

RESPONSES TO COMMENTS RECEIVED ON SEPTEMBER 6, 2006, NOTICES ON FINANCIAL REPORTING UNDER ASSET MANAGEMENT

On September 6, 2006, HUD published a Federal Register notice entitled, “Public Housing Operating Fund Program; Guidance on Implementation of Asset Management,” (71 FR 52710). On the same day, HUD also published PIH 2006-33 (HA), *Changes in Financial Management and Reporting Requirements for Public Housing Agencies Under the New Operating Fund Rule (24 CFR Part 990): Interim Instructions*. PIH Notice 2006-33 (HA) updated HUD Handbook 7475.1 REV., CHG-1, Financial Management Handbook, through a supplement (the supplement) named, “Changes in Financial Management and Reporting Requirements for Public Housing Agencies Under the New Operating Fund Rule (24 CFR 990).”

The Federal Register notice was intended to clarify and provide interim guidance pertaining to various aspects of public housing’s conversion to asset management at a high level. The PIH notice provided greater accounting detail, consistent with the Federal Register notice. Public comments were solicited on both notices.

The public comment period for the proposed notices closed on November 6, 2006. HUD received comments from 48 sources. Comments were submitted by PHAs, PHA industry groups, advocates for low-income housing, housing experts, and other organizations and individuals. This document presents a summary of the significant issues raised by the public comments and HUD’s responses to the comments.

Summary of Changes

The following is a list of the major changes made to the interim guidance and now reflected in PIH Notice 2007-9 (HA), *Updated Changes in Financial Management and Reporting for Public Housing Agencies Under the New Operating Fund Rule (24 CFR Part 990)* issued April 10, 2007.

- The elimination of the restriction that excess cash exceed one month of operating expenses in the second year of project-based budgeting and accounting, affecting fungibility and payment of an asset management fee.
- Deletion of the payment of Capital Fund Program management fees based on disbursements. Instead, PHAs will earn their Capital Fund Program management fees based in the first year of program award.
- Revised language regarding payment of management fee for Replacement Housing Factor grants. These funds are part of the “development” and, therefore, subject to the safe harbors for Mixed Finance developments.
- An updated list of new Financial Data Schedule (FDS) line items.
- Revised policy reflecting that audit costs should be reasonably allocated to the AMPs, programs, and central office cost center (previous guidance treated these audit costs as fees).

- The reclassification of costs associated with Physical Needs Assessments as a front-line expense of the Capital Fund Program (treated as a management fee expense in the original version of the supplement).
- Revised language regarding reasonableness of management fees, consistent with the Federal Register notice (71 FR 52710), and associated transition provisions.
- The establishment of fee-for-service arrangements for all centrally-provided maintenance services (previously limited to technical maintenance services) as well as related transition provisions for the initial year of project-based budgeting and accounting.
- Updated management fee tables to reflect most recent FHA data and vacancy rates in each FHA office, as well as the inclusion of limited dividend properties in the data set used to determine the 80th percentile fee method.
- Other clarifying and technical amendments.

Responses to Public Comments

Comments are grouped below by subject area, followed by a brief description of the comment and HUD's response to the comment. For ease of reference, comments have been numbered sequentially.

Associated Regulatory Reform

1. *A number of commenters noted that HUD should grant immediate regulatory and statutory relief to assist PHAs make the conversion to asset management, as recommended by the Harvard Cost Study.*

HUD Response: HUD is currently undertaking various initiatives to provide regulatory relief to facilitate PHA conversion to asset management. See Federal Register Notice FR-5128-N-01, Regulatory Waivers for Public Housing Programs to Assist with Transition to Asset Management, dated March 1, 2007. Also see Asset Management E-Newsletter, Issue 02, dated March 2007, Special Issue on Administrative Reform. The website address is:

(<http://www.hud.gov/offices/pih/programs/ph/am/>)

Public Housing Assessment System (PHAS)

2. *A number of commenters noted that the current PHAS is no longer adequate under an asset management model and needs to be updated. Some suggested that the old system should not just be "pushed" down to the property level. Others noted that HUD should work with the industry in revising and improving the assessment system.*

HUD Response: HUD acknowledges the need to update the PHAS to support asset management. HUD anticipates publishing proposed rulemaking later in 2007. HUD convened a meeting of PHAs and industry groups on January 25, 2007, to outline conceptual reforms to the PHAS.

Small PHAs

3. *One commenter noted that small PHAs (defined as fewer than 250 public housing units) should continue to have full fungibility with the Capital Fund Program.*

HUD Response: The guidance issued does not change current program rules that permit, for small PHAs, full fungibility between the Capital Fund and Operating Fund Programs.

4. *One commenter remarked that small PHAs that wish to convert to asset management should not be required to establish a separate central office cost center (COCC).*

HUD Response: Under the guidance issued, HUD has permitted, for the first-two years of implementation, an alternative method for small PHAs to demonstrate successful conversion to asset management that does not require them to establish a COCC (see section 9.2 of the supplement).

5. *Several commenters requested that this alternative method of demonstrating successful conversion to asset management be extended permanently.*

HUD Response: HUD supports this comment and will initiate rulemaking soon to modify the final rule on the Operating Fund Program (24 CFR 990) to eliminate the need for small PHAs to establish a COCC beyond the first two years.

