpreventable event or occurrence that poses an immediate threat to the health and safety of the residents that must be corrected within one year of funding. A natural disaster for purposes of the Capital Fund reserve, is a non-presidentially declared disaster. In the event an emergency or natural disaster arises, HUD may require a PHA to use any other source that may legally be available, including unobligated Capital Funds, prior to providing emergency or natural disaster funds from the set-aside. The Department will review, on a case-by-case basis, requests for emergency and natural disaster funding from PHAs.

(c) *Procedure to request emergency or natural disaster funds.* To obtain emergency or natural disaster funds, a PHA shall submit a written request in the form and manner prescribed by HUD. In a natural disaster where the PHA requires immediate relief to preserve the property and safety of the residents, the PHA may submit a preliminary request outlined in paragraph (d) of this section. Subsequently, the PHA is required to complete and submit the remaining information outlined in paragraph (e) of this section, at a time prescribed by HUD. For emergency requests, PHAs are to follow the procedures outlined in paragraph (e) of this section.

(d) *Procedure to request preliminary natural disaster grant for immediate preservation.* A PHA may request a preliminary grant only for costs necessary for immediate preservation of the property and safety of the residents. The application should include the reasonable identification of damage and preservation costs as determined by the PHA. An independent assessment will be required when the PHA submits the final request or when the PHA reconciles the preliminary application grant with the actual amounts received from the Federal Emergency Management Agency (FEMA), insurance carriers, and other natural disaster relief sources. Regardless of whether further funding from the set-aside is requested, at a time specified by HUD, the PHA will be expected to provide a reconciliation of all funds received, to ensure that the PHA does not receive duplicate funding.

(e) *Procedure for an emergency or a final request for natural disaster funds.* In the request the PHA shall:

(1) Identify the public housing project(s) with the emergency or natural disaster condition(s).

(2) Identify and provide the date of the conditions that present an unforeseen or unpreventable threat to the health, life, or safety of residents, in the case of emergency; or Natural disaster (e.g., hurricane, tornado, etc.).

(3) Describe the activities that will be undertaken to correct the emergency or the conditions caused by the natural disaster and the estimated cost.

(4) Provide an independent assessment of the extent of and the cost to correct the condition. The assessment must be specific as to the damage and costs associated with the emergency or natural disaster. An independent estimate of damage and repair cost is required as a part of the final natural disaster application. For natural disasters, the assessment must identify damage specifically caused by the natural disaster. The set-aside can be used only to pay costs to repair or replace a public housing project damaged as a result of the natural disaster, not for nonroutine maintenance or other improvements.

(5) Provide a copy of a currently effective DOT covering the property and an opinion of counsel that there are no preexisting liens or other encumbrances on the property.

(6) Demonstrate that without the requested funds from the set-aside, the PHA does not have adequate funds available to correct the emergency condition(s).

(7) Identify all other sources of available funds (e.g., insurance proceeds, FEMA).

(8) Any other material required by HUD.

(f) *HUD Action.* HUD shall review all requests for emergency or natural disaster funds. If HUD determines that a PHA's request meets the requirements of this section, HUD shall approve the request subject to the availability of funds in the set-aside, in the order in which requests are received and are determined approvable.

(g) *Submission of the CF ACC.* Upon being provided with a CF ACC Amendment from HUD, the PHA must sign and date the CF ACC Amendment and return it to HUD by the date established by HUD. HUD will execute the signed and dated CF ACC Amendment submitted by the PHA.

Subpart C—General Program Requirements

§ 905.300 Capital fund submission requirements.

(a) *General.* Unless otherwise stated, the requirements in this section apply to

both qualified PHAs (as described in § 903.3(c) of this chapter) and nonqualified PHAs. Each PHA must complete a comprehensive physical needs assessment (PNA).

(1) *Applicability.* Small PHAs (PHAs that own or operate fewer than 250 public housing units) must comply with the requirements of this section beginning 30 days after the end of the federal fiscal year quarter following HUD's publication of a notice in the **Federal Register**.

(2) [Reserved].

(b) *Capital Fund program submission requirements.* At the time that the PHA submits the ACC Amendment(s) for its Capital Fund Grants(s) to HUD, the PHA must also submit the following items:

(1) *CFP 5-Year Action Plan.* (i) *Content.* The CFP 5-Year Action Plan must describe the capital improvements necessary to ensure long-term physical and social viability of the PHA's public housing developments, including the capital improvements to be undertaken within the 5-year period, their estimated costs, status of environmental review, and any other information required for participation in the CFP, as prescribed by HUD. In order to be entitled to fungibility, PHA's must have an approved 5-year Action Plan. Except in the case of emergency/disaster work, the PHA shall not spend Capital Funds on any work that is not included in an approved CFP 5-Year Action Plan and its amendments.

(ii) *Budget.* The Capital Fund Budget for each of the 5 years shall be prepared by a PHA using the form(s) prescribed by HUD. Work items listed in the budget must include, but are not limited to, the following:

(A) Where a PHA has an approved Capital Fund Financing Program (CFFP) loan, debt service payments for the grants from which the payments are scheduled;

(B) Where a PHA has an approved CFFP loan, the PHA shall also include all work and costs, including debt service payments, in the CFP 5-Year Action Plan. Work associated with the use of financing proceeds will be reported separately in a form and manner prescribed by HUD; or

(C) Work affecting health and safety and compliance with regulatory requirements such as section 504 of the Rehabilitation Act of 1973 and HUD's implementing regulations at 24 CFR part 8, and the lead-based paint poisoning prevention standards at 24 CFR part 35, before major systems (e.g., heating, roof, etc.) and other costs of lower priority.

(iii) PHA Criteria for Significant Amendment or Modification. The PHA must include in the basic criteria that

the PHA will use for determining a significant amendment or modification to the CFP 5-Year Action Plan. In addition to the criteria established by the PHA, for the purpose of the CFP, a proposed demolition, disposition, homeownership, Capital Fund financing, development, or mixed-finance proposal are considered significant amendments to the CFP 5-Year Action Plan.

(iv) *Submission.* The PHA must submit a Board-approved CFP 5-Year Action Plan at least once every 5 years. The PHA may choose to update its CFP 5-Year Action Plan every year. The PHA shall indicate whether its CFP 5-Year Action Plan is fixed or rolling. Prior to submission to HUD, the 5-Year Action Plan must have been approved by the PHA's Board of Commissioners. In any given year that a PHA does not have a CFP 5-Year Action Plan that is approved by the PHA Board of Commissioners and HUD, the Capital Fund grant(s) for these PHAs will be reserved and obligated; however, the PHA will not have access to those funds until its CFP 5-Year Action Plan is approved by the PHA Board of Commissioners and HUD.

(v) Significant amendments or modification to the CFP 5 Year Action Plan. PHAs making significant amendments or modifications to the CFP 5-Year Action Plan, as defined in paragraph (b)(1)(iii) of this section, must follow the requirements of this section.

(A) A PHA after submitting its 5-Year Action Plan may amend or modify the plan. If the amendment or modification is a significant amendment or modification, as defined in paragraph (b)(1)(iii) of this section, the PHA:

(1) May not adopt the amendment or modification until the PHA has duly called a meeting of its Board of Commissioners (or similar governing body) and the meeting at which the amendment or modification is adopted, is open to the public; and

(2) May not implement the amendment or modification until notification of the amendment or modifications are provided to HUD and approved by HUD in accordance with HUD's plan review procedures, as provided in paragraph (b)(6) of this section.

(B) Each significant amendment or modification to a plan submitted to HUD is subject to the requirement of paragraph (b)(3) of this section.

(2) *Certifications required for receipt of Capital Fund grants.* The PHA is also required to submit various certifications to HUD, in a form prescribed by HUD, including, but not limited to:

(i) Certification of PIC Data;

(ii) Standard Form—Disclosure of Lobbying Activities;

(iii) Civil Rights Compliance, in a form prescribed by HUD; and

(iv) Certification of Compliance with Public Hearing Requirements.

(3) *Conduct of public hearing and Resident Advisory Board Consultation.* A PHA must annually conduct a public hearing and consult with the Resident Advisory Board (RAB) of the PHA to discuss the Capital Fund submission. The PHA may elect to conduct a separate annual public hearing in order to solicit public comments or to hold the annual public hearing at the same time as the hearing for the Annual PHA Plan, the 5-Year Plan, or the required annual hearing for qualified public housing authorities. The hearing must be conducted at a location that is convenient to the residents served by the PHA.

(i) Not later than 45 days before the public hearing is to take place, the PHA must:

(A) Make the Capital Fund submission along with the material required under this paragraph (b) available to the residents and the RAB; and

(B) Publish a notice informing the public that the information is available for review and inspection; that a public hearing will take place on the plan; and of the date, time, and location of the hearing.

(C) PHAs shall conduct reasonable outreach activities to encourage broad public participation in the review of the Capital Fund submission.

(4) *Public and RAB comments.* The PHA must consider the comments from the residents, the public, and the RAB on the Capital Fund submission, or any significant modification thereto. In submitting the final CFP 5-Year Action Plan to HUD for approval, or any significant amendment or modification to the 5-Year Action Plan to HUD for approval, the PHA must include a copy of the recommendations made by the RAB(s) and a description of the manner in which the PHA addressed these recommendations.

(5) *Consistency with Consolidated Plan.* The Capital Fund submission must be consistent with any applicable Consolidated Plan.

(6) *HUD review and approval.* The CFP submission requirements must meet the requirements of this part as well as the Public Housing Program Requirements as defined in § 905.108 of this part. A PHA is required to revise or correct information that is not in compliance, and HUD has the authority to impose administrative sanctions until the appropriate revisions are made.

HUD will review the CFP submission requirements to determine whether:

(i) All of the information that is required to be submitted is included;

(ii) The information is consistent with the needs identified in the PNA and data available to HUD; and

(iii) There are any issues of compliance with applicable laws, regulations, or contract requirements that have not been addressed with the proposed use of the Capital Fund.

(7) *Time frame for submission of CFP requirements.* The requirements identified in this paragraph (b) must be submitted to HUD, in a format prescribed by HUD, at the time that the PHA submits its signed CF ACC Amendment.

(8) *Performance and Evaluation Report.* (i) All PHAs must prepare a CFP Annual Statement/Performance and Evaluation Report at a time and in a format prescribed by HUD. These reports shall be retained on file for all grants for which a final Actual Modernization Cost Certificate (AMCC) or an Actual Development Cost Certificate (ADCC) has not been submitted. A final Performance and Evaluation Report must be submitted in accordance with 24 CFR 905.322, at the time the PHA submits its AMCC or ADCC.

(ii) PHAs that are designated as troubled performers under PHAS (24 CFR part 902) or as troubled under the Section 8 Management Assessment Program (SEMAP) (24 CFR part 985), and/or were identified as noncompliant with section 9(j) obligation and expenditure requirements during the fiscal year, shall submit their CFP Annual Statement/Performance and Evaluation Reports to HUD for review and approval.

(iii) All other PHAs, that are not designated as troubled performers under PHAS and are not designated as troubled under SEMAP, and that were in compliance with section 9(j) obligation and expenditure requirements during the fiscal year, shall prepare a CFP Annual Statement/Performance and Evaluation report for all open grants and shall retain the report(s) on file at the PHA, to be available to HUD upon request.

(9) *Moving to Work (MTW) PHAs.* MTW PHAs are to submit the Capital Fund submissions as part of the MTW Plan annually, as required by the MTW Agreement.

(c) [Reserved]

(d) [Reserved]

§ 905.302 Timely submission of the CF ACC amendment by the PHA.

Upon being provided with a CF ACC Amendment from HUD, the PHA must sign and date the CF ACC Amendment and return it to HUD by the date established. HUD will execute the signed and dated CF ACC Amendment submitted by the PHA. If HUD does not receive the signed and dated Amendment by the submission deadline, the PHA will receive the Capital Fund grant for that year; however, it will have less than 24 months to obligate 90 percent of the Capital Fund grant and less than 48 months to expend these funds because the PHA's obligation start date and disbursement end date for these grants will remain as previously established by HUD.

§ 905.304 CF ACC term and covenant to operate.

(a) *Period of obligation to operate as public housing.* The PHA shall operate all public housing projects in accordance with the CF ACC, as amended, and applicable HUD regulations, for the statutorily prescribed period. These periods shall be evidenced by a recorded DOT on all public housing property. If the PHA uses Capital Funds to develop public housing or to modernize existing public housing, the CF ACC term and the covenant to operate those projects are as follows:

(1) *Development activities.* Each public housing project developed using Capital Funds shall establish a restricted use covenant, either in the DOT or as a Declaration of Restrictive Covenants, to operate under the terms and conditions applicable to public housing for a 40-year period that begins on the date on which the project becomes available for occupancy, as determined by HUD.

(2) *Modernization activities.* For PHAs that receive Capital Fund assistance, the execution of each new CF ACC Amendment establishes an additional 20-year period that begins on the latest date on which modernization is completed, except that the additional 20-year period does not apply to a project that receives Capital Fund assistance only for management improvements.

