

Memo

To: Greg Byrne and Cheryl Teninga
From: Gina Metrakas
Re: Structure Group Recommendations

Attached please find two documents which contain the recommendations of the Structure Group (“the Group”) for the Administrative Reform Initiative. The Group also went through the Annual Contributions Contract (ACC) section by section, and provided comments and questions for individual sections. However, the Group decided to put forward the general recommendations first, and will follow up with the more detailed recommendations after HUD responds to the general principles.

The Group all agreed that a new ACC is necessary, and the first document attached is a memo of basic principles for the revised ACC prepared by Megan Glasheen (Reno & Cavanaugh, PLLC) and William Maher (NAHRO General Counsel). The memo was created to be used by the Group during our discussions. Upon review, the Group decided that the five principles contained in the memo captured the recommendations of the entire Group. Therefore, the memo in its original form is being put forward as the recommendations for the ACC.

The second document attached contains recommendations for the Declaration of Trust (DOT), the General Depository Agreement (GDA) and Consortia.

The collective desire of the Group is that these recommendations serve as a starting point for further collaborative work between HUD, PHAs, the Industry and other interested parties. All of the participants in the Structure Group would like to be provided with the opportunity to participate in furthering the recommendations of the Group, including developing and drafting the revised documents.

TO: Structure Committee – HUD Administrative Reform

FROM: Megan Glasheen, Reno & Cavanaugh, PLLC
William Maher, NAHRO General Counsel

DATE: August 28, 2007

RE: Proposed Basic Principles for Revised ACC

As discussed, Bill Maher and I have talked and put together some general principles for the group to consider. The principles that we set forth below are based on the notion that there is intent for the ACC to have real meaning and be a true bilateral agreement. A tailored agreement that represents a true give-and-take is the preferred course of action. If however, there is not an intent or interest in having a document that evidences mutuality, then we would advocate an approach where the ACC is a simple one page document that simply keeps track of funds awarded and requires compliance with law and regulation.

We think an agreement that sets a more mutual tone will be more beneficial for HUD and PHAs and would create a more constructive work environment for both entities. A minimum goal of this process, however, should be to eliminate items in the ACC that are slightly different from statute or regulation or not required by law to avoid needless funds being spent on monitoring, enforcing, and defending the differences.

This memo is a first step at these issues that is produced to solicit your feedback.

Principle #1: Mutuality.

If the annual contributions contract is genuinely to reflect principles of contract it must have mutuality. The present ACC is so one-sided, with respect to the respective rights and obligations of the parties that knowledgeable lawyers have questioned if it is not “illusory.”

Mutuality should be reflected in two ways:

- A. **Mutuality of obligations.** – The ACC should genuinely reflect the basic bargain between the federal government and the PHA that is contemplated in the U.S. Housing Act of 1937. That is, the PHA as owner of the public housing property agrees to operate it according to the federal regulatory scheme. This includes, importantly, targeting admissions to low- and extremely low-income families, limiting tenant rents to 30 percent of adjusted household income, and carrying out a number of other statutory and regulatory duties pursuant to federal policy. For its part, the federal government is to provide subsidy in amounts reasonably adequate to carry out the regulatory scheme and to maintain the properties as decent, safe, and sanitary housing.

Presently, the ACC contains no meaningful obligation to supply funds in amounts necessary to carry out its part of the basic bargain. While conceding that the

contract cannot obligate the government beyond funds appropriated, the ACC fails to require even that sufficient funds be *requested* to be appropriated, and it provides no adjustment in PHA obligations, or the regulatory scheme, if sufficient funding is not provided.

An ACC with appropriate mutuality will provide for mechanisms to establish a baseline of funding for operation of each development and for capital funding. PHA obligations should relate to HUD funding.

B. Mutuality of Remedies. – What happens when a party to the ACC fails to uphold its end of the basic bargain? Presently, the federal government is provided with a virtual arsenal of remedies, including receivership, assuming possession, or even claiming title to the properties if the PHA materially breaches the “contract.” Not so for the federal government. When, as now, the federal government materially under-funds operations and capital needs, the ACC affords the PHA no remedy at all. An appropriate ACC will anticipate that inadequacies in funding may occur and will recognize operational realities by providing realistic adjustments to PHA obligations.

Adjustments could include, by way of example, an option to the PHA to 1) Convert to project based section 8 model, 2) Release the 10 year affordability tail, 3) Pro-rate and reduce the number of units maintained as public housing, and/ or 4) Rent to higher income eligible families to meet the gap between costs and revenues?