6. *Several commenters suggested that the threshold of 250 units, below which the conversion to asset management is required, be raised to 500 units. These commenters indicated that the administrative burdens of converting to asset management for PHAs of this size grouping outweigh the benefits.*

HUD Response: HUD does not support this recommendation. The 250-unit threshold was a fundamental component of the rule that was negotiated. Moreover, there are many non-profit operators of HUD subsidized housing programs with similarly sized inventories who must abide by essentially the same asset management requirements, including project-based budgeting and project-based accounting.

7. *One small PHA noted that, had they understood the detailed requirements associated with converting to asset management, they would not have selected multiple AMPs, but would instead have combined all units into one project and taken advantage of the alternative approach to asset management.*

HUD Response: The election to convert to asset management for a small PHA is not permanent. A small PHA can change its election to convert to asset management. Similarly, PHAs can modify their initial AMP groupings, including the consolidation of all units into one project for small PHAs. Under asset management, small PHAs may still need multiple AMPs, but could elect not to use the COCC concept. HUD will issue upcoming guidance on changes to AMP groupings. In the meantime, PHAs should consult with their local field office.

8. *One commenter stated that HUD has not considered the impacts of asset management on small PHAs with large geographic areas.*

HUD response: Small PHAs have the election not to convert to asset management and, along with that, to combine all units into one project.

Excess Cash and Fungibility

9. *Under the guidance issued, following the first year of project-based budgeting and accounting, PHAs would need to have excess cash equal to one month of operating expenses before a PHA can transfer funds between projects or charge an asset management fee. One commenter felt the standard was too low. Many more believed the standard was too high. Others suggested that the fungibility provisions not be effective until 2011.*

HUD Response: While sound financial management practices would dictate that projects maintain at least one month of working capital, HUD has removed the one month of operating expenses in the calculation of excess cash for year two of project-based budgeting and accounting to assist PHAs with the transition to asset management.

10. *Several commenters stated that PHAs should be able to use excess cash to support the COCC.*

HUD Response: HUD disagrees. Section 990.280(c) of the final rule clearly establishes that the COCC shall be funded with property management fees and asset management fees and not through excess cash flow.

11. *One commenter expressed concern that a PHA would need to wait until submission of audited financial statements before accessing excess cash for purposes of fungibility and/or payment of an asset management fee. Given that audited financial statements are not due until nine months after the close of the fiscal year, PHAs would have to wait ten months to earn their asset management fee.*

HUD Response: Section 6.6 of the supplement states that, as soon as the AMP closes its books and determines the availability of excess cash, such excess cash can be used for approved purposes. The PHA does not have to wait for the audited submission. However, the final determination of excess cash will be based on approved audited submissions.

12. *One commenter requested that HUD clarify the timing of the calculation of excess cash, and the application of the fungibility provisions, given that HUD now funds PHAs on calendar year, and not necessarily a fiscal year, basis.*

HUD Response: Operating subsidy is fully fungible between projects and COCC during a PHA's first year of project-based budgeting and accounting, not based on a PHA's funding year for operating subsidy. The initial assignment of assets and liabilities will also occur at the end of a PHA's first year of project-based budgeting and accounting.

Capital Fund Program Reporting

13. *Several commenters wrote of potential hardships imposed by tying Capital Fund Program management fees to actual disbursements. The hardships noted included the complexity in calculating the fee and unstable cash flows.*

HUD Response: HUD agrees with the commenters. Consequently, HUD has removed the approach to tying management fees to actual disbursements. Instead, PHAs will be able to draw their entire Capital Fund Program management fees in the first year of award.

14. *Several commenters questioned the authority of HUD to include the Capital Fund Program in the requirement for project-based budgeting and accounting.*

HUD Response: Section 990.280(a) stipulates that “project-based budgeting and accounting will be applied to all programs and revenue sources that support projects under an ACC (e.g., the Operating Fund Program, the Capital Fund Program, etc.)” On a larger policy level, any model of asset management would be incomplete if it excluded an examination of the capital activities associated with a project.

15. *Several commenters were confused by, or disagreed with, the provision that, when PHAs transfer Capital Fund Program funds to operations, the amounts transferred become governed by the Operating Fund Program.*

HUD Response: HUD has not revised its guidance in response to this comment. On a practical matter, once these Capital Fund Program funds are transferred to the Operating Fund Program, they lose their Capital Fund Program identity and their use must then be governed by the Operating Fund Program. This guidance is consistent with how HUD has always treated this provision of the Quality Housing and Work Responsibility Act of 1998 (QHWRA).

16. *Several commenters regarded HUD’s guidance restricting the use of Capital Fund Program grants to support the COCC as a violation of QHWRA.*

HUD Response: HUD has not revised the guidance in response to these public comments. Section 990.280(c), agreed to during the negotiated rulemaking process, provides that the COCC be funded from the earning of property-management fees (including the annual management fee of ten percent from the Capital Fund Program) to fund non-project specific costs.

17. *Two commenters suggested that the procurement of Capital Fund Program contracts should be a front-line cost and not paid through Capital Fund Program management fees.*

HUD Response: HUD has not revised its guidance in response to these comments. Procurement actions are included as a cost of the COCC reimbursed through the Capital Fund Program management fee. They have historically been funded through the Administrative line item in the Capital Fund Program, which has long been capped at 10 percent of the total grant.