(3) *Operating Fund.* Any public housing project developed that receives Operating Fund assistance shall have a covenant to operate under requirements applicable to public housing for a 10-year period beginning upon the conclusion of the fiscal year for which such amounts were provided, except for such shorter period as permitted by HUD by an exception.

(b) *Mortgage or security interests.* The PHA shall not allow any mortgage or security interest in public housing assets, including under section 30 of the 1937 Act (42 U.S.C. 1437z-2), without prior written approval from HUD. PHAs that undertake financing unsecured by public housing assets shall include the following nonrecourse language in all financing documents as follows:

“This financing is non-recourse to any public housing property (real or personal property including all public housing assets or income), or disposition proceeds approved pursuant to Section 18 of the United States Housing Act of 1937 (unless explicitly permitted by HUD in the Section 18 approval letter).”

(c) *Applicability of latest expiration date.* All public housing subject to this part or required by law shall be maintained and operated as public housing, as prescribed, until the latest expiration date provided in section 9(d)(3) of the 1937 Act (42 U.S.C. 1437g(d)(3)) or any other provision of law or regulation mandating the operation of the housing as public housing, or under terms and conditions applicable to public housing, for a specified period of time.

§ 905.306 Obligation and expenditure of Capital Fund grants.

(a) *Obligation.* A PHA shall obligate each Capital Fund grant, including formula grants, Replacement Housing Factor (RHF) grants, Demolition and Disposition Transitional Funding (DDTF) grants, and natural disaster grants, no later than 24 months after, and emergency grants no later than 12 months after, the date on which the funds become available to the PHA for obligation, except as provided in paragraphs (c) and (d) of this section. However, a PHA with unobligated funds from a grant shall disregard this requirement for up to not more than 10 percent of the originally allocated funds from that grant. The funds become available to the PHA when HUD executes the CF ACC Amendment. With HUD approval, and subject to the availability of appropriations, the PHA can accumulate RHF grants for up to 5 years or until it has adequate funds to undertake replacement housing. The PHA shall obligate 90 percent of the RHF grant within 24 months from the date that the PHA accumulates adequate funds, except as provided in paragraph (c) of this section.

(b) *Items and costs.* For funds to be considered obligated, all items and costs must meet the definition of “obligation” in § 905.108 of this part.

(c) *Extension to obligation requirement.* The PHA may request an extension of the obligation deadline, and HUD may grant an extension for a period of up to 12 months, based on:

- (1) The size of the PHA;
- (2) The complexity of the CFP of the PHA;
- (3) Any limitation on the ability of the PHA to obligate the amounts allocated for the PHA from the Capital Fund in a timely manner as a result of state or local law; or
- (4) Any other factors that HUD determines to be relevant.

(d) *HUD extension for other reasons.* HUD may extend the obligation deadline for a PHA for such a period as HUD determines to be necessary, if HUD determines that the failure of the PHA to obligate assistance in a timely manner is attributable to:

- (1) Litigation;
- (2) Delay in obtaining approvals from the Federal Government or a state or local government that is not the fault of the PHA;
- (3) Compliance with environmental assessment and abatement requirements;
- (4) Relocating residents;
- (5) An event beyond the control of the PHA; or
- (6) Any other reason established by HUD by notice in the **Federal Register**.

(e) *Failure to obligate.* (1) For any month during the fiscal year, HUD shall withhold all new Capital Fund grants from any PHA that has unobligated funds in violation of paragraph (a) of this section. The penalty will be imposed once the violations of paragraph (a) are known. The PHA may cure the noncompliance by:

- (i) Requesting in writing that HUD recapture the unobligated balance of the grant; or
- (ii) Continuing to obligate funds for the grant in noncompliance until the noncompliance is cured.

(2) After the PHA has cured the noncompliance, HUD will release the withheld Capital Fund grant(s) minus a penalty of one-twelfth of the grant for each month of noncompliance.

(f) *Expenditure.* The PHA shall expend all grant funds within 48 months after the date on which funds become available, as described in paragraph (a) of this section. The deadline to expend funds may be extended only by the period of time of a HUD-approved extension of the obligation deadline. No other extensions of the expenditure deadline will be granted. All funds not expended will be recaptured.

§ 905.308 Federal requirements applicable to all Capital Fund activities.

(a) The PHA shall comply with the requirements of 24 CFR part 5 (General HUD Program Requirements; Waivers), 24 CFR part 85 (Administrative Requirements for Grants and Cooperative Agreements to State, Local and Federally Recognized Indian Tribal Governments), and this part.

(b) The PHA shall also comply with the following program requirements.

(1) *Nondiscrimination and equal opportunity.* The PHA shall comply with all applicable nondiscrimination and equal opportunity requirements, including, but not limited to, the Department’s generally applicable nondiscrimination and equal opportunity requirements at 24 CFR 5.105(a) and the Architectural Barriers Act of 1968 (42 U.S.C. 4151 *et seq.*), and its implementing regulations at 24 CFR parts 40 and 41. The PHA shall affirmatively further fair housing in its use of funds under this part, which includes, but is not limited to, addressing modernization and development in the completion of requirements at 24 CFR 903.7(o).

(2) *Environmental requirements.* All activities under this part are subject to an environmental review by a responsible entity under HUD’s environmental regulations at 24 CFR part 58 and must comply with the requirements of the National Environmental Policy Act of 1969 (NEPA)(42 U.S.C. 4321 *et seq.*) and the related laws and authorities listed at 24 CFR 58.5. HUD may make a finding in accordance with 24 CFR 58.11 and may perform the environmental review itself under the provisions of 24 CFR part 50. In those cases where HUD performs the environmental review under 24 CFR part 50, it will do so before approving a proposed project, and will comply with the requirements of NEPA and the related requirements at 24 CFR 50.4.

(3) *Wage rates.* (i) Davis-Bacon wage rates. For all work or contracts exceeding \$2,000 in connection with development activities or modernization activities (except for nonroutine maintenance work, as defined in § 905.200(b)(5) of this part), all laborers and mechanics employed on the construction, alteration, or repair shall be paid not less than the wages prevailing in the locality, as determined by the Secretary of Labor pursuant to the Davis-Bacon Act (40 U.S.C. 3142).

(ii) HUD-determined wage rates. For all operations work and contracts, including routine and nonroutine maintenance work (as defined in § 905.200(b)(5) of this part), all laborers and mechanics employed shall be paid

not less than the wages prevailing in the locality, as determined or adopted by HUD pursuant to section 12(a) of the 1937 Act, 42 U.S.C. 1437j(a).

(iii) *State wage rates.* Preemption of state prevailing wage rates as provided at 24 CFR 965.101.

(iv) *Volunteers.* The prevailing wage requirements of this section do not apply to volunteers performing development, modernization, or nonroutine maintenance work under the conditions set out in 24 CFR part 70.

(4) *Technical wage rates.* All architects, technical engineers, draftsmen, and technicians (other than volunteers under the conditions set out in 24 CFR part 70) employed in a development or modernization project shall be paid not less than the wages prevailing in the locality, as determined or adopted (subsequent to a determination under applicable state or local law) by HUD.

(5) *Lead-based paint poisoning prevention.* The PHA shall comply with the Lead-Based Paint Poisoning Prevention Act (LPPPA) (42 U.S.C. 4821 *et seq.*), the Residential Lead-Based Paint Hazard Reduction Act (42 U.S.C. 4851 *et seq.*), and the Lead Safe Housing Rule and the Lead Disclosure Rule at 24 CFR part 35.

(6) *Fire safety.* A PHA shall comply with the requirements of section 31 of the Federal Fire Prevention and Control Act of 1974 (15 U.S.C. 2227).

(7) *Flood insurance and floodplain requirements.* The PHA will not engage in the acquisition, construction, or improvement of a public housing project located in an area that has been identified by the FEMA as having special flood hazards, unless:

(i) The requirements of 24 CFR part 55, Floodplain Management, have been met, including a determination by a responsible entity under 24 CFR part 58 or by HUD under 24 CFR part 50 that there is no practicable alternative to locating in an area of special flood hazards and the minimization of unavoidable adverse impacts;

(ii) Flood insurance on the building is obtained in compliance with the Flood Disaster Protection Act of 1973 (42 U.S.C. 4001 *et seq.*); and

(iii) The community in which the area is situated is participating in the National Flood Insurance Program in accordance with 44 CFR parts 59 through 79, or less than one year has passed since FEMA notification regarding flood hazards.

(8) *Coastal barriers.* In accordance with the Coastal Barriers Resources Act (16 U.S.C. 3501 *et seq.*), no financial assistance under this part may be made

available within the Coastal Barrier Resources System.

(9) *Displacement, relocation, and real property acquisition.* All acquisition or rehabilitation activities carried out under the Capital Fund, including acquisition of any property for development, shall comply with the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (URA) (42 U.S.C. 4601–4655) and with implementing regulations at 49 CFR part 24. Demolition or disposition under section 18 of the 1937 Act, 42 U.S.C. 1437p, is covered by the relocation provisions at 24 CFR 970.21.

(10) *Procurement and contract requirement.* PHAs and their contractors shall comply with section 3 of the Housing and Community Development Act of 1968 (12 U.S.C. 1701u) and HUD's implementing rules at 24 CFR part 135.

§ 905.310 Disbursements from HUD.

(a) The PHA shall initiate a fund requisition from HUD only when funds are due and payable, unless HUD approves another payment schedule as authorized by 24 CFR 85.21.

(b) The PHA shall maintain detailed disbursement records to document eligible expenditures (e.g., contracts or other applicable documents), in a form and manner prescribed by HUD.

§ 905.312 Design and construction.

The PHA shall meet the following design and construction standards, as applicable, for all development and modernization.

(a) Physical structures shall be designed, constructed, and equipped to be consistent with the neighborhoods they occupy; meet contemporary standards of modest design, comfort, and livability (see also § 905.202(c) of this part); promote security; promote energy conservation; and be attractive so as to harmonize with the community.

(b) All development projects shall be designed and constructed in compliance with:

(1) A national building code, such as those developed by the International Code Council or the National Fire Protection Association; and the IECC or ASHRAE 90.1–2010 (both incorporated by reference, see § 905.110 of this part), for multifamily high-rises (four stories or higher), or a successor energy code or standard that has been adopted by HUD pursuant to 42 U.S.C. 12709 or other relevant authority;

(2) Applicable state and local laws, codes, ordinances, and regulations;

(3) Other federal requirements, including fire protection and safety standards implemented under section

31 of the Fire Administration Authorization Act of 1992, 15 U.S.C. 2227 and HUD minimum property standards (e.g., 24 CFR part 200, subpart S);

(4) Accessibility Requirements as required by section 504 of the Rehabilitation Act (29 U.S.C. 794) and implementing regulations at 24 CFR part 8; title II of the Americans with Disabilities Act (42 U.S.C. 12101 *et seq.*) and implementing regulations at 28 CFR part 35; and, if applicable, the Fair Housing Act (42 U.S.C. 3601–3619) and implementing regulations at 24 CFR part 100; and

(5) Occupancy of high-rise elevator structures by families with children. Pursuant to 42 U.S.C. 1437d(a), a high-rise elevator structure shall not be provided for families with children regardless of density, unless the PHA demonstrates and HUD determines that there is no practical alternative.

(c) All modernization projects shall be designed and constructed in compliance with:

(1) The modernization standards as prescribed by HUD;

(2) Accessibility requirements as required by section 504 of the Rehabilitation Act (29 U.S.C. 794) and implementing regulations at 24 CFR part 8; title II of the Americans with Disabilities Act (42 U.S.C. 12101 *et seq.*) and implementing regulations at 28 CFR part 35; and, if applicable, the Fair Housing Act (42 U.S.C. 3601–3619) and implementing regulations at 24 CFR part 100; and

(3) Cost-effective energy conservation measures, identified in the PHA's most recently updated energy audit.

(d) Pursuant to the Energy Policy Act of 2005, in purchasing appliances, PHAs shall purchase appliances that are Energy Star products or Federal Energy Management Program designed products, unless the PHA determines that the purchase of these appliances is not cost effective.

§ 905.314 Cost and other limitations.

(a) *Eligible administrative costs.* Where the physical or management improvement costs will benefit programs other than Public Housing, such as the Housing Choice Voucher program or local revitalization programs, eligible administrative costs are limited to the amount directly attributable to the public housing program.

(b) *Maximum project cost.* The maximum project cost represents the total amount of public housing capital assistance used in connection with the development of a public housing project, and includes:

(1) Project costs that are subject to the TDC limit (i.e., HCC and Community Renewal Costs); and

(2) Project costs that are not subject to the TDC limit (i.e., Additional Project Costs). The total project cost to be funded with public housing capital assistance, as set forth in the proposal and as approved by HUD, becomes the maximum project cost stated in the ACC Amendment. Upon completion of the project, the actual project cost is determined based upon the amount of public housing capital assistance expended for the project, and this becomes the maximum project cost for purposes of the ACC Amendment.