Principle #2 – Individual Contracts for Developments

Contracts should be entered into for each development specific to needs of the development involved. The consolidated contract should be eliminated. The contracts should reflect, among other things, mixed-finance or operating subsidy only, or capital only, or using public housing operating subsidy as rental assistance per statute.

Each contract must be free standing. A PHA’s contracts should not be interrelated by cross-default provisions or other mechanism involving cross- or mass-default.

Each contract would establish baseline operating and capital funding. Contracts would permit funds not needed for the operation of a particular project to be available to the PHA for transfer to other projects where the funds may be effectively utilized.

Principle #3 – Elimination of Duplicative or Selective Statements of Applicable Law

The ACC, as presently written, contains recitations of applicable requirements, some of which are not comprehensive and others of which elevate “requirements” to legal obligations. An appropriate ACC need only to refer to applicable law. It should allow statutes and regulations to speak for themselves and should avoid paraphrasing and

selective incorporation of legal requirements. Further, it should not convert “requirements”, which would not ordinarily carry the force of law, into binding legal obligations through the vehicle of contract.

Examples of subject areas in which these issues should be addressed are civil rights, troubled PHA remedies, and use restriction

Principle #4 – Objective Standards for HUD Oversight/Auditing Standards

Both informal and formal actions by HUD officials relating to enforcement of ACC obligations must be objective and based upon compliance with statutory law and regulations rather than discretionary judgments about the propriety of PHA actions. This principle is in keeping with the maximum flexibility that the Housing Act provided to PHA that are performing satisfactorily. Contract language and the assertion of PHA defaults must proceed under an objective process that recognizes the role of HUD as a regulatory oversight agency rather than a direct participant in programs whose administration is contracted to the PHA.

Principle #5. Due Process in Resolving Contractual Disputes.

An appropriate ACC will incorporate a mutually acceptable mechanism for resolving differences of opinion between the parties concerning contractual compliance, including regulatory compliance. Since the efficacy of contractual language is as a practical matter dependent upon the practical ability of each party to insist that it be followed, an appropriate ACC will afford to both parties an efficient and timely method of resolving disputes without judicial intervention. This is particularly necessary where, as here, an imbalance exists in the relative power of the parties. A reasonable dispute resolution mechanism helps assure mutuality and adherence to the principles of the contract, encourages uniformity and transparency in federal decision making, and, perhaps most importantly, helps assure that disputes are resolved in accordance with applicable law,

A successful dispute resolution mechanism must call for decision by an impartial party, contain the basic elements of due process, which are already well-established in HUD regulations, and, not least, be expeditious.

Without such a system, the inherent imbalance of power between federal and non-federal parties will tend, in practice, to negate the bilateral character of the contract regardless of the clarity of its language.

ADMINISTRATIVE REFORM INITIATIVE: **STRUCTURE GROUP RECOMMENDATIONS**

I. Declaration of Trust (DOT)

Recommendation #1: Develop new document that is more streamlined and more like extended use agreement in tax credit deals.

The document should be updated to reflect more up-to-date language and purpose of DOT. In addition, it should be called a use agreement (or something of that sort) which is more understandable to the private sector.

- Why? Banks don't understand or accept current DOT, which requires work around solutions (e.g. Long Term Leases).

Recommendation #2: Order of Liens

A joint subordination where the lender subordinates to the use restriction and HUD subordinates to the financing. Or in the alternative, could HUD be the second lien as long as HUD use restriction is kept.

- Why? DOT is an obstacle to financing/leveraging.

Recommendation #3: Part of Asset Management Checklist

Have DOT for each project on asset management checklist, so that PHA has not successfully converted to asset management unless all of the DOTs have been recorded.

- Why? Many PHAs do not have recorded DOTs for property.

Recommendation #4: Explore removing use restriction

Explore option of removing use restriction by paying off capital fund (operating fund) contributions over time, with the PHA eventually obtaining a release.

- Why? DOT is an obstacle to financing/leveraging.

II. General Depository Agreement (GDA)

Recommendation #1: Asset Management Effect

The language and document needs to be reviewed in light of asset management. What is the statutory basis for having a GDA? In addition, due to the fee structure of asset management (i.e. federal funds lose federal identity when earned as fees), what control is appropriate for HUD to have over a PHA's funds?

III. Consortia

Recommendation #1: Revise ACC, and have one master ACC.

Each individual PHA would have individual “project” ACC. Look at governance and operations separately.

Recommendation #2: Review regulations for workability and need for changes to address asset management.

Currently, lead agency submits all documents for all PHAs in consortia.

- Why? With asset management the lead agency will be responsible for all submissions and documents at the project level for each PHA in the consortia.