18. *Some commenters suggested that PHAs should be permitted to use cost allocation, in lieu of timesheets, to prorate front-line Capital Fund Program costs at the project level.*

HUD Response: HUD has not revised its guidance in response to these public comments. A goal of asset management is to identify the actual costs of operating each project. The documentation of direct costs charged to the AMP is a crucial element of this process.

19. *PHAs should be permitted to use Capital Fund Program grants to make renovations to non-dwelling structures that are assigned to the COCC.*

HUD Response: Costs to acquire or rehabilitate non-dwelling structures that are assigned to the COCC but still under a Declaration of Trust are an eligible expenditure under the Capital Fund Program. However, since the existing building is considered part of the Public Housing Program, any proceeds collected (office rent charges, community room rentals, etc.) are deemed program income subject to Operating Fund Program requirements. (See question 68 for related discussion.)

20. *Several commenters felt that PHAs should earn a management fee on the amount of debt generated by the Capital Fund Financing Program (CFFP) and not a PHA's annual Capital Fund Program grant.*

HUD Response: HUD has not revised its guidance on this issue. The Capital Fund Program management fee is a fee earned for the overall administration of the grant and the strategic planning for the use of these funds. Proceeds from debt are typically used to complete large-scale modernization work at the AMPs. Actual construction supervision/monitoring, as well as various "soft" costs such as permits, architectural fees, and engineering fees, would all be front-line costs charged to AMPs. Therefore, HUD believes that the Capital Fund Program management fee should be based on the annual award of the Capital Fund Program only.

21. *Several commenters felt that the Capital Fund Program management fee of 10 percent of the annual grant was not sufficient to cover administrative costs.*

HUD Response: HUD has not revised the guidance in response to this public comment, particularly in light of the fact that, historically, HUD has permitted PHAs to charge 10 percent of the Capital Fund Program grant for "Administration."

22. *Several commenters suggested that the purchase of centralized equipment should be allowed as an eligible Capital Fund Program expense.*

HUD Response: HUD has revised its guidance in this area with the revised notice. To the extent that a PHA maintains a central maintenance operation, it must do so through fee-for-service (see question 28). Under such conditions, any equipment used by the COCC to provide that service must be recovered through fees and not through the Capital Fund Program. Only project-specific equipment can be purchased through the Capital Fund Program. The only exception is for certain centrally-provided front-line administrative activities.

23. *Several commenters requested additional guidance as to the treatment of architectural and engineering fees as either front-line or COCC cost under the Capital Fund Program.*

HUD Response: Architect and engineering fees that can be directly related to a construction project and supported by timesheets can be charged as a front-line cost. Time that is not directly related to the construction project of the AMPs, such as time spent on the Annual Plan process of the PHA, general capital planning and budgeting, procurement, and reporting requirements of the Capital Fund Program, is included in the management fee.

Management Fees

24. *Some commenters suggested that HUD should publish documentation that HUD's Office of General Counsel (OGC), HUD's Office of Inspector General (OIG), and the President's Office of Management and Budget (OMB) have approved the recognition of fee income as "non-program income."*

HUD Response: The Office of Management and Budget (OMB) has determined that HUD can design and implement a recovery process to allow a PHA to use fee-for-service in lieu of cost allocation to claim its overhead and administrative costs. Such process is permitted under Section A(2)(b) of Circular A-87 as alternative method that reduces the administrative burden regarding the establishment of overhead rates. The fee income under the alternative method is not considered as "non-program income. A fee-for-service system has a number of advantages, which results in reduced administrative requirements for both PHAs and Federal oversight agencies. HUD regulatory procedures include consultation and clearance with all relevant offices, including the views of HUD's Inspector General.

25. *Several commenters suggested that PHAs not be required to comply with the reasonableness requirements for management fees until 2011.*

HUD Response: Section 990.280 of the final rule requires PHAs to develop and maintain a system of project based budgeting and accounting, including a management fee to fund the operations of the central office. Section 990.290(d) establishes that PHAs must be in compliance with these project-based budgeting and accounting requirements in FY 2007. To assist with the transition to asset management, PHAs are not required to comply with the cost reasonableness standards pertaining to the management fees in the first year of project-based budgeting and accounting. HUD has retained the requirement that a PHA be in compliance with reasonable fees by the second year of project-based budgeting and accounting. However, HUD has added new language to Section 7.4 of the supplement, as follows:

“HUD will presume that fees established pursuant to these guidelines are “reasonable.” PHAs are not required to comply with the reasonableness requirements of § 990.280 until the second year of project-based budgeting and accounting. A PHA may consult with HUD regarding its fees. HUD will provide its views on the reasonableness of the PHA fees, and work with the PHA to develop a fee schedule. As part of the consultation, HUD may request that a PHA provide documentation on the actual costs in the jurisdiction and explain the factors causing any differences between actual costs and the PHA fee schedule. Generally, HUD will consider a schedule with an additional two-year phase-in for compliance to be reasonable, based on the review of such documentation/explaining factors. A fee schedule agreed upon by the PHA and HUD meets the reasonableness standard for fees under the Operating Fund regulations.”

26. *Several commenters suggested that HUD allow centralized purchasing and that it be treated as a front line expense of AMPs.*

HUD Response: Under asset management, a PHA may elect to treat the purchasing function as a centralized activity. Although project level purchasing is the norm in multifamily property management, HUD does not require PHAs to adopt project-level purchasing. The decision to use project-level vs. centralized purchasing should be based on the best interests of the project. However, if a PHA elects to use centralized purchasing, the cost of providing this service to AMPs must be supported by the property management fee. Such a practice is the norm in multifamily housing.