(c) *TDC limit.* (1) Public housing funds, including Capital Funds, may not be used to pay for HCC and Community Renewal Costs in excess of the TDC limit, as determined under paragraph (b)(2) of this section. However, HOPE VI grantees will be eligible to request a TDC exception for public housing and HOPE VI funds awarded in FFY 1996 and prior years. PHAs may also request a TDC exception for integrated utility management, capital planning, and other capital and management activities that promote energy conservation and efficiency. HUD will examine the request for TDC exceptions to ensure that they would be cost-effective, so as to ensure that up-front expenditures subject to the exceptions would be justified by future cost savings.

(2) *Determination of TDC limit.* HUD will determine the TDC limit for a public housing project as follows:

(i) *Step 1: Unit construction cost guideline.* HUD will first determine the applicable "construction cost guideline" by averaging the current construction costs as listed in two nationally recognized residential construction cost indices for publicly bid construction of a good and sound quality for specific bedroom sizes and structure types. The two indices HUD will use for this purpose are the R.S. Means cost index for construction of "average" quality and the Marshall & Swift cost index for construction of "good" quality. HUD has the discretion to change the cost indices to other such indices that reflect comparable housing construction quality through a notice published in the **Federal Register**.

(ii) *Step 2: Bedroom size and structure types.* The construction cost guideline is then multiplied by the number of units for each bedroom size and structure type.

(iii) *Step 3: Elevator and nonelevator type structures.* HUD will then multiply the resulting amounts from step 2 by 1.6 for elevator type structures and by 1.75 for nonelevator type structures.

(iv) *Step 4: TDC limit.* The TDC limit for a project is calculated by adding the resulting amounts from step 3 for all the public housing units in the project.

(3) *Costs not subject to the TDC limit.* Additional project costs are not subject to the TDC limit.

(4) *Funds not subject to the TDC limit.* A PHA may use funding sources not subject to the TDC limit (e.g., Community Development Block Grant (CDBG) funds, low-income housing tax credits, private donations, private financing, etc.) to cover project costs that exceed the TDC limit or the HCC limit described in this paragraph (c). Such funds, however, may not be used for items that would result in substantially increased operating, maintenance, or replacement costs, and must meet the requirements of section 102 of the Department of Housing and Urban Development Reform Act of 1989 (Pub. L. 101-235, approved December 15, 1989) (42 U.S.C. 3545). These funds must be included in the project development cost budget.

(d) *Housing Construction Costs (HCC).* (1) *General.* A PHA may not use Capital Funds to pay for HCC in excess of the amount determined under paragraph (d)(2) of this section.

(2) *Determination of HCC limit.* HUD will determine the HCC limit as listed in at least two nationally recognized residential construction cost indices for publicly bid construction of a good and sound quality for specific bedroom sizes and structure types. The two indices HUD will use for this purpose are the R.S. Means cost index for construction of "average" quality and the Marshall & Swift cost index for construction of "good" quality. HUD has the discretion to change the cost indices to other such indices that reflect comparable housing construction quality through a notice published in the **Federal Register**. The resulting construction cost guideline is then multiplied by the number of public housing units in the project, based upon bedroom size and structure type. The HCC limit for a project is calculated by adding the resulting amounts for all public housing units in the project.

(3) The HCC limit is not applicable to the acquisition of existing housing, whether or not such housing will be rehabilitated. The TDC limit is applicable to such acquisition.

(e) *Community Renewal Costs.* Capital Funds may be used to pay for Community Renewal Costs in an amount equivalent to the difference between the HCC paid for with public housing capital assistance and the TDC limit.

(f) *Rehabilitation of existing public housing projects.* The HCC limit is not

applicable to the rehabilitation of existing public housing projects. The TDC limit for modernization of existing public housing is 90 percent of the TDC limit as determined under paragraph (c) of this section. This limitation does not apply to the rehabilitation of any property acquired pursuant to § 905.600 of this part.

(g) *Modernization cost limits.* If the modernization costs are more than 90 percent of the TDC, then the project shall not be modernized. Capital Funds shall not be expended to modernize an existing public housing development that fails to meet the HUD definition of reasonable cost found in § 905.108 of this part, except for:

(1) Emergency work;
(2) Essential maintenance necessary to keep a public housing project habitable until the demolition or disposition application is approved; or
(3) The costs of maintaining the safety and security of a site that is undergoing demolition.

(h) *Administrative cost limits and Capital Fund Program Fee.* (1) Administrative cost limits (for non-asset-management PHAs). The PHA shall not budget or expend more than 10 percent of its annual Capital Fund grant on administrative costs, in accordance with the CFP 5-Year Action Plan.

(2) Capital Fund Program Fee (for asset-management PHAs). For a PHA that is under asset management, the Capital Fund Program Fee and administrative cost limits are the same. For the Capital Fund Program Fee, a PHA may charge a management fee of up to 10 percent of the annual CFP formula grant(s) amount, excluding emergency and disaster grants and also excluding any costs related to lead-based paint or asbestos testing, in-house architectural and engineering work, or other special administrative costs required by state or local law.

(i) Modernization. The PHA shall not budget or expend more than 10 percent of its annual Capital Fund grant on administrative costs, in accordance with its CFP 5-Year Action Plan. The 10 percent limit excludes any costs related to lead-based paint or asbestos testing, in-house Architectural and Engineering work, or other special administrative costs required by state or local law.
(ii) Development. For development work with Capital Fund and RHF grants, the administrative cost limit is 3 percent of the total project budget, or, with HUD's approval, up to 6 percent of the total project budget.

(i) *Management improvement cost limits.* In Fiscal Year (FY) 2014, a PHA shall not use more than 18 percent of its annual Capital Fund grant for eligible

management improvement costs identified in its CFP 5-Year Action Plan. In FY 2015, a PHA shall not use more than 16 percent of its annual Capital Fund grant for eligible management improvement costs identified in its CFP 5-Year Action Plan. In FY 2016, a PHA shall not use more than 14 percent of its annual Capital Fund grant for eligible management improvement costs identified in its CFP 5-Year Action Plan. In FY 2017, a PHA shall not use more than 12 percent of its annual Capital Fund grant for eligible management improvement costs identified in its CFP 5-Year Action Plan. In FY 2018 and thereafter, a PHA shall not use more than 10 percent of its annual Capital Fund grant for eligible management improvement costs identified in its CFP 5-Year Action Plan. Management improvements are an eligible expense for PHAs participating in asset management.

(j) *Types of labor.* A PHA may use force account labor for development and modernization activities if included in a CFP 5-Year Action Plan that is approved by the PHA Board of Commissioners and HUD. HUD approval to use force account labor is not required when the PHA is designated as a high performer under PHAS.

(k) *RMC activities.* When the entire development, financing, or modernization activity, including the planning and architectural design, is administered by an RMC, the PHA shall not retain any portion of the Capital Funds for any administrative or other reason, unless the PHA and the RMC provide otherwise by contract.

(l) *Capital Funds for operating costs.* A PHA may use Capital Funds for operating costs only if it is included in the CFP 5-Year Action Plan that is approved by the PHA Board of Commissioners and HUD, and limited as described in paragraphs (l)(1) and (2) of this section. Capital Funds identified in the CFP 5-Year Action Plan to be transferred to operations are obligated once the funds have been budgeted and drawn down by the PHA. Once such transfer of funds occurs, the PHA must follow the requirements of 24 CFR part 990 with respect to those funds.

(1) *Large PHAs.* A PHA with 250 or more units may use no more than 20 percent of its annual Capital Fund grant for activities that are eligible under the Operating Fund at 24 CFR part 990.

(2) *Small PHAs.* A PHA with less than 250 units, that is not designated as troubled under PHAS, may use up to 100 percent of its annual Capital Fund grant for activities that are eligible under the Operating Fund at 24 CFR part 990, except that the PHA must have

determined that there are no debt service payments, significant Capital Fund needs, or emergency needs that must be met prior to transferring 100 percent of its funds to operating expenses.

§ 905.316 Procurement and contract requirements.

(a) *General.* PHAs shall comply with 24 CFR 85.36, and HUD implementing instructions, for all capital activities including modernization and development, except as provided in paragraph (c) in this section.

(b) *Contracts.* The PHA shall use all contract forms prescribed by HUD. If a form is not prescribed, the PHA may use any Office of Management and Budget (OMB) approved form that contains all applicable federal requirements and contract clauses.

(c) *Mixed-finance development projects.* Mixed-finance development partners may be selected in accordance with 24 CFR 905.604(h). Contracts and other agreements with mixed-finance development partners must specify that they comply with the requirements of §§ 905.602 and 905.604 of this part.

(d) *Assurances of completion.* Notwithstanding 24 CFR 85.36(h), for each construction contract over \$100,000, the contractor shall furnish the PHA with the following:

(1) A bid guarantee from each bidder, equivalent to 5 percent of the bid price; and

(2) One of the following:

(i) A performance bond and payment bond for 100 percent of the contract price;

(ii) A performance bond and a payment bond, each for 50 percent or more of the contract price;

(iii) A 20 percent cash escrow;

(iv) A 10 percent irrevocable letter of credit with terms acceptable to HUD, or

(v) Any other payment method acceptable to HUD.

(e) *Procurement of recovered materials.* PHAs that are state agencies and agencies of a political subdivision of a state that are using assistance under this part for procurement, and any person contracting with such PHAs with respect to work performed under an assisted contract, must comply with the requirements of section 6002 of the Solid Waste Disposal Act, as amended by the Resource Conservation and Recovery Act. In accordance with section 6002, these agencies and persons must procure items designated in guidelines of the Environmental Protection Agency (EPA) at 40 CFR part 247 that contain the highest percentage of recovered material practicable, consistent with maintaining a

satisfactory level of competition, where the purchase price of the item exceeds \$10,000 or the value of the quantity acquired in the preceding fiscal year exceeded \$10,000; must procure solid waste management services in a manner that promotes energy and resource recovery; and must have established an affirmative procurement program for procurement of recovered materials identified in the EPA guidelines.

§ 905.318 Title and deed.

The PHA, or, in the case of mixed-finance, the Owner Entity, shall obtain title insurance that guarantees the title is good and marketable before taking title to any and all sites and properties acquired with public housing funds. Immediately upon taking title to a property, the PHA or Owner Entity shall record the deed and a Declaration of Trust or, in the case of mixed finance, a Declaration of Restrictive Covenants, in the form and in the manner and order prescribed by HUD. The PHA shall at all times maintain a recorded Declaration of Trust or Declaration of Restrictive Covenants in the form and in the manner and order prescribed by HUD on all public housing projects covering the term required by this part.

§ 905.320 Contract administration and acceptance of work.

(a) *Contract administration.* The PHA is responsible, in accordance with 24 CFR 85.36, for all contractual and administrative issues arising out of their procurements. The PHA shall maintain full and complete records on the history of each procurement transaction.

(b) *Inspection and acceptance.* The PHA, or, in the case of mixed finance, the Owner Entity shall carry out inspections of work in progress and goods delivered, as necessary, to ensure compliance with existing contracts. If, upon inspection, the PHA determines that the work and/or goods are complete, satisfactory and, as applicable, otherwise undamaged, except for any work that is appropriate for delayed completion, the PHA shall accept the work. The PHA shall determine any holdback for items of delayed completion and the amount due and payable for the work that has been accepted, including any conditions precedent to payment that are stated in the construction contract or contract of sale. The contractor shall be paid for items only after the PHA inspects and accepts that work.

(c) *Guarantees and warranties.* The PHA or, in the case of mixed finance, the Owner Entity, shall specify the guaranty period and amounts to be withheld, as applicable, and shall

provide that all contractor, manufacturer, and supplier warranties required by the construction and modernization documents shall be assigned to the PHA. The PHA shall inspect each dwelling unit and the overall project approximately 3 months after the beginning of the project guaranty period, 3 months before its expiration, and at other times as may be necessary to exercise its rights before expiration of any warranties. The PHA shall require repair or replacement of all defective items prior to the expiration of the guaranty or warranty periods.

(d) *Notification of completion.* The PHA, or in the case of mixed finance, the Owner Entity, shall require that all contractors and developers notify the PHA in writing when the contract work, including any approved off-site work, will be completed and ready for inspection.

§ 905.322 Fiscal closeout.

(a) *General.* Each Capital Fund grant and/or development project is subject to fiscal closeout. Fiscal closeout includes the submission of a cost certificate; an audit, if applicable; a final Performance and Evaluation Report; and HUD approval of the cost certificate.

(b) *Submission of cost certificate.* (1) When an approved development or modernization activity is completed or when HUD terminates the activity, the PHA must submit to HUD the:

(i) Actual Development Cost Certificate (ADCC) within 12 months. For purposes of the CF ACC, costs incurred between the completion of the development and the date of full availability (DOFA) becomes the actual development cost; and

(ii) Actual Modernization Cost Certificate (AMCC) for each grant, no later than 12 months after the expenditure deadline but no earlier than the obligation end date. A PHA with under 250 units with an approved CFP 5-Year Action Plan for use of 100 percent of the Capital Fund grant in operations may submit the cost certificate any time after the funds have been budgeted to operations and withdrawn, as described in § 905.314(l) of this part.