27. *Several commenters objected to HUD not allowing the cost of supervision of centralized routine maintenance provided to an AMP to be included in the cost charged to the AMP.*

HUD Response: The guidance is consistent with the norms in multifamily housing. Routine maintenance functions are typically provided by site personnel and supervised by the property manager. Since the property manager is typically responsible for supervision of routine maintenance activities, to allow the cost of centralized supervision would result in double charging the AMP for this oversight.

28. *One commenter was concerned that, by HUD only allowing PHAs to charge AMPs for direct personnel costs for centrally provided routine maintenance services, they would be precluded from charging AMPs for other direct costs of providing routine maintenance such as tools, equipment, vehicle maintenance and other direct costs of providing routine maintenance.*

HUD Response: HUD has revised its guidance with respect to centrally provided maintenance, which should address this issue. In the initial notices, PHAs could establish a fee-for-service for centrally provide technical maintenance services but not routine maintenance. In the revised notice, PHAs must use fee-for-service for any centrally provided maintenance. Section 990.280(d) of the final rule states that: “In the case where a PHA chooses to centralize functions that directly support a project (e.g., central maintenance), it must charge each project using a fee-for-service approach. Each project shall be charged for the actual services received and only to the extent that such amounts are reasonable.” The original supplement did not permit fee-for-service for general maintenance because of the difficulty in establishing a market-price. Market pricing is more commonly available for technical services such as unit painting or extermination. For ease in accounting and for consistency with the final rule, the revised supplement (as contained in PIH Notice 2007-9 (HA)), now require a PHA to use fee-for-service for any centrally provided maintenance and to establish documentation to support the rates charged. As with management fees, PHAs will not be required to convert to this fee-for-service arrangement for central maintenance until the second year of project-based budgeting and accounting. After the initial assignment of assets between projects and the COCC, a PHA would need to pay for the cost of any centralized asset with its fee income. The exception to the above remains in the area of front-line administrations functions that are centralized. HUD will continue to allow, for example, a PHA to prorate the costs of a central waiting list to projects; however, a PHA can propose for HUD approval fee-for-service amounts for front-line administrative tasks.

29. *One commenter stated that, under the guidance issued, centrally provided plumbing, electrical, elevator service, window replacement and repair, fire alarm, security, and gutter, blacktop, countertops and sidewalk replacements would be eliminated.*

HUD Response: Consistent with the above response, all are eligible activities that a PHA can establish through a fee-for-service.

30. *One commenter stated that all IT costs should be treated as front line AMP costs.*

HUD Response: HUD does not agree. IT costs incurred to support the COCC are to be recovered through the management fee. IT costs incurred by AMPs that are reasonable and necessary are front line costs of the AMPs.

31. *One commenter was concerned that the Federal Register used the phrase, “PHAs are encouraged to consult with HUD on fees that depart from their guidance” while the Supplement to the Financial Management Handbook says that PHAs, “will need the Department’s approval.”*

HUD Response: The revised notice reads: “PHAs should consult with HUD on fees that depart from this guidance.”

32. *One commenter suggested that HUD should allow PHAs to charge properties a program fee to cover the costs of managing the Public Housing Program, indicating that PHAs must undertake many activities that private property managers do not.*

HUD Response: HUD does not support this proposal, which was deliberated (but not adopted) during negotiated rulemaking on the Operating Fund Program.

33. *One commenter suggested that HUD not require PHAs to meet the reasonableness test for fees as long as the AMPs were standard performers.*

HUD Response: HUD does not agree. The requirement that PHAs comply with reasonable fees was a fundamental component of the final rule on the Operating Fund Program that was negotiated with industry and other groups.

34. *One commenter objected to a PHA’s inability to receive a property management fee and bookkeeping fee for limited vacancies and suggested that HUD allow PHAs to receive fees on these units.*

HUD Response: HUD disagrees with the commenter. To pay a management fee (which includes a bookkeeping fee) on limited vacancies would be a disincentive for the PHA to quickly turn these vacant units over. In addition, the payment of fees for leased units is common practice in multifamily programs.

35. *Several commenters expressed concern that the bookkeeping fee of \$7.50 is inadequate and that it should be increased. Several challenged the method used to establish the bookkeeping*

fee, arguing that the FHA database is unreliable because thousands of properties report no bookkeeping fee. Others noted that they could not provide project accounting services for the amount established.

HUD Response: In multifamily housing, it is far from universal that management firms charge a bookkeeping fee for the project accounting function. Many firms instead charge only a management fee, which covers the responsibility for the project accounting function. Nationally, the median bookkeeping fee for FHA projects in 2005 was \$3.73 PUM; however, nearly 30 percent of projects report no bookkeeping fee. In these cases, the management fee includes compensation to the management company for the project accounting function. Indeed, in the case of private management of public housing, few housing authorities pay a separate bookkeeping fee and instead pay only a management fee. Because of the large number of projects that pay no bookkeeping fee, there is not a normal distribution of bookkeeping fees in most markets. Therefore, HUD has not used the same convention (as with management fees) in allowing the 80th percentile of bookkeeping fees paid in each market. Such would result in grossly distorted figures. Rather, HUD has established a national figure, one that is nearly \$4 PUM higher than the national median. The establishment of bookkeeping fees will be included in the anticipated rulemaking on management fees, as reported earlier.

36. Several commenters suggested that HUD apply an annual inflation factor to the property management and bookkeeping fee amounts.

HUD Response: HUD plans to issue revised fee schedules on a yearly basis. The revised fee schedules will be reflective of inflationary/deflationary factors or be benchmarked to the next year of available data in the FHA database. The revised notice includes updated fee tables based on most recent FHA data.

37. Several commenters objected to HUD basing the property management fee on the fee schedules established for HUD's subsidized housing programs, indicating that such projects are not representative of the costs of PHA program administration.

HUD Response: HUD disagrees. The new Operating Fund Program formula is based on the operating costs of operators of HUD's subsidized housing program, so it is logical that the management fee schedules would be similarly benchmarked. In fact, while the formula for determining each project's Project Expense Level (PEL) is based on **median** operating costs, HUD has permitted PHAs to use the 80th percentile of management fees in each market.

38. Several commenters objected to the \$10 asset management fee on the grounds it is insufficient to cover the costs of asset management.

HUD Response: HUD disagrees. The asset management fee is intended to compensate PHAs for distinctly owner costs (above and beyond property management) for which they have not otherwise been funded (for example, PHAs are paid a Capital Fund Program management fee that pays for capital planning tasks). It is not intended to provide the equivalent of "return on investment" for private operators. Recently, HUD published on its

asset management web site (<http://www.hud.gov/offices/pih/programs/ph/am/>) the results of an analysis of cash flow (excess cash) in HUD's multifamily housing programs. In 2004, the median cash flow was \$33.33 per unit month (PUM). It is not possible to ascertain how much of this cash flow was used to pay for "distinctly owner functions," such as strategic capital planning, and how much reflected an owner's "free and clear" return. It seems logical, however, that owners would want to minimize the former and maximize the latter. In essence, the \$10 PUM asset management fee is around one-third of a typical multifamily project's cash flow.

39. *One commenter objected to HUD prohibiting PHAs from booking a receivable for unpaid asset management fees in light of the low proration levels for the Operating Fund Program.*

HUD Response: In the first year of project-based budgeting and accounting, there is no excess cash requirement for payment of an asset management fee. HUD will examine this issue in light of future funding levels.

40. *One commenter suggested that PHAs should be allowed to charge an asset management fee as long as the PHA is performing asset management functions.*

HUD Response: HUD disagrees with the commenter. The final rule on the Operating Fund Program stipulates that the asset management fee be paid contingent on an AMP's excess cash.

41. *One commenter requested that HUD conduct a cost study to determine how much should be provided in the form of a fee for human resources costs.*

HUD Response: HUD disagrees. Human resources are a central office function, the costs of which are included inside the management fee.

42. *One commenter indicated that HUD should not require PHAs to charge management fees to the Capital Fund Program, Housing Choice Voucher Program and other grant programs as the only vehicle to recover administrative expenses incurred. The commenter further said that PHAs should have a guarantee that the management fee for the Housing Choice Voucher Program will remain voluntary.*

HUD Response: The commenter misunderstood the guidance issued. HUD is only requiring fee-for-service in the Operating Fund and Capital Fund Programs. For all other programs, fee-for-service is voluntary. HUD cannot provide a guarantee of future actions.

43. *One commenter recommended that certain board member stipends, travel, and training should be an eligible "front-line" expense.*

HUD Response: Project-related training and the associated expenses to attend training from project staff and the Board of Directors are eligible front-line expenses. Training expenses include fees and travel costs to attend the training (e.g., airfare, hotel, per-diem, local travel, etc., where required). Training and related expenses must be reasonable and included in the

project's budget. Generally, a reasonable training/travel budget would not exceed \$5,000 or one half of one percent (0.005) of the project's yearly gross rents and operating subsidy. Training expenses related to board training may be prorated to projects using a reasonable methodology. Training expenses incurred by COCC staff are management fee expenses and may not be charged to projects.

44. *One commenter suggested that HUD should add language to the definition of "Fee Expenses" that allows for prorating costs to the properties whenever the PHA can demonstrate that it is in the best interest of the property with concrete savings data.*

HUD Response: HUD disagrees with the commenter. HUD has already defined some elements of costs that can be front-line allocated costs. To allow all PHAs the option to use an allocation system for all costs would defeat the goals of asset management.

45. *One commenter suggested that inspections centrally provided should be considered a front line expense.*

HUD Response: HUD has clarified the guidance so that property inspections (excluding quality control inspections by the COCC, which are a COCC expense) must, if handled centrally, be handled through fee-for-service. Generally, centralized inspections are not necessary in multifamily housing programs because on-site staff is responsible for those duties.

46. *One commenter pointed out there may be an inconsistency in the supplement with regard to which pro-rated front line administrative costs could include supervisory costs.*

HUD Response: HUD agrees with the commenter. PHAs will be allowed to include the cost of supervision as part of the pro-rated front line administrative costs for centrally provided waiting lists, resident services, and security/protective services. HUD has updated the supplement to include this correction.

47. *One commenter suggested that once a project has been scheduled for demolition, the on-going monitoring and winding up costs that continue after the project has been shut down should be shifted to the COCC, including the operating subsidy provided for these projects.*

HUD Response: HUD disagrees with the commenter. The Operating Fund Program final rule requires that operating subsidy be calculated by HUD at a project level. After subsidy is calculated at a project level, operating subsidy can be transferred as the PHA determines during the PHA's fiscal year to another project(s) if a project has excess cash flow. Operating subsidy can only be paid to the COCC in the form of property management fees, bookkeeping fees, asset management fees, and other fee-for-service, as provided in the final rule.