(2) If the PHA does not submit the cost certificate and the final CFP Annual Statement/Performance and Evaluation Report within the period prescribed in this section, HUD may impose restrictions on open Capital Fund grants; e.g., establish review thresholds, set the grant to "auto review" (HUD automatically reviews it on a periodic basis), or suspend grants, until the cost certificate for the affected grant is submitted. These restrictions may be

imposed by HUD after notification of the PHA.

(c) *Audit.* The cost certificate is a financial statement subject to audit pursuant to 24 CFR 85.26. After submission of the cost certificate to HUD, the PHA shall provide the cost certificate to its independent public auditor (IPA) as part of its annual audit. After audit, the PHA will notify HUD of the grants included in the audit, any exceptions noted by the PHA auditor, and the schedule to complete corrective actions recommended by the auditor.

(d) *Review and approval.* For PHAs exempt from the audit requirements, HUD will review and approve the cost certificate based on available information regarding the Capital Fund grant. For PHAs subject to an audit, HUD will review the information from the annual audit provided by the PHA and approve the certificate after all exceptions, if any, have been resolved.

(e) *Recapture.* All Capital Funds in excess of the actual cost incurred for the grant are subject to recapture. Any funds awarded to the PHA that are returned or any funds taken back from the PHA in a fiscal year after the grant was awarded are subject to recapture.

§ 905.324 Data reporting requirements.

The PHA shall provide, at minimum, the following data reports, at a time and in a form prescribed by HUD:

(a) The Performance and Evaluation Report as described in § 905.300(b)(8) of this part;

(b) Updates on the PHA's building and unit data as required by HUD;

(c) Reports of obligation and expenditure; and

(d) Any other information required for participation in the Capital Fund Program.

§ 905.326 Records.

(a) The PHA will maintain full and complete records of the history of each Capital Fund grant, including, but not limited to, CFP 5-Year Action Plans, procurement, contracts, obligations, and expenditures.

(b) The PHA shall retain for 5 years after HUD approves either the actual development or modernization cost certificate all documents related to the activities for which the Capital Fund grant was received, unless a longer period is required by applicable law.

(c) HUD and its duly authorized representatives shall have full and free access to all PHA offices, facilities, books, documents, and records, including the right to audit and make copies.

Subpart D—Capital Fund Formula

§ 905.400 Capital Fund formula (CF formula).

(a) *General.* This section describes the formula for allocating Capital Funds to PHAs.

(b) *Formula allocation based on relative needs.* HUD shall allocate Capital Funds to the PHAs in accordance with the CF formula. The CF formula measures the existing modernization needs and accrual needs of PHAs.

(c) *Allocation for existing modernization needs under the CF formula.* HUD shall allocate one-half of the available Capital Fund amount based on the relative existing modernization needs of PHAs, determined in accordance with paragraph (d) of this section.

(d) *PHAs with 250 or more units in FFY 1999, except the New York City and Chicago Housing Authorities.* The estimates of the existing modernization needs for these PHAs shall be based on the following:

(1) Objective measurable data concerning the following PHA, community, and project characteristics applied to each project:

(i) The average number of bedrooms in the units in a project (Equation coefficient 4604.7);

(ii) The total number of units in a project (Equation coefficient: 10.17);

(iii) The proportion of units in a project in buildings completed in 1978 or earlier. In the case of acquired projects, HUD will use the DOFA unless the PHA provides HUD with the actual date of construction completion. When the PHA provides the actual date of construction completion, HUD will use that date (or, for scattered sites, the average dates of construction of all the buildings), subject to a 50-year cap. (Equation coefficient: 4965.4);

(iv) The cost index of rehabilitating property in the area (Equation coefficient: -10608);

(v) The extent to which the units of a project were in a nonmetropolitan area as defined by the United States Bureau of the Census (Census Bureau) during FFY 1996 (Equation coefficient: 2703.9);

(vi) The PHA is located in the Southern census region, as defined by the Census Bureau (Equation coefficient: -269.4);

(vii) The PHA is located in the Western census region, as defined by the Census Bureau (Equation coefficient: -1709.5);

(viii) The PHA is located in the Midwest census region as defined by the Census Bureau (Equation coefficient: 246.2); and

(2) An equation constant of 13851.

(i) *Newly constructed units.* Units with a DOFA date of October 1, 1991, or after, shall be considered to have a zero existing modernization need.

(ii) *Acquired projects.* Projects acquired by a PHA with a DOFA date of October 1, 1991, or after, shall be considered to have a zero existing modernization need.

(3) *For New York City and Chicago Housing Authorities, based on a large sample of direct inspections.* Prior to the cost calibration in paragraph (d)(5) of this section, the number used for the existing modernization need of family projects shall be \$16,680 in New York City and \$24,286 in Chicago, and the number for elderly projects shall be \$14,622 in New York City and \$16,912 in Chicago.

(i) *Newly constructed units.* Units with a DOFA date of October 1, 1991, or after, shall be considered to have a zero existing modernization need.

(ii) *Acquired projects.* Projects acquired by a PHA with a DOFA date of October 1, 1991, or after, shall be considered to have a zero existing modernization need.

(4) *PHAs with fewer than 250 units in FFY 1999.* The estimates of the existing modernization need shall be based on the following:

(i) Objective measurable data concerning the PHA, community, and project characteristics applied to each project:

(A) The average number of bedrooms in the units in a project. (Equation coefficient: 1427.1);

(B) The total number of units in a project. (Equation coefficient: 24.3);

(C) The proportion of units in a project in buildings completed in 1978 or earlier. In the case of acquired projects, HUD shall use the DOFA date unless the PHA provides HUD with the actual date of construction completion, in which case HUD shall use the actual date of construction completion (or, for scattered sites, the average dates of construction of all the buildings), subject to a 50-year cap. (Equation coefficient: -1389.7);

(D) The cost index of rehabilitating property in the area, as of FFY 1999. (Equation coefficient: -20163);

(E) The extent to which the units of a project were in a nonmetropolitan area as defined by the Census Bureau during FFY 1996. (Equation coefficient: 6157.7);

(F) The PHA is located in the Southern census region, as defined by the Census Bureau. (Equation coefficient: 4379.2);

(G) The PHA is located in the Western census region, as defined by the Census Bureau. (Equation coefficient: 3747.7);

(H) The PHA is located in the Midwest census region as defined by the Census Bureau. (Equation coefficient: -2073.5); and

(ii) An equation constant of 24762.

(A) *Newly constructed units.* Units with a DOFA date of October 1, 1991, or after, shall be considered to have a zero existing modernization need.

(B) *Acquired projects.* Projects acquired by a PHA with a DOFA date of October 1, 1991, or after, shall be considered by HUD to have a zero existing modernization need.

(5) *Calibration of existing modernization need for cost index of rehabilitating property in the area.* The estimated existing modernization need determined under paragraphs (d)(1), (2), or (3) of this section shall be adjusted by the values of the cost index of rehabilitating property in the area.

(6) *Freezing of the determination of existing modernization need.* FFY 2008 is the last fiscal year that HUD will calculate the existing modernization need. The existing modernization need will be frozen for all developments at the calculation as of FFY 2008 and will be adjusted for changes in the inventory and paragraph (d)(4) of this section.

(e) *Allocation for accrual needs under the CF formula.* HUD shall allocate the other half of the remaining Capital Fund amount based on the relative accrual needs of PHAs, determined in accordance with this paragraph of this section.

(1) PHAs with 250 or more units, except the New York City and Chicago Housing Authorities. The estimates of the accrual need shall be based on the following:

(i) Objective measurable data concerning the following PHA, community, and project characteristics applied to each project:

(A) The average number of bedrooms in the units in a project. (Equation coefficient: 324.0);

(B) The extent to which the buildings in a project average fewer than 5 units. (Equation coefficient: 93.3);

(C) The age of a project, as determined by the DOFA date. In the case of acquired projects, HUD shall use the DOFA date unless the PHA provides HUD with the actual date of construction completion, in which case HUD shall use the actual date of construction (or, for scattered sites, the average dates of construction of all the buildings), subject to a 50-year cap. (Equation coefficient: -7.8);

(D) Whether the development is a family project. (Equation coefficient: 184.5);

(E) The cost index of rehabilitating property in the area. (Equation coefficient: -252.8);

(F) The extent to which the units of a project were in a nonmetropolitan area as defined by the Census Bureau during FFY 1996. (Equation coefficient: -121.3);

(G) PHA size of 6,600 or more units in FFY 1999. (Equation coefficient: -150.7);

(H) The PHA is located in the Southern census region, as defined by the Census Bureau. (Equation coefficient: 28.4);

(I) The PHA is located in the Western census region, as defined by the Census Bureau. (Equation coefficient: -116.9);

(J) The PHA is located in the Midwest census region as defined by the Census Bureau. (Equation coefficient: 60.7); and

(ii) An equation constant of 1371.9.

(2) *For the New York City and Chicago Housing Authorities, based on a large sample of direct inspections.* Prior to the cost calibration in paragraph (e)(4) of this section the number used for the accrual need of family developments is \$1,395 in New York City, and \$1,251 in Chicago, and the number for elderly developments is \$734 in New York City and \$864 in Chicago.

(3) PHAs with fewer than 250 units. The estimates of the accrual need shall be based on the following:

(i) Objective measurable data concerning the following PHA, community, and project characteristics applied to each project:

(A) The average number of bedrooms in the units in a project. (Equation coefficient: 325.5);

(B) The extent to which the buildings in a project average fewer than 5 units. (Equation coefficient: 179.8);

(C) The age of a project, as determined by the DOFA date. In the case of acquired projects, HUD shall use the DOFA date unless the PHA provides HUD with the actual date of construction completion. When provided with the actual date of construction completion, HUD shall use this date (or, for scattered sites, the average dates of construction of all the buildings), subject to a 50-year cap. (Equation coefficient: -9.0);

(D) Whether the project is a family development. (Equation coefficient: 59.3);

(E) The cost index of rehabilitating property in the area. (Equation coefficient: -1570.5);

(F) The extent to which the units of a project were in a nonmetropolitan area as defined by the Census Bureau during

FFY 1996. (Equation coefficient: -122.9);

(G) The PHA is located in the Southern census region, as defined by the Census Bureau. (Equation coefficient: -564.0);

(H) The PHA is located in the Western census region, as defined by the Census Bureau. (Equation coefficient: -29.6);

(I) The PHA is located in the Midwest census region as defined by the Census Bureau. (Equation coefficient: -418.3); and

(ii) An equation constant of 3193.6.

(4) *Calibration of accrual need for the cost index of rehabilitating property in the area.* The estimated accrual need determined under either paragraph (e)(2) or (3) of this section shall be adjusted by the values of the cost index of rehabilitation.

(f) *Calculation of number of units.* (1) *General.* For purposes of determining the number of a PHA's public housing units and the relative modernization needs of PHAs:

(i) HUD shall count as one unit:

(A) Each public housing and section 23 bond-financed CF unit, except that each existing unit under the Turnkey III program shall count as one-fourth of a unit. Units receiving operating subsidy only shall not be counted.

(B) Each existing unit under the Mutual Help program.

(ii) HUD shall add to the overall unit count any units that the PHA adds to its inventory when the units are under CF ACC amendment and have reached DOFA by the date that HUD establishes for the FFY in which the CF formula is being run (hereafter called the "reporting date"). New CF units and those reaching DOFA after the reporting date shall be counted for CF formula purposes in the following FFY.

(2) *Replacement units.* Replacement units newly constructed on or after October 1, 1998, that replace units in a project funded in FFY 1999 by the Comprehensive Grant formula system or the Comprehensive Improvement Assistance Program (CIAP) formula system shall be given a new CF ACC number as a separate project and shall be treated as a newly constructed development as outlined in § 905.600 of this part.

(3) *Reconfiguration of units.* Reconfiguration of units may cause the need to be calculated by the new configuration based on the formula characteristics in the building and unit's PIC module (refer to the formula sections here). The unit counts will be determined by the CF units existing after the reconfiguration.

(4) *Reduction of units.* For a project losing units as a result of demolition

and disposition, the number of units on which the CF formula is based shall be the number of units reported as eligible for Capital Funds as of the reporting date. Units are eligible for funding until they are removed due to demolition and disposition in accordance with a schedule approved by HUD.

(g) *Computation of formula shares under the CF formula.* (1) *Total estimated existing modernization need.* The total estimated existing modernization need of a PHA under the CF formula is the result of multiplying for each project the PHA's total number of formula units by its estimated existing modernization need per unit, as determined by paragraph (d) of this section, and calculating the sum of these estimated project needs.

(2) *Total accrual need.* The total accrual need of a PHA under the CF formula is the result of multiplying for each project the PHA's total number of formula units by its estimated accrual need per unit, as determined by paragraph (e) of this section, and calculating the sum of these estimated accrual needs.

(3) *PHA's formula share of existing modernization need.* A PHA's formula share of existing modernization need under the CF formula is the PHA's total estimated existing modernization need divided by the total existing modernization need of all PHAs.