48. *One commenter suggested that participants in the negotiated rulemaking on the Operating Fund Program did not agree, nor does the rule provide, that central office supervisory*

functions relating to project management could only be paid from HUD approved property management and asset management fees.

HUD Response: HUD does not agree with the commenter. The rule provides, at 990.255, that PHAs shall manage their properties according to an asset management model, consistent with the management norms in the broader multi-family management industry. It is common practice in the multi-family industry that supervision of centrally provided services be supported by the management fee. HUD has already provided exceptions to this norm by providing PHAs the ability to treat supervisory costs for central waiting list, resident services, security/protective services as part of the front-line prorated costs.

49. *One commenter suggested that the rule was implicitly forcing PHAs to eliminate central maintenance and central warehouses.*

HUD Response: HUD disagrees. HUD is not requiring that PHAs under asset management eliminate central maintenance or central warehouses. However, if a PHA elects to maintain central maintenance, these services must be performed through fee-for-service. As included in the guidance, a PHA can retain central warehouse if the PHA, with HUD approval, can document that such arrangements are in the best interests of the project.

Fees for the Housing Choice Voucher (HCV) Program

50. *One commenter questioned HUD's authority to set fee limits in the HCV Program.*

HUD Response: The guidance provides safe harbor amounts for PHAs wishing to adopt fee-for-service in the HCV Program and has been approved by HUD.

51. *One commenter expressed concern that the HCV fee threshold is insufficient to cover the costs associated with the functions in the notice.*

HUD Response: HUD disagrees. PHAs are not required to convert to a fee-for-service system in the HCV Program. Although HUD believes using the same system to recover COCC costs will ease the accounting burden on PHAs, it is a PHA management decision to do so.

52. *One commenter requested that all references to a fee-for-service in the HCV Program be removed from the notices and issued in a separate notice for the HCV Program.*

HUD Response: HUD disagrees. HUD believes that it will ease the accounting burden on PHAs to fully convert to a fee-for-service methodology across all programs a PHA operates. For those PHAs who administer various federal and non-federal programs, it is important to provide guidance regarding HUD's policy on fee-for-service. For those PHAs that do not administer Operating Fund Programs, it is a PHA's decision whether to convert to a fee-for-service methodology.

53. *One commenter suggested that HUD should provide guidance with regard to the leasing threshold below which a PHA can drop below before they are limited to using a lower percentage of Section 8 administrative fees or dollars per PUM than HUD proposes.*

HUD Response: The commenter has misunderstood the voluntary safe harbor fees for the HCV Program. It is a PHA decision to determine whether the PHA uses the 20 percent amount or the flat \$12 PUM amount as a fee.

54. *One commenter questioned whether HUD had the authority to declare the management fee (as opposed to the entire administrative fee paid to the PHA to administer the HCV Program) to be considered non-program income and requested HUD provide the authority for this guidance.*

HUD Response: As indicated, this notice has been subjected to Departmental Clearance and approved by OGC, OIG, and OMB.

55. *One commenter was concerned that the safe harbor fee-for-service amounts established for the HCV Program would encourage PHAs to charge the HCV Program more than PHAs currently are charging the program for indirect costs.*

HUD Response: The decision to convert the HCV Program to a fee-for-service methodology is voluntary. The PHA can also charge a fee less than the guidelines offered.

Mixed Finance Projects

56. *One commented suggested that Chapter 8 of the supplement, relating to Mixed Finance projects, be modified to reflect the fact that PHAs are not owners of Mixed Finance properties and, accordingly, the direct and primary responsibilities are vested in other entities.*

HUD Response: HUD has updated the guidance on mixed-finance projects in the supplement to clarify the unique nature of these transactions.

57. *One commenter suggested that HUD revise its guidance to indicate that, in some instances, Mixed Finance projects would not be included as part of the financial statement of the PHA (i.e., included with the FDS).*

HUD Response: The language of the supplement has been updated accordingly. While historically Mixed Finance projects have been reported as component units, PHAs should report Mixed Finance entities in accordance with GAAP, as determined by the client in conjunction with its auditor. HUD believes that guidance provided by the GASB for reporting on these entities is sufficient.

58. *Section 8.2 of the supplement should be expanded to include reference to separate phases of Mixed Finance developments that should be reported as a separate AMP. Also, HUD should not allow Mixed Finance to be “rolled” into one AMP.*

HUD Response: HUD has modified the supplement to try to clarify these issues.

59. *HUD should clarify in Chapter 8 of the supplement and cross reference other pertinent points to other chapters to clarify the asset management concepts.*

HUD Response: Although HUD agrees that certain information on Mixed Finance entities needs to be strengthened, it anticipates readers of the document will be able to read the relevant sections of the document to understand the nature of the asset management requirements.

60. *HUD should consider acknowledging that, with respect to ACC units in Mixed Finance entities, the PHA will be deemed to be in compliance with asset management if it is complying with its review and monitoring requirements under the governing documents of the development.*

HUD Response: HUD believes that adherence to the governing documents of the development does not guarantee compliance with the asset management requirements outlined in the supplement. For instance, while excess cash restrictions may not exist in the underlying documents of the development, these restrictions would still apply.