(4) *PHA's formula share of accrual need.* A PHA's formula share of accrual need under the CF formula is the PHA's total estimated accrual need divided by the total existing accrual need of all PHAs.

(5) *PHA's formula share of capital need.* A PHA's formula share of capital need under the CF formula is the average of the PHA's share of existing modernization need and its share of accrual need (by which method each share is weighted 50 percent).

(h) *CF formula capping.* (1) For units that are eligible for funding under the CF formula (including replacement housing units discussed below), a PHA's CF formula share shall be its share of capital need, as determined under the CF formula, subject to the condition that no PHA's CF formula share for units funded under the CF formula can be less than 94 percent of its formula share had the FFY 1999 formula system been applied to these CF formula-eligible units. The FFY 1999 formula system is based upon the FFY 1999 Comprehensive Grant formula system for PHAs with 250 or more units in FFY 1999 and upon the FFY 1999 Comprehensive Improvement Assistance Program (CIAP) formula

system for PHAs with fewer than 250 units in FFY 1999.

(2) For a Moving to Work (MTW) PHA whose MTW agreement provides that its CF formula share is to be calculated in accordance with the previously existing formula, the PHA's CF formula share, during the term of the MTW agreement, may be approximately the formula share that the PHA would have received had the FFY 1999 formula funding system been applied to the CF formula eligible units.

(i) *Replacement Housing Factor to reflect formula need for developments with demolition or disposition occurring on or after October 1, 1998, and prior to September 30, 2013.* (1) *RHF generally.* PHAs that have a reduction in the number of units attributable to demolition or disposition of units during the period (reflected in data maintained by HUD) that lowers the formula unit count for the CFF calculation qualify for application of an RHF, subject to satisfaction of criteria stated in paragraph (i)(5) of this section

(2) *When applied.* The RHF will be added, where applicable:

(i) For the first 5 years after the reduction of units described in paragraph (i)(1) of this section; and

(ii) For an additional 5 years if the planning, leveraging, obligation, and expenditure requirements are met. As a prior condition of a PHA's receipt of additional funds for replacement housing provided for the second 5-year period or any portion thereof, a PHA must obtain a firm commitment of substantial additional funds, other than public housing funds, for replacement housing, as determined by HUD.

(3) *Computation of RHF.* The RHF consists of the difference between the CFF share without the CFF share reduction of units attributable to demolition or disposition and the CFF share that resulted after the reduction of units attributable to demolition or disposition.

(4) *Replacement housing funding in FFYs 1998 and 1999.* Units that received replacement housing funding in FFY 1998 will be treated as if they had received 2 years of replacement housing funding by FFY 2000. Units that received replacement housing funding in FFY 1999 will be treated as if they had received one year of replacement housing funding as of FFY 2000.

(5) *PHA Eligibility for the RHF.* A PHA is eligible for this factor only if the PHA satisfies the following criteria:

(i) The PHA will use the funding in question only for replacement housing;

(ii) The PHA will use the restored funding that results from the use of the replacement factor to provide

replacement housing in accordance with the PHA's 5-Year Action Plan, as approved by HUD under part 903 of this chapter as well as the PHA's Board of Commissioners;

(iii) The PHA has not received funding for public housing units that will replace the lost units under Public Housing Development, Major Reconstruction of Obsolete Public Housing, HOPE VI, Choice Neighborhoods, Rental Assistance Payment (RAP), or programs that otherwise provide for replacement with public housing units;

(iv) The PHA, if designated as a troubled PHA by HUD, and not already under the direction of HUD or an appointed receiver, in accordance with part 902 of this chapter, uses an Alternative Management Entity, as defined in part 902 of this chapter, for development of replacement housing and complies with any applicable provisions of its Memorandum of Agreement executed with HUD under that part; and

(v) The PHA undertakes any development of replacement housing in accordance with applicable HUD requirements and regulations.

(6) *Failure to provide replacement housing in a timely fashion.* (i) A PHA will be subject to the actions described in paragraph (i)(7)(ii) of this section if the PHA does not:

(A) Use the restored funding that results from the use of the RHF to provide replacement housing in a timely fashion, as provided in paragraph (i)(7)(i) of this section and in accordance with applicable HUD requirements and regulations, and

(B) Make reasonable progress on such use of the funding, in accordance with applicable HUD requirements and regulations.

(ii) If a PHA fails to act as described in paragraph (i)(6)(i) of this section, HUD will require appropriate corrective action under these regulations, may recapture and reallocate the funds, or may take other appropriate action.

(7) *Requirement to obligate and expend RHF funds within the specified period.* (i) In addition to the requirements otherwise applicable to obligation and expenditure of funds, PHAs are required to obligate assistance received as a result of the RHF within:

(A) 24 months from the date that funds become available to the PHA; or

(B) With specific HUD approval, 24 months from the date that the PHA accumulates adequate funds to undertake replacement housing.

(ii) To the extent the PHA has not obligated any funds provided as a result of the RHF within the time frames

required by this paragraph, or has not expended such funds within a reasonable time, HUD shall recapture the unobligated amount of the grant.

(j) *Demolition and Disposition Transitional Funding (DDTF) to reflect formula need for developments with demolition or disposition on or after October 1, 2013.* (1) *DDTF generally.* In FFY 2014 and thereafter, PHAs that have a reduction in the number of units occurring in FFY 2013 and attributable to demolition or disposition are automatically eligible to receive Demolition and Disposition Transitional Funding. The DDTF will be included in their annual Capital Fund grant for a 5-year period to offset the reduction in funding a PHA would receive from removing units from inventory. DDTF is subject to the criteria stated in paragraph (j)(4) of this section.

(2) *When applied.* DDTF will be added to a PHA's annual CFP grant, where applicable, for 5 years after the reduction of units described in paragraph (j)(1) of this section.

(3) *Computation of DDTF.* The DDTF consists of the difference between the CFF share without the CFF share reduction of units attributable to demolition or disposition and the CFF share that resulted after the reduction of units attributable to demolition or disposition.

(4) *PHA eligibility for the DDTF.* A PHA is eligible for this factor only if the PHA satisfies the following criteria:

(i) The PHA will automatically receive the DDTF for reduction of units in accordance with paragraph (j)(1) of this section, unless the PHA rejects the DDTF funding for that fiscal year in writing;

(ii) The PHA will use the funding in question for eligible activities under the Capital Fund Program, found at 905.200—such as modernization and development—that are included in the PHA's HUD approved CFP 5-Year Action Plan.

(iii) The PHA has not received funding for public housing units that will replace the lost units from disposition proceeds, or under Public Housing Development, Major Reconstruction of Obsolete Public Housing, HOPE VI, Choice Neighborhoods, RAP, or programs that otherwise provide for replacement with public housing units;

(iv) The PHA, if designated as a troubled PHA by HUD, and not already under the direction of HUD or an appointed receiver, in accordance with part 902 of this chapter, uses an Alternative Management Entity, as defined in part 902 of this chapter, and complies with any applicable provisions

of its Memorandum of Agreement executed with HUD under that part; and

(v) The PHA undertakes any eligible activities in accordance with applicable HUD requirements and regulations.

(5) *Requirement to obligate and expend DDTF funds within the specified period.* (i) In addition to the requirements otherwise applicable to obligation and expenditure of Capital Funds, including 42 U.S.C. 1437g(j) and the terms of the appropriation from Congress, PHAs are required to obligate funds received as a result of the DDTF within 24 months from the date that funds become available to the PHA; or

(ii) To the extent the PHA has not obligated any funds provided as a result of the DDTF within the time frames required by this paragraph, or expended such funds within a reasonable time frame, HUD shall reduce the amount of DDTF to be provided to the PHA.

(k) *RHF Transition.* (1) PHAs that would be newly eligible for RHF in FFY 2014 will receive 5 years of DDTF.

(2) PHAs that received a portion of a first increment RHF grant in FY 2013, for units removed from inventory prior to the reporting date of June 30, 2012, will receive up to 10 years of funding consisting of the remainder of first-increment RHF, subject to the requirements of § 905.400(i) of this part, and, if eligible, 5 years of DDTF, subject to the requirements of § 905.400(j) of this part.

(3) PHAs that received a portion of a second increment RHF grant in FY 2013, for units removed from inventory prior to the reporting date of June 30, 2012, will continue to receive the remaining portion of the 5-year increment as a separate second increment RHF grant, as described in § 905.400(i) of this part.

(1) *Performance reward factor.* (1) *High performer.* A PHA that is designated a high performer under the PHA's most recent final PHAS score may receive a performance bonus that is:

(i) Three (3) percent above its base formula amount in the first 5 years these awards are given (for any year in this 5-year period in which the performance reward is earned); or

(ii) Five (5) percent above its base formula amount in future years (for any year in which the performance reward is earned);

(2) *Condition.* The performance bonus is subject only to the condition that no PHA will lose more than 5 percent of its base formula amount as a result of the redistribution of funding from nonhigh performers to high performers.

(3) *Redistribution.* The total amount of Capital Funds that HUD has recaptured

or not allocated to PHAs as a sanction for violation of expenditure and obligation requirements shall be allocated to the PHAs that are designated high performers under PHAS.

■ 6. Add subparts F, G, and H to read as follows:

Subpart F—Development Requirements

Sec.

905.600	General.
905.602	Program requirements.
905.604	Mixed-finance development.
905.606	Development proposal.
905.608	Site acquisition proposal.
905.610	Technical processing.
905.612	Disbursement of Capital Funds—predevelopment costs.

Subpart G—Other Security Interests

905.700	Other security interests.
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Subpart H—Compliance, HUD Review, Penalties, and Sanctions

905.800	Compliance.
905.802	HUD review of PHA performance.
905.804	Sanctions.

Subpart F—Development Requirements

§ 905.600 General.

(a) *Applicability.* This subpart F applies to the development of public housing units to be included under an ACC and which will receive funding from public housing funds. PHAs must comply, or cause the Owner Entity and its contractors to comply, as applicable, with all of the applicable requirements in this subpart. Pursuant to § 905.106 of this part, when a PHA, a PHA partner, and/or an Owner Entity submits a development proposal and, if applicable, a site acquisition proposal, and executes an ACC covering the public housing units being developed, it is deemed to have certified by those executed submissions its compliance with this subpart. Noncompliance with any provision of this subpart or other applicable statutes or regulations, or the ACC Amendment, and any amendment thereto may subject the PHA, the PHA's partner and/or the Owner Entity to sanctions contained in § 905.804 of this part.

(b) *Description.* A PHA may develop public housing through the construction of new units or the acquisition, with or without rehabilitation, of existing units. A PHA may use any generally accepted method of development including, but not limited to:

(1) *Conventional.* The PHA designs a project on a property it owns. The PHA then competitively selects an entity to build or rehabilitate the project.

(2) *Turnkey.* The PHA advertises for and competitively selects a developer

who will develop public housing units on a site owned or to be owned by the developer. Following HUD approval of the development proposal, the PHA and the developer execute a contract of sale and the developer builds the project. Once the project is complete, the developer sells it to the PHA.

(3) *Acquisition with or without rehabilitation.* The PHA acquires an existing property that requires substantial, moderate, or no repair. Any repair work is done by PHA staff or contracted out by the PHA. The PHA must certify that the property was not constructed with the intent of selling it to the PHA or, alternatively, the PHA must certify that HUD requirements were followed in the development of the property.

(4) *PHA use of force account labor.* The PHA uses staff to carry out new construction or rehabilitation, as provided in § 905.314(j) of this part.

(5) *Mixed finance.* Development or modernization of public housing units where the public housing units are owned in whole or in part by an entity other than a PHA, pursuant to Section 905.604.

(c) *Development process.* The general development process for public housing development, using any method and with any financing, is as follows:

(1) The PHA will identify a site to be acquired or a public housing project to be developed or redeveloped. The PHA or its Partner and/or the Owner Entity will prepare a site acquisition proposal pursuant to § 905.608 of this part and/or a development proposal pursuant to § 905.606 of this part for submission to HUD or as otherwise directed by HUD. The PHA may request predevelopment funding necessary for preparation of the acquisition proposal and/or development proposal, as stated in § 905.612(a) of this part.

(2) The PHA must consult with affected residents prior to submission of an acquisition proposal, development proposal, or both to HUD to solicit resident input into development of the public housing project.

(3) After HUD approval of the site acquisition proposal and/or development proposal, HUD and the PHA shall execute the applicable ACC Amendment for the public housing units and record a Declaration of Trust or Declaration of Restrictive Covenants on all property acquired and/or to be developed. The PHA may then commence development of the units.

(4) Upon completion of the public housing project, the PHA will establish the DOFA. After the DOFA, the PHA will submit a cost certificate to HUD

attesting to the actual cost of the project that will be subject to audit.