61. *The PHA actually has a higher asset management fee in its Mixed Finance documents than the amounts approved by HUD.*

HUD Response: In the case where a PHA has an approved Mixed Finance agreement that allows it to pay to a higher asset management fee per the governing documents, the PHA is bound and allowed by the agreement to pay that asset management fee.

62. *HUD should clarify that the restriction on bookkeeping fees is directed to PHA-owned projects and is not intended to limit the fees to be paid to the PHA by the Mixed Finance project under the terms of their individual agreements.*

HUD Response: Once again, the guidance contained in the supplement does not replace agreement contained in documents governing the Mixed Finance development.

63. *One commenter questioned if HUD's intention is to limit excess cash on the PHA's balance sheet and not on the Mixed Finance project's balance sheet.*

HUD Response: The excess cash referred to in Section 8.4 of the supplement refers to excess cash generated by the ACC units for those transactions reported in the AMP column on the FDS within the Mixed Finance entity. Nothing HUD has issued should be construed to limit excess cash to something other than that, which is required under the Mixed Finance governing documents.

64. *Since Mixed Finance projects are undertaken under third-party agreements, the fee based funding of the COCC seems counter productive. It makes no sense to limit these fees below those established in these third party agreements.*

HUD Response: HUD's intention is not to reduce fees available to the PHA under separate legal documents governing the Mixed Finance entity. The PHA will always be allowed to recover or pay the full amount of the fees allowed under the agreement.

65. *One commenter strongly disagreed with the limitation of a three percent administrative fee paid from Capital Fund Program for Mixed Finance properties. The commenter stated it should be doubled to six percent without a requirement to support that the fee is appropriate.*

HUD Response: HUD disagrees with the suggestion. Historically, the administrative fee limitation for use of Capital Fund Program funds for the PHA's portion of the administrative costs of development has been limited to three percent. Amounts in excess of three percent have been approved by HUD on a case-by-case basis.

Project-Based Budgeting and Accounting

66. *Several commenters wrote that six-month reserve levels for the COCC are either too restrictive or insufficient and that there should be no limits on the PHA assigning its own assets to the COCC.*

HUD Response: HUD believes that assignment of up to six months of fees, based on units under ACC, is adequate for initial working capital of the COCC.

67. *In calculating gross rent potential and losses due to vacancies, the amounts are determined using average or mean rents. One commenter wrote that the range of rents can be large, so average rents do not mean much.*

HUD Response: HUD provided the most straightforward approach in determining both gross potential rent and vacancy loss. However, PHAs have the option of using a more complicated methodology such as using a weighted average to determine the average rent for gross rent potential and losses due to vacancies based on other factors such as bed-room mix or unit size, for example.

68. *Under the guidance, real property paid with public housing funds that are assigned to the COCC will be treated as "restricted" assets, whereas property purchased with fee income will be non-restricted (general) assets of the COCC. This distinction will create many complicated and impracticable divisions in the asset accounts of the central offices.*

HUD Response: HUD seeks to provide relief in the near future to this accounting issue. Initially, PHAs will have capital assets that are still restricted, as they were purchased with program income. For short-lived assets, such as office equipment, these will be replaced by non-restricted assets purchased through fee income and, therefore, present only a short-term issue. In the case of real property, HUD is examining current statutory requirements related to the disposition of such assets. HUD expects to issue supplemental guidance soon on how PHAs may request that assets assigned to the COCC, and not essential to the operation of projects, can be disposed from the Public Housing Program and provided to the COCC. Such guidance will be consistent with section 18 of the United States Housing Act, 24 CFR part 970, and the ACC.

69. *Several commenters requested information on how the financial performance of projects will be scored under a revised PHAS, particularly in relation to a project's retained earnings. Another commenter questioned whether the COCC will be scored separately from the AMPs.*

HUD Response: As indicated previously, HUD expects to publish a proposed PHAS rule later in 2007. Consistent with the final rule's shift in focus to the performance of projects, it is not anticipated that the COCC will be scored under a revised PHAS.

70. *One commenter noted that with all the new accounting requirements, additional accounting staff will be required for compliance, which, the commenter believed, could not be supported within the safe harbor management fees.*

HUD Response: HUD disagrees. The preparation of monthly project-based financial statements is standard in multifamily housing, a task for which management companies are compensated through the management fee/bookkeeping fee.

Comments on Changes to Financial Statement and Financial Data Schedule Reporting

71. *HUD should require an FDS Maintenance Cost Center column.*

HUD Response: HUD disagrees. The FDS will only collect information at the COCC, which would include any centralized maintenance functions. Each PHA needs to assess its management needs for information at a lower level and should base its decision based on that need.

72. *One commenter suggested that HUD extend the period for FDS submissions from 60 to 90 days, allowing agencies the necessary time to ensure accuracy of all the newly required information.*

HUD Response: The current reporting deadlines will remain unchanged.

General Comments

73. *Several commenters expressed concern that current appropriations levels do not allow PHAs to effectively transition to the asset management model. These commenters further noted that, in light of these restrained funding levels, HUD should be much more flexible in the policies and timing surrounding the overall conversion to asset management.*

HUD Response: The initial guidance issued provided PHAs with full fungibility between projects and central office cost centers in the first year of implementation of project-based budgeting and accounting, which covers, at a minimum, the Fiscal Year 2007 appropriation. Additionally, this notice removes the one-month calculation for excess cash for the second year of implementation. While it is not possible to determine appropriations levels in the future, one of the primary benefits of the move to asset management is to improve strategic financial planning.