(d) *Funding sources.* A PHA may engage in development activities using any one or a combination of the following sources of funding:

- (1) Capital Funds;
- (2) HOPE VI funds;
- (3) Choice Neighborhoods funds;
- (4) Proceeds from the sale of units under a homeownership program in accordance with 24 CFR part 906;
- (5) Proceeds resulting from the disposition of PHA-owned land or improvements;
- (6) Private financing used in accordance with § 905.604 of this part, Mixed-finance development;
- (7) Capital Fund Financing Program (CFFP) proceeds under § 905.500 of this part;
- (8) Proceeds resulting from an Operating Fund Financing Program (OFFP) approved by HUD pursuant to 24 CFR part 990; and
- (9) Funds available from any other eligible sources.

§ 905.602 Program requirements.

(a) *Local cooperation.* Except as provided under § 905.604(i) of this part for mixed-finance projects, the PHA must enter into a Cooperation Agreement with the applicable local governing body that includes sufficient authority to cover the public housing being developed under this subpart, or provide an opinion of counsel that the existing, amended, or supplementary Cooperation Agreement between the jurisdiction and the PHA includes the project or development.

(b) *New construction limitation.* These requirements apply to the development (including new construction and acquisition) of public housing. All proposed new development projects must meet both of the following requirements:

(1) *Limitation on the number of units.* A PHA may not use Capital Funds to pay for the development cost of public housing units if such development would result in a net increase in the number of public housing units that the PHA owned, assisted, or operated on October 1, 1999. Subject to approval by the Secretary, a PHA may develop public housing units in excess of the limitation if:

- (i) The units are available and affordable to eligible low-income families and the CF formula does not provide additional funding for the specific purpose of constructing, modernizing, and operating such excess units; or
- (ii) The units are part of a mixed-finance project or otherwise leverage

significant additional investment, and the cost of the useful life of the projects is less than the estimated cost of providing tenant-based assistance under section 8(o) of the 1937 Act.

(2) *Limitations on cost.* A PHA may not construct public housing unless the cost of construction is less than the cost of acquisition or acquisition and rehabilitation of existing units, including the amount required to establish, as necessary, an upfront reserve for replacement accounts for major repairs. A PHA shall provide evidence of compliance with this subpart either by:

(i) Demonstrating through a cost comparison that the cost of new construction in the neighborhood where the PHA proposes to construct the housing is less than the cost of acquisition of existing housing, with or without rehabilitation, in the same neighborhood; or

(ii) Documenting that there is insufficient existing housing in the neighborhood to acquire.

(c) *Existing PHA-owned nonpublic housing properties.* Nonpublic housing properties may be used in the development of public housing units provided all requirements of the 1937 Act and the development requirements of this part are met.

(d) *Site and neighborhood standards.* Each proposed site to be newly acquired for a public housing project or for construction or rehabilitation of public housing must be reviewed and approved by the field office as meeting the following standards, as applicable:

(1) The site must be adequate in size, exposure, and contour to accommodate the number and type of units proposed. Adequate utilities (e.g., water, sewer, gas, and electricity) and streets shall be available to service the site.

(2) The site and neighborhood shall be suitable to facilitating and furthering full compliance with the applicable provisions of title VI of the Civil Rights Act of 1964, title VIII of the Civil Rights Act of 1968, Executive Order 11063, and HUD regulations issued under these statutes.

(3) The site for new construction shall not be located in an area of minority concentration unless:

(i) There are already sufficient, comparable opportunities outside areas of minority concentration for housing minority families in the income range that is to be served by the proposed project; or

(ii) The project is necessary to meet overriding housing needs that cannot feasibly be met otherwise in that housing market area. "Overriding housing needs" shall not serve as the

basis for determining that a site is acceptable if the only reason that these needs cannot otherwise feasibly be met is that, due to discrimination because of race, color, religion, creed, sex, disability, familial status, or national origin, sites outside areas of minority concentration are unavailable.

(4) The site for new construction shall not be located in a racially mixed area if the project will cause a significant increase in the proportion of minority to nonminority residents in the area.

(5) Notwithstanding the foregoing, after demolition of public housing units a PHA may construct public housing units on the original public housing site or in the same neighborhood if the number of replacement public housing units is significantly fewer than the number of public housing units demolished. One of the following criteria must be satisfied:

(i) The number of public housing units being constructed is not more than 50 percent of the number of public housing units in the original development; or

(ii) In the case of replacing an occupied development, the number of public housing units being constructed is the number needed to house current residents who want to remain at the site, so long as the number of public housing units being constructed is significantly fewer than the number being demolished; or

(iii) The public housing units being constructed constitute no more than 25 units.

(6) The site shall promote greater choice of housing opportunities and avoid undue concentration of assisted persons in areas containing a high proportion of low-income persons.

(7) The site shall be free from adverse environmental conditions, natural or manmade, such as: Toxic or contaminated soils and substances; mudslide or other unstable soil conditions; flooding; septic tank backups or other sewage hazards; harmful air pollution or excessive smoke or dust; excessive noise or vibrations from vehicular traffic; insect, rodent, or vermin infestation; or fire hazards. The neighborhood shall not be seriously detrimental to family life. It shall not be filled with substandard dwellings nor shall other undesirable elements predominate, unless there is a concerted program in progress to remedy the undesirable conditions.

(8) The site shall be accessible to social, recreational, educational, commercial, and health facilities; health services; and other municipal facilities and services that are at least equivalent to those typically found in

neighborhoods consisting largely of similar unassisted standard housing. The availability of public transportation must be considered.

(9) The site shall be accessible to a range of jobs for low-income workers and for other needs. The availability of public transportation must be considered, and travel time and cost via public transportation and private automobile must not be excessive. This requirement may be given less consideration for elderly housing.

(10) The project may not be built on a site that has occupants unless the relocation requirements at § 905.308(b)(9) of this part are met.

(11) The site shall not be in an area that HUD has identified as having special flood hazards and in which the sale of flood insurance has been made available under the National Flood Insurance Act of 1968, unless the development is covered by flood insurance required by the Flood Disaster Protection Act of 1973 and meets all applicable HUD standards and local requirements.

(e) *Relocation.* All acquisition or rehabilitation activities carried out with public housing funds must comply with the provisions of § 905.308(b)(9).

(f) *Environmental requirements.* All activities under this part are subject to an environmental review by a responsible entity under HUD's environmental regulations at 24 CFR Part 58 and must comply with the requirements of the National Environmental Policy Act of 1969 (NEPA) (42 U.S.C. 4321 *et seq.*) and the related laws and authorities listed at 24 CFR 58.5. HUD may make a finding in accordance with 24 CFR 58.11 and may perform the environmental review itself under the provisions of 24 CFR Part 50. In those cases where HUD performs the environmental review under 24 CFR Part 50, it will do so before approving a proposed project, and will comply with the requirements of NEPA and the related requirements at 24 CFR 50.4.

§ 905.604 Mixed-finance development.

(a) *General.* Mixed-finance development refers to the development (through new construction or acquisition, with or without rehabilitation) or modernization of public housing, where the public housing units are owned in whole or in part by an entity other than a PHA. If the public housing units being developed are 100 percent owned by the PHA, the project is not a mixed-finance project and will be not be subject to mixed-finance development requirements. However, all other development requirements of part 905

are applicable, and, if the project includes both public housing funds and private funding for development, the project may be subject to other applicable program requirements; e.g., the Capital Fund Financing Program, Operating Fund Financing Program, Public Housing Mortgage Program, etc.

(1) *Ownership.* There are various potential scenarios for the ownership structure of a mixed-finance project, such as: public housing units may be owned entirely by a private entity; a PHA may co-own with a private entity; or a PHA affiliate or instrumentality may own or co-own the units.

(2) *Partnerships.* PHAs may choose to enter into a partnership or other contractual arrangement with a third party entity for the mixed-finance development and/or ownership of public housing units.

(3) *Funding.* Funding for mixed-finance developments may include one or a combination of funding sources, pursuant to § 905.600(d) of this part.

(4) *Modernization.* A mixed-finance project that involves modernization, rather than new construction, shall maintain the DOFA date that existed prior to modernization and shall be subject to the provisions of § 905.304(a)(2) of this part regarding the applicable period of obligation to operate the public housing units.

(b) *Definitions applicable to this subpart.* (1) *Mixed-finance.* The development (through new construction or acquisition, with or without rehabilitation) or modernization of public housing, using public housing, nonpublic housing, or a combination of public housing and nonpublic housing funds, where the public housing units are owned in whole or in part by an entity other than the PHA. A mixed-finance development may include 100 percent public housing (if there is an Owner Entity other than the PHA) or a mixture of public housing and nonpublic housing units.

(2) *Owner Entity.* As defined in § 905.108 of this part.

(3) *PHA instrumentality.* An instrumentality is an entity related to the PHA whose assets, operations, and management are legally and effectively controlled by the PHA, and through which PHA functions or policies are implemented, and which utilizes public housing funds or public housing assets for the purpose of carrying out public housing development functions of the PHA. An instrumentality assumes the role of the PHA, and is the PHA under the Public Housing Requirements, for purposes of implementing public housing development activities and programs, and must abide by the Public

Housing Requirements. Instrumentalities must be authorized to act for and to assume such responsibilities. For purposes of development, ownership of public housing units by an instrumentality would be considered mixed-finance development.

(4) *PHA affiliate.* An affiliate is an entity, other than an instrumentality, formed by a PHA and in which a PHA has a financial or ownership interest or participates in its governance. The PHA has some measure of control over the assets, operations, or management of the affiliate, but such control does not rise to the level of control to qualify the entity as an instrumentality. For the purposes of development, ownership of public housing units by an affiliate would be considered mixed-finance development.

(5) *Public housing funds.* As defined in § 905.108 of this part.

(c) *Structure of projects.* Each mixed-finance project must be structured to:

(1) Ensure the continued operation of the public housing units in accordance with all Public Housing Requirements;

(2) Ensure that public housing funds committed to a mixed-finance project are used only to pay for costs associated with the public housing units, including such costs as demolition, site work, infrastructure, and common area improvements.

(3) To ensure that the amount of public housing funds committed to a project is proportionate to the number of public housing units contained in the project. To meet this "pro rata test," the proportion of public housing funds compared to total project funds committed to a project must not exceed the proportion of public housing units compared to total number of units contained in the project. For example, if there are a total of 120 units in the project and 50 are public housing units, the public housing units are 42 percent of the total number of units in the project. Therefore the amount of public housing funds committed to the project cannot exceed 42 percent of the total project budget, unless otherwise approved by the Secretary. However, if public housing funds are to be used to pay for more than the pro rata cost of common area improvements, HUD will evaluate the proposal to ensure that common area improvements will benefit the residents in the development in a mixed-income project; and

(4) Ensure that the project is within the Total Development Cost (TDC) and Housing Construction Cost (HCC) limits pursuant to § 905.314(c) and (d) of this part.

(d) *Process.* Except as provided in this section, development of a mixed-finance project under this subpart is subject to the same requirements as development of public housing by a PHA entirely with public housing funds, as stated in § 905.600 of this part. PHAs must submit an acquisition proposal under § 905.608 and/or a development proposal under § 905.606 or as otherwise specified by HUD.

(e) *Conflicts.* In the event of a conflict between the requirements for a mixed-finance project and other requirements of this subpart, the mixed-finance Public Housing Requirements shall apply, unless HUD determines otherwise.

(f) *HUD approval.* For purposes of this section only, any action or approval that is required by HUD pursuant to the requirements set forth in this section shall be construed to mean HUD Headquarters, unless the field office is authorized in writing by Headquarters to carry out a specific function in this section.

(g) *Comparability.* Public housing units built in a mixed-financed development must be comparable in size, location, external appearance, and distribution to nonpublic housing units within the development.

(h) *Mixed-finance procurement.* The requirements of 24 CFR Part 85 and 24 CFR 905.316 are applicable to this subpart with the following exceptions:

(1) PHAs may select a development partner using competitive proposals procedures for qualifications-based procurement, subject to negotiation of fair and reasonable compensation and compliance with TDC and other applicable cost limitations;

(2) An Owner Entity (which, as a private entity, would normally not be subject to 24 CFR Part 85) shall be required to comply with 24 CFR Part 85 if HUD determines that the PHA or PHA instrumentality, or either of their members or employees, exercises significant decision making functions within the Owner Entity with respect to managing the development of the proposed units. HUD may, on a case-by-case basis, exempt such an Owner Entity from the need to comply with 24 CFR Part 85 if it determines that the Owner Entity has developed an acceptable alternative procurement plan.

(i) *Identity of interest.* If the Owner Entity or partner (or any other entity with an identity of interest with the Owner Entity or partner) of a mixed-finance project wants to serve as the general contractor for the mixed-finance project, it may award itself the construction contract only if:

(1) The identity of interest general contractor's bid is the lowest bid submitted in response to a request for bids; or

(2) The PHA submits a written justification to HUD that includes an independent third-party cost estimate that demonstrates that the identity of interest general contractor's costs are less than or equal to the independent third-party cost estimate; and

(3) HUD approves the identity of interest general contractor in conjunction with HUD's approval of the development proposal for the mixed-finance project.

(j) *Operating Subsidy-Only and Capital Fund-Only Assistance.* (1) *General.* This section refers to the mixed-finance development of public housing units that will be developed without public housing funds but will receive operating subsidy, or will be developed with public housing funds but will not receive operating subsidy.