74. *Many commenters considered HUD's guidance to be overly prescriptive, resulting in PHA micromanagement. These commenters expressed the need for a more flexible model, one*

that allows different business forms and organizational structures. Some suggested that the current model is overly complex and will require additional funding to administer properly.

HUD Response: HUD has developed its guidance based on the norms in multifamily housing, as required under the final rule on the Operating Fund Program that was negotiated with PHAs, industry representatives, and other interested and affected groups. HUD recognizes, however, the need for a transition period, which is reflected in the fact that, under the first year of project-based budgeting and accounting, PHAs: (1) have full fungibility between projects and central office cost centers; and (2) are not required to meet the reasonableness standards for management fees. Additionally, for the second year of project-based budgeting and accounting, HUD has, through these revised notices, removed the need for excess cash equal to one month of operating expenses for purposes of fungibility between projects. HUD disagrees that it is micromanaging but merely providing the guidance necessary to move to this new model. Such guidance is based on the collective body of instructions provided to operators of HUD subsidized housing. HUD acknowledges that the level of documentation does increase where PHAs provide property management services centrally; however, such arrangements are voluntary and the associated levels of documentation are essentially the same as for operators of subsidized housing.

75. Without formal rulemaking, HUD cannot establish binding requirements related to asset management, particularly in the area of management fee.

HUD Response: The notices were intended to provide guidance to PHAs in understanding the types of changes in financial management necessary for full implementation of the final rule. While such direction was clearly stated in the Federal Register notice, the PIH notice inaccurately referred to the guidance as “binding program requirements.” This language in the PIH notice has been modified. When PHAs exceed these guidelines, the notices have been revised to indicate that PHAs should first consult with HUD. To eliminate uncertainty, HUD intends to begin rulemaking in the area of fees, which may establish binding requirements for the future.

76. A number of commenters believe that the asset management model is fundamentally flawed and will lead to inefficient and ineffective public housing.

HUD Response: The Operating Fund Program final rule requires PHAs with over 250 units to adopt a new management model known as asset management that is based on the norms of multifamily management. HUD strongly disagrees that this model, practiced by thousands of owners of multifamily housing, and established for HUD’s other subsidized and unsubsidized housing programs, is flawed. Asset management moves PHAs from a traditionally entity-centric model to a property-centric model, consistent with standards in private housing.

77. A number of commenters expressed concern of an apparent piece-meal approach to the implementation of asset management and the lack of general information regarding the overall schedule of implementation.

HUD Response: Through its asset management website, HUD is attempting to provide PHAs and other interested and affected parties with plans related to implementation.

78. *Several commenters remarked that the Operating Fund Program formula either needs clarification or is inaccurate.*

HUD Response: These notices relate to financial reporting requirements under asset management, not the model or its associated coefficients. HUD has already completed rulemaking regarding formula components.

79. *Several commenters mentioned that rents in multifamily housing tend to be higher than in public housing. Moreover, multifamily projects often receive annual rent increases.*

HUD Response: Rent levels in multifamily housing do not affect financial reporting standards. Rent levels can affect resources available to cover operating expenses; however, the new Operating Fund Program formula is based on expense levels in multifamily housing.

80. *Several comments were received on different aspects regarding implementation of “stop-loss,” including: (1) small PHAs should not be subject to stop-loss rule; (2) small PHAs should be able to cap their net loss at a fixed percentage instead of complying with the current criteria under PIH Notice 2006-14 to comply with stop-loss; (3) PHAs should not be required to comply with all criteria under stop-loss and instead should only need to comply with a “majority” of criteria; and (4) the deadline for submission should be moved from April 15, 2007, to October 15, 2007.*

HUD Response: Although stop-loss is not the subject of these notices, HUD would like to indicate that: (1) small PHAs currently have reduced requirements to meet the stop-loss requirements, which HUD considers to be reasonable; (2) HUD believes that the current criteria for small and large PHAs to be reasonable; (3) meeting only some of the criteria would not constitute for HUD “successful conversion;” and (4) HUD has already extended the deadline for implementing stop-loss twice. Further extensions are not anticipated. HUD is reviewing what additional guidance may be required to clarify the stop-loss requirements.

81. *Under the guidance issued, when a PHA charges a fee-for-service for central maintenance services (e.g., central landscaping services), such fees are considered non-program income. One commenter desired clarification that such practices are allowable under the cost principles contained in OMB Circular A-87.*

HUD Response: OMB has determined that such fee-for-service activities are considered non-program income under OMB Circular A-87.

82. *Conversion to asset management is not required until 2011, but HUD is imposing its management fee schedules on PHAs in 2008. That appears to violate the implementation schedule by forcing PHAs to convert before 2011.*

HUD Response: Section 990.280, regarding project-based budgeting and accounting, requires that PHAs must charge a reasonable management fee for the operation of the central office. Then, Section 990.290(d) of the final rule establishes that PHAs must be in compliance with these project-based budgeting and requirements by FY 2007. To assist with transition, under the guidance provided, PHAs have until the second year of project-based budgeting and accounting to comply with the management fee schedules. Also see response to question 25 regarding additional transition provisions.