(2) *Operating Subsidy-Only Development.* Operating Subsidy-Only Development refers to mixed-finance projects where public housing units are developed without the use of public housing funds, but for which HUD agrees to provide operating subsidies under Section 9(e) of the 1937 Act. These types of project are subject to the following provisions:

(i) The newly developed public housing units will be included in the calculation of the Capital Fund formula in § 905.400 of this part.

(ii) An ACC Amendment will be executed to include the new public housing units. The term of the ACC Amendment will be determined based on the assistance as provided in § 905.304, unless reduced by the Secretary.

(iii) There shall be no disposition of the public housing units without the prior written approval of HUD, during, and for 10 years after the end of, the period in which the public housing units receive operating subsidy from the PHA, as required by 42 U.S.C. 1437g(3), as those requirements may be amended from time to time. However, if the PHA is no longer able to provide operating subsidies to the Owner Entity pursuant to Section 9(e) of the 1937 Act, the PHA may (on behalf of the Owner Entity) request that HUD terminate the Declaration of Trust or Declaration of Restrictive Covenants, as applicable. Termination under this section does not require disposition approval from HUD pursuant to Section 18 of the 1937 Act, 42 U.S.C. 1437p. However, the PHA must provide public housing residents with a decent, safe, sanitary, and affordable unit to which they can

relocate, which may include a public housing unit in another development or a Housing Choice Voucher, and pay for the tenant's reasonable moving costs. The URA is not applicable in this situation.

(iv) Where the PHA elects in the future to use public housing funds for modernization of these units, the PHA must execute an ACC Amendment with a 20-year use restriction and record a Declaration of Trust or Declaration of Restrictive Covenants, in accordance with § 905.304. There may be no disposition of the public housing units without the prior written approval of HUD during the 20-year period, and the public housing units shall be maintained and operated in accordance with all applicable Public Housing Requirements (including the ACC), as those requirements may be amended from time to time.

(3) *Capital Fund-Only Development.* Capital Fund-Only projects refers to mixed-finance projects where a PHA and its partners may develop public housing units using public housing funds for development of new units, but for which HUD will not be providing operating subsidy under Section 9(e) of the Act, 42 U.S.C. 1437g(e). These types of projects are subject to the following provisions:

(i) The newly developed public housing units will not be included in the calculation of the Operating Fund formula.

(ii) The PHA must sign an ACC Amendment, with a 40-year use restriction, for development of new units and record a Declaration of Trust or Declaration of Restrictive Covenants in accordance with § 905.304 of this part, unless the time period is reduced by the Secretary.

(iii) There shall be no disposition of the public housing units, without the prior written approval of HUD, during a 40-year period, and the public housing units shall be maintained and operated in accordance with all applicable Public Housing Requirements (including the ACC), as required by section 9(d)(3) of the 1937 Act, 42 U.S.C. 1437g(d)(3), as those requirements may be amended from time to time.

(4) *Procedures.* PHAs must follow the development approval process identified in § 905.600.

(k) *Mixed-finance operations: Deviation from HUD requirements pursuant to section 35(h) of the 1937 Act, 42 U.S.C. 1437z-7(h).* (1) *Deviation.* If a PHA enters into a contract with an entity that owns or operates a mixed-finance project, and the terms of the contract obligate the entity to operate and maintain a specified number of

units in the project as public housing units, the contract may include terms that allow the Owner Entity to deviate from otherwise applicable Public Housing Requirements regarding rents, income eligibility, and other areas of public housing management with respect to all or a portion of the public housing units, subject to the following conditions:

(i) There are a significant number of units in the mixed-finance project that are not public housing units;

(ii) There is a reduction in appropriations under Section 9(e) of the 1937 Act (see 42 U.S.C. 1437g(e)) or a change in applicable law that results in the PHA being unable to fulfill its contractual obligation to the Owner Entity with respect to the public housing units;

(iii) Prior to implementation of the contractual terms related to deviation from the Public Housing Requirements, HUD approves an Alternative Management Plan for the mixed-finance project; and

(iv) The deviation shall be to the extent necessary to preserve the viability of those units while maintaining the low-income character of the units to the maximum extent practicable.

(2) *Preparation of an Alternative Management Plan.* Should the PHA and the Owner Entity determine a need to deviate from the Public Housing Requirements, the PHA, on behalf of the Owner Entity, must submit an Alternative Management Plan to HUD for review and approval prior to implementation of any changes. The Plan must include the following:

(i) A statement describing the Owner Entity's reasons for deviating from the Public Housing Requirements;

(ii) An explanation of the Owner Entity's proposed remedies, including, but not limited to:

(A) How the Owner Entity will select the residents (including the number and income levels of the families proposed to be admitted to the public housing units) and units to be affected by the proposed change;

(B) The Owner Entity's timetable for implementing the Alternative Management Plan;

(C) The impact on existing residents. Note that for any resident who is unable to remain in the unit as a result of implementation of the Alternative Management Plan, the resident must be relocated to a public housing unit or given a Housing Choice Voucher by the PHA or by another entity as provided for in the contractual agreement between the PHA and the Owner Entity;

(iii) An amendment to the existing contractual agreement between the PHA and the Owner Entity that includes provisions which ensure that:

(A) An update on the Alternative Management Plan is submitted annually to HUD to ensure that implementation of the provisions of the Alternative Management Plan continue to be appropriate;

(B) The Owner Entity complies with the requirements of this subpart in its management and operation of the public housing units in accordance with the Alternative Management Plan;

(C) The Owner Entity provides the PHA any income that is generated by the public housing units in excess of the Owner Entity's expenses on behalf of those units, as a result of implementation of provisions in the Alternative Management Plan;

(D) The Owner Entity reinstates all Public Housing Requirements (including rent and income eligibility requirements) with respect to the original number of public housing units and number of bedrooms in the mixed-finance development, following the PHA's reinstatement of operating subsidies at the level originally agreed to in its contract with the Owner Entity; and

(iv) Additional evidence. The PHA must provide documentation that:

(A) The Owner Entity has provided copies of the Alternative Management Plan to residents of the project and provided the opportunity for review and comment prior to submission to HUD. The Owner Entity must have provided written notice to each of the public housing residents in the mixed-finance development of its intention to implement the Alternative Management Plan. Such notice must comply with all relevant federal, state, and local substantive and procedural requirements and, at a minimum, provide public housing residents 90 days advance notice of any proposal to increase rents or to relocate public housing residents to alternative housing;

(B) The revenues being generated by the public housing units (in combination with the reduced allocation of Operating Subsidy resulting primarily from a reduction in appropriations or changes in applicable law such that the PHA is unable to comply with its contractual obligations to the Owner Entity) are inadequate to cover the reasonable and necessary operating expenses of the public housing units. Documentation should include a financial statement showing actual operating expenses and revenues over the past 5 years and the projected

expenses and revenues over the next 10 years;

(C) A demonstration that the PHA cannot meet its contractual obligation, and;

(D) The Owner Entity has attempted to offset with regard to the project, the impact of reduced operating subsidies or changes in applicable law by all available means; including the use of other public and private development resources, the use of cash flow from any nonpublic housing units, and funds from other operating deficient reserves.

(3) *HUD review.* HUD will review the Alternative Management Plan to ensure that the plan meets the requirements of this subpart and that any proposed deviation from the Public Housing Requirements will be implemented only to the extent necessary to preserve the viability of the public housing units. Upon completion of HUD's review, HUD will either approve or disapprove the Alternative Management Plan. Reasons for HUD disapproval may include, but are not limited to, the following:

(i) The justification for deviation from the Public Housing Requirements does not qualify in accordance with section 35(h) of the Act (42 U.S.C. 1437z-7(h)).

(ii) The proposed deviation(s) from the Public Housing Requirements are not limited to preserving the viability of the public housing units.

(iii) The information that HUD requires to be included in the Alternative Management Plan has not been included, is not accurate, or does not support the need for deviation from the Public Housing Requirements.

(iv) HUD has evidence that the proposed Alternative Management Plan is not in compliance with other federal requirements, including civil rights laws.

(4) *HUD reevaluation and reapproval.* The PHA, on behalf of the Owner Entity, must provide to HUD, for HUD approval, an annual update on the implementation of the Alternative Management Plan. The update must provide the status of the project and whether the circumstances originally triggering the need for the conditions contained in the Alternative Management Plan remain valid and appropriate. Any proposed changes in the Alternative Management Plan should also be identified. Once the annual update of the Alternative Management Plan is properly submitted, the existing Alternative Management Plan shall remain in effect until such time as HUD takes additional action to approve or disapprove the annual update.

§ 905.606 Development proposal.

(a) *Development proposal.* Prior to developing public housing, either through new construction or through acquisition, with or without rehabilitation, a PHA must submit a development proposal to HUD in the form prescribed by HUD, which will allow HUD to assess the viability and financial feasibility of the proposed development. A development proposal must be submitted for all types of public housing development, including mixed-finance. Failure to submit and obtain HUD approval of a development proposal may result in the public housing funds used in conjunction with the project being deemed ineligible expenses. In determining the amount of information to be submitted by the PHA, HUD shall consider whether the documentation is required for HUD to carry out mandatory statutory, regulatory, or Executive order reviews; the quality of the PHA's past performance in implementing development projects under this subpart; the PHA's demonstrated administrative capability; and other program requirements. The development proposal shall include some or all of the following documentation, as deemed necessary by HUD.

(1) *Project description.* A description of the proposed project, including:

(i) Proposed development method (e.g., mixed-finance, new construction, acquisition with or without rehabilitation, turnkey, etc.), including the extent to which the PHA will use force account labor and use procured contractors. For new construction projects, the PHA must meet the program requirements contained in § 905.602. For projects involving acquisition of existing properties less than 2 years old, the PHA must include an attestation from the PHA and the owner of the property that the property was not constructed with the intent that it would be sold to the PHA or, if it was constructed with the intent that it be sold to the PHA, that it was constructed in compliance with all applicable requirements (e.g., Davis Bacon wage rates, accessibility, etc.);

(ii) Type of residents to occupy the units (e.g., family, elderly, persons with disabilities, or families that include persons with disabilities);

(iii) Number and type of unit (detached, semidetached, row house, walkup, elevator), with bedroom count, broken out by public housing vs. nonpublic housing, if applicable;

(iv) The type and size of nondwelling space, if applicable; and

(v) Schematic drawings of the proposed buildings, unit plans, and additional information regarding plans and specifications, as needed by HUD to review the project.

(2) *Site information.* An identification and description of the proposed site and neighborhood, a site plan, and a map of the neighborhood.

(3) *Participant description.* Identification of participating parties and a description of the activities to be undertaken by each of the participating parties and the PHA; and the legal and business relationships between the PHA and each of the participating parties, as applicable.

(4) *Development project schedule.* A schedule for the development project that includes each major stage of development, through and including the submission of an Actual Development Cost Certificate to HUD.

(5) *Accessibility.* A PHA must provide sufficient information for HUD to determine that dwelling units and other public housing facilities meet accessibility requirements specified at § 905.312 of this part, including, but not limited to, the number, location, and bedroom size distribution of accessible dwelling units (see 24 CFR 8.32 and 24 CFR part 40).

(6) *Project costs.* (i) *Budgets.* To allow HUD to assess sources of funding and projected uses of funds, the PHA shall submit a project budget, in the form prescribed by HUD, reflecting the total permanent development budget for the project, including all sources and uses of funds, including hard and soft costs. The PHA shall also submit a budget for the construction period and a construction draw schedule showing the timing of construction financing contributions and disbursements. In addition, the PHA shall submit an independent construction cost estimate or actual construction contract that supports the permanent and construction budgets.

(ii) *TDC calculation.* The PHA must submit a calculation of the TDC and HCC, subject to § 905.314 of this part.

(iii) *Financing.* A PHA must submit a detailed description of all financing necessary for the implementation of the project, specifying the sources and uses. In addition, HUD may require documents related to the financing (e.g., loan documents, partnership or operating agreement, regulatory and operating agreement, etc.) to be submitted in final draft form as part of the development proposal. Upon financial closing, HUD may also require final, executed copies of these documents to be submitted to HUD for

final approval, per § 905.612(b)(2) of this part.

(A) *Commitment of funds.* Documents submitted pursuant to this section must irrevocably commit funds to the project. Irrevocability of funds means that binding legal documents—such as loan agreements, mortgages, deeds of trust, partnership agreements or operating agreements, or similar documents committing funds—have been executed by the applicable parties; though disbursement of such funds may be subject to meeting progress milestones, the absence of default, and/or other conditions generally consistent with similar non-public housing transactions. For projects involving revolving loan funds, the irrevocability of funds means that funds in an amount identified to HUD as the maximum revolving loan have been committed pursuant to legally binding documents; though disbursement of such funds may be subject to meeting progress milestones, the absence of default, and/or other conditions generally consistent with similar affordable housing transactions. The PHA must confirm the availability of each party's financing, the amount and source of financing committed to the proposal by the parties, and the irrevocability of those funds.

(B) *Irrevocability of funds.* To ensure the irrevocable nature of the committed funds, the PHA shall review the legal documents committing such funds to ensure that the progress milestones and conditions precedent contained in such contracts are generally consistent with similar affordable housing transactions; that the PHA and/or its Owner Entity know of no impediments that would prevent the project from moving forward consistent with the project milestones and conditions precedent; and, after conducting sufficient due diligence, that such documents are properly executed by persons or entities legally authorized to bind the entity committing such funds.

(C) *Third-party documents.* The PHA is not required to ensure the availability of funds by enforcing documents to which it is not a party.

(D) *Opinion of counsel.* As part of the proposal, the PHA may certify as to the irrevocability of funds through the submission of an opinion of the PHA's counsel attesting that counsel has examined the availability of the participating parties' financing, and the amount and source of financing committed to the project by the participating parties, and has determined that such financing has been irrevocably committed, as defined in paragraph (a)(6)(iii)(A) of this section, and that such commitments are

consistent with the project budget submitted under paragraph (a)(6)(i) of this section.

(7) *Operating pro-forma/Operating Fund methodology.* To allow HUD to assess the financial feasibility of projects, PHAs shall submit a 10-year operating pro-forma, including all assumptions, to assure that operating expenses do not exceed operating income. For mixed-finance development, the PHA must describe its methodology for providing and distributing operating subsidy to the Owner Entity for the public housing units.

(8) *Local Cooperation Agreement.* A PHA may elect to exempt all public housing units in a mixed-finance project from the payment in lieu of taxes provisions under section 6(d) of the Act, 42 U.S.C. 1437d(d), and from the finding of need and cooperative agreement provisions under sections 5(e)(1)(ii) and (e)(2) of the Act, 42 U.S.C. 1437c(e)(1)(ii) and (e)(2), and instead subject units to local real estate taxes, but only if the PHA provides documentation from an authorized official of the local jurisdiction that development of the units is consistent with the jurisdiction's comprehensive housing affordability strategy. If the PHA does not elect this exemption, the Cooperation Agreement as provided in § 905.602(a) is required and must be submitted.

(9) *Environmental requirements.* The PHA must provide an approved Request for Release of Funds and environmental certification, submitted in accordance with 24 CFR part 58, or approval in accordance with 24 CFR part 50. HUD will not approve a development proposal without the appropriate environmental approval.

(10) *Market analysis.* For a mixed-finance development that includes nonpublic housing units, the PHA must include an analysis of the projected market for the proposed project.

(11) *Program income and fees.* The PHA must provide information identifying fees to be paid to the PHA, the PHA's partner(s), the Owner Entity, and/or other participating parties identified by HUD and on the receipt and use of program income.

(b) *Additional HUD-requested information.* PHAs are required to provide any additional information that HUD may need to assess the development proposal.

§ 905.608 Site acquisition proposal.

(a) *Submission.* When a PHA determines that it is necessary to acquire vacant land for development of public housing through new

construction, using public housing funds, prior to submission and approval of a development proposal under § 905.606 of this part, the PHA must submit an acquisition proposal to HUD for review and approval prior to acquisition. The acquisition proposal shall include the following:

(b) *Justification*. A justification for acquiring property prior to development proposal submission and approval.

(c) *Description*. A description of the property (i.e., the proposed site and/or project) to be acquired.

(d) *Project description; site and neighborhood standards*. An identification and description of the proposed project, site plan, and neighborhood, together with information sufficient to enable HUD to determine that the proposed site meets the site and neighborhood standards at § 905.602(d) of this part.

(e) *Zoning*. Documentation that the proposed project is permitted by current zoning ordinances or regulations, or evidence to indicate that needed rezoning is likely and will not delay the project.

(f) *Appraisal*. Documentation attesting that an appraisal of the proposed property by an independent, state certified appraiser has been conducted and that the acquisition is in compliance with § 905.308(b)(9) of this part. The purchase price of the site/property may not exceed the appraised value without HUD approval.

(g) *Schedule*. A schedule of the activities to be carried out by the PHA.

(h) *Environmental assessment*. An environmental review or request for HUD to perform the environmental review pursuant to § 905.308(b)(2) of this part.

§ 905.610 Technical processing.

(a) *Review*. HUD shall review all development proposals and site acquisition proposals for compliance with the statutory, Executive order, and regulatory requirements applicable to the development of public housing and the project. HUD's review will evaluate whether the proposed sources and uses of funds are eligible and reasonable, and whether the financing and other documentation establish to HUD's satisfaction that the development is financially viable and structured so as to adequately protect the federal investment of funds in the development. For this purpose, HUD will consider the PHA's proposed methodology for allocating operating subsidies on behalf of the public housing units, the projected revenue to be generated by any nonpublic housing units in a mixed-finance development, and the 10-

year operating pro forma and other information contained in the development proposal.

(b) *Subsidy layering analysis*. After the PHA submits the documentation required under paragraph (a) of this section, HUD or its designee (e.g., the State Housing Finance Agency) shall carry out a subsidy layering analysis, pursuant to section 102(d) of the Department of Housing and Urban Development Reform Act of 1989 (42 U.S.C. 3545) (see 24 CFR part 4), to determine that the amount of assistance being provided for the development is not more than necessary to make the assisted activity feasible after taking into account the other governmental assistance.

(c) *Safe harbor standards*. For mixed-finance projects, in order to expedite the mixed-finance review process and control costs, HUD may make available safe harbor and maximum fee ranges for a number of costs. If a project is at or below a safe harbor standard, no further review will be required by HUD. If a project is above a safe harbor standard, additional review by HUD will be necessary. In order to approve terms above the safe harbor, the PHA must demonstrate to HUD in writing that the negotiated terms are appropriate for the level of risk involved in the project, the scope of work, any specific circumstances of the development, and the local or national market for the services provided.

(d) *Approval*. If HUD determines that a site acquisition proposal or a development proposal is approvable, HUD shall notify the PHA in writing of its approval. The HUD approval of a development proposal will include the appropriate form of ACC for signature. The PHA must execute the ACC and return it to HUD for execution. Until HUD approves a development proposal, a PHA may only expend public housing funds for predevelopment costs, as provided in § 905.612 of this part.

(e) *Amendments to approved development proposals*. HUD must approve any material change to an approved development proposal. HUD defines material change as:

(1) A change in the number of public housing units;

(2) A change in the number of bedrooms by an increase/decrease of more than 10 percent;

(3) A change in cost or financing by an increase/decrease of more than 10 percent; or

(4) A change in the site.

§ 905.612 Disbursement of Capital Funds—predevelopment costs.

(a) *Predevelopment costs*. After a new development project has been included in the CFP 5-Year Action Plan that has been approved by the PHA Board of Commissioners and HUD, a PHA may use funding for predevelopment expenses. Predevelopment funds may be expended in accordance with the following requirements:

(1) Predevelopment assistance may be used to pay for materials and services related to proposal development and project soft costs. It may also be used to pay for costs related to the demolition of units on a proposed site. Absent HUD approval, predevelopment assistance may not be used to pay for site work, installation of infrastructure, construction, or other hard costs related to a development.

(2) For non-mixed-finance projects, predevelopment funding up to 5 percent of the total amount of the public housing funds committed to a project does not require HUD approval. HUD shall determine on a case-by-case basis that an amount greater than 5 percent may be drawn down by a PHA to pay for necessary and reasonable predevelopment costs, based upon a consideration of the nature and scope of activities proposed to be carried out by the PHA. Before a request for predevelopment assistance in excess of 5 percent may be approved, the PHA must provide to HUD information and documentation specified in §§ 905.606 and 905.608 of this part, as HUD deems appropriate.

(3) For mixed-finance projects, all funding for predevelopment costs must be reviewed and approved by HUD prior to expenditure.

(4) The requirements in paragraph (b) of this section to disburse funds for mixed-financed projects in an approved ratio to other public and private funding do not apply to disbursement of predevelopment funds.

(b) *Standard drawdown requirements*.

(1) *General*. If HUD determines that the proposed development is approvable, it may execute with the PHA the applicable ACC Amendment to provide funds for the purposes and in the amounts approved by HUD. Upon approval of the development proposal and all necessary documentation evidencing and implementing the development plan, the PHA may disburse amounts as are necessary and consistent with the approved development proposal without further HUD approval, unless HUD determines that such approval is necessary. Once HUD approves the site acquisition proposal, the PHA may request funds

for acquisition activities. Each Capital Fund disbursement from HUD is deemed to be an attestation of compliance by the PHA with the requirements of this part, as prescribed in § 905.106 of this part. If HUD determines that the PHA is in noncompliance with any provision of this part, the PHA may be subject to the sanctions in § 905.800, subpart H, of this part.

(2) *Mixed-finance projects.* For mixed-finance projects, prior to PHA disbursement of public housing funds, except predevelopment funds identified in paragraph (a) of this section, HUD may require a PHA to submit to HUD, for review and approval, copies of final, fully executed, and, where appropriate, recorded documents, submitted as part of the development proposal process. Upon completion of the project, the ratio of public housing funds to non-public housing funds for the overall project must remain as reflected in the executed documents. The ratio does not apply during the construction period.

Subpart G—Other Security Interests

§ 905.700 Other security interests.

(a) The PHA may not pledge, mortgage, enter into a transaction that provides recourse to public housing assets, or otherwise grant a security interest in any public housing project, portion thereof, or other property of the PHA without the written approval of HUD.

(b) The PHA shall submit the request in the form and manner prescribed by HUD.

(c) HUD shall consider:

(1) The ability of the PHA to complete the financing, the improvements, and repay the financing;

(2) The reasonableness of the provisions in the proposal; or

(3) Any other factors HUD deems appropriate.

Subpart H—Compliance, HUD Review, Penalties, and Sanctions

§ 905.800 Compliance.

As provided in § 905.106 of this part, PHAs or other owner/management entities and their partners are required to comply with all applicable provisions of this part. Execution of the CF ACC Amendment received from the PHA,

submissions required by this part, and disbursement of Capital Fund grants from HUD are individually and collectively deemed to be the PHA's certification that it is in compliance with the provisions of this part and all other Public Housing Program Requirements. Noncompliance with any provision of this part or other applicable requirements may subject the PHA and/or its partners to sanctions contained in § 905.804 of this part.

§ 905.802 HUD review of PHA performance.

(a) *HUD determination.* HUD shall review the PHA's performance in completing work in accordance with this part. HUD may make such other reviews when and as it determines necessary. When conducting such a review, HUD shall, at minimum, make the following determinations:

(1) HUD shall determine whether the PHA has carried out its activities under this part in a timely manner and in accordance with its CFP 5-Year Action Plan and other applicable requirements.

(2) HUD shall determine whether the PHA has a continuing capacity to carry out its Capital Fund activities in a timely manner.

(3) HUD shall determine whether the PHA has accurately reported its obligation and expenditures in a timely manner.

(4) HUD shall determine whether the PHA has accurately reported required building and unit data for the calculation of the formula.

(5) HUD shall determine whether the PHA has obtained approval for any CFFP or OFFP proposal and any PHA development proposal.

(b) [Reserved]

§ 905.804 Sanctions.

(a) If at any time, HUD finds that a PHA has failed to comply substantially with any provision this part, HUD may impose one or a combination of sanctions, as it determines is necessary. Sanctions associated with failure to obligate or expend in a timely manner are specified at § 905.306 of this part.

Other possible sanctions that HUD may impose for noncompliance by the PHA include, but are not limited to, the following:

(1) Issue a corrective action order, at any time, by notifying the PHA of the

specific program requirements that the PHA has violated, and specifying that any of the corrective actions listed in this section must be taken. Any corrective action ordered by HUD shall become a condition of the CF ACC Amendment.

(2) Require reimbursement from non-HUD sources.

(3) Limit, withhold, reduce, or terminate Capital Fund or Operating Fund assistance.

(4) Issue a Limited Denial of Participation or Debar responsible PHA officials, pursuant to 2 CFR parts 180 and 2424.

(5) Withhold assistance to the PHA under section 8 of the Act, 42 U.S.C. 1437f.

(6) Declare a breach of the CF ACC with respect to some or all of the PHA's functions.

(7) Take any other available corrective action or sanction as HUD deems necessary.

(b) *Right to appeal.* Before taking any action described in paragraph (a) of this section, HUD shall notify the PHA of its finding and proposed action and provide to the PHA an opportunity, within a prescribed period of time, to present any arguments or additional facts and data concerning the finding and proposed action to HUD's Assistant Secretary for Public and Indian Housing.

PART 941—[REMOVED]

■ 7. Under the authority of 42 U.S.C. 3535(d), remove part 941, consisting of §§ 941.101–941.616.

PART 968—[REMOVED]

■ 8. Under the authority of 42 U.S.C. 3535(d), remove part 968, consisting of §§ 968.101–968.435.

PART 969—[REMOVED]

■ 9. Under the authority of 42 U.S.C. 3535(d), remove part 969, consisting of §§ 969.101–969.107.

Dated: September 18, 2013.

Sandra B. Henriquez,
Assistant Secretary for Public and Indian Housing.

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