U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

SEP 26 2014

MEMORANDUM FOR: All Multifamily Hub Directors
All Multifamily Program Center Directors
All Multifamily Operations Officers

FROM: Benjamin T. Metcalf, Deputy Assistant Secretary,
For Multifamily Housing Programs, HT

SUBJECT: Better Buildings Challenge Multifamily Partner Incentive: PRAC Shared Savings

The Department of Housing and Urban Development, in partnership with the U.S. Department of Energy and the White House, expanded the Better Buildings Challenge (BBC) to include multifamily residential buildings in December 2013. BBC Multifamily Partners have made a commitment to reduce their portfolio energy usage by 20 percent within 10 years. The Office of Multifamily Housing Programs has established the Project Rental Assistance Contract (PRAC) Shared Savings incentive to help BBC Multifamily Partners realize savings resulting from energy and water improvements at PRAC properties.

Part 1: Purpose

There are approximately 155,000 PRAC units in approximately 5,600 properties in HUD's portfolio. These units serve the elderly and disabled and offer both ongoing rental assistance and supportive services to residents. The average per unit cost for PRACs is approximately $7,000, and approximately thirty percent of PRAC owners pay all of the utilities at the property. PRAC tenants pay an average $580 directly to the utility companies, which is offset by the Utility Allowance (there is no way to identify *which* utilities are covered within the Utility Allowance, which is the primary data point for HUD to identify the energy cost/usage for tenant paid utilities). The earliest properties funded under this program (begun in 1992) are more than 20 years old, and therefore were not built to contemporary energy efficiency standards. Overall, HUD spends more than $6.5 billion on utility expenses across our program areas and seeks to both control and reduce these costs now and in the coming years.

Due to the underlying program regulations, PRAC properties are not designed to take on debt in order to support capital improvements of any kind, which may include energy and water reducing-related improvements. This incentive will provide PRAC properties with the opportunity to make energy and water improvements within the confines of the current regulations.

Budget renewals for PRACs are estimated yearly based on the project's prior year expenses and based on an analysis of expense levels at comparable properties. When a property performs better than anticipated – e.g. actual expenses are less than budgeted expenses - surplus cash is deposited into a residual receipts account at the end of the fiscal year in accordance with the project regulatory agreement. Residual receipts funds are applied to subsequent years' budgets to minimize or eliminate the need for PRAC rent increases. Consequently, better than estimated financial performance by the Owner/Agent is not rewarded. This dynamic is known as the "split incentive" between the Owner/Agent and HUD, with respect to energy and water efficiency improvements at PRAC properties. There is also a split incentive between the Owner/Agent and the tenants, which is not addressed by this memorandum and only applies to those properties where tenants pay a portion or all of the utilities. The incentive discussed in this memorandum applies to all properties with some portion of utilities paid by the Owner/Agent.

In establishing the mechanics for realizing the savings resulting from energy/water improvements for PRAC properties covered by this incentive, HUD has sought to minimize administrative changes. Therefore, instead of issuing a new form, Owner/Agents will change the way they use the existing budget form (HUD Form-92547-A) and provide supplemental information as detailed below. Further explanation of the process to realize the savings is included in the rest of this memorandum. This incentive is as "user friendly" as possible, limiting the obligations of the Owner/Agent and testing out an administrative "pay for success" option that HUD is exploring for its Project Based Rental Assistance (PBRA) portfolio. The desired result is beneficial physical improvements, improved resident comfort, and concomitantly lower expenses and reduced rental assistance renewal burden for the PRAC portfolio when the incentive period concludes.

PRAC Owner/Agents may use the Reserve for Replacement account to fund energy/water retrofits based on policy outlined in the Expedited Reserve for Replacement Account Releases memorandum, released by the Office of Multifamily Housing Programs dated June 12, 2014. If the PRAC property's Reserve for Replacement account is underfunded, where the current reserve for replacement deposit is not sufficient to meet the capital repair needs of the property as identified in the Project Capital Needs Assessment (PCNA) or alternatively during the development stage of the PRAC property, a release is still permissible for a cost-saving energy/water retrofit. However, the Multifamily Hub/Program Center (Multifamily Hub/PC) Project Manager must work with the PRAC Owner/Agent to ensure the reserve deposit, moving forward, is adequate to address the underfunded reserve and cover needed capital repairs in the future. This may require the Owner/Agent to submit a request to the Multifamily Hub/PC to increase the reserve for replacement deposit.

Part 2: Eligibility

This policy will apply to PRAC properties that are part of a BBC Multifamily Partner's portfolio that are either master metered for all utilities, or have some utility meters for which the property

Owner/Agent pays the utility costs directly. Currently, there is no way to capture savings that may accrue on tenant paid meters through this incentive, therefore PRAC properties where tenants are responsible for 100 percent of the utilities are not considered eligible at this time.

Part 3: Calculating Energy and Water Costs Averted

For applicable PRAC properties that are part of a BBC Multifamily Partner's portfolio, Owner/Agents will be permitted to capture 100 percent of their previous year's averted energy and water cost on the Fuel Oil/Coal budget line (Acct. No. 6420) of Form HUD-92547-A. Any fuel oil/coal costs should be added to the Gas budget line item (Acct. No. 6452) (please see Appendix A for further guidance).

The Owner/Agent should follow the below process to determine the energy and water costs averted to include on Form HUD-92547-A:

1. To determine the amount of energy and water costs averted, the Owner/Agent must establish a baseline through one of the following methods. The Owner/Agent should indicate if there were any extenuating circumstances that affected the baseline (i.e. high vacancy resulting in low utility costs in year one or extreme weather):

    - One year of data on utility usage and cost per unit of utility used entered in to EPA's Portfolio Manager or like software (www.energystar.gov/benchmark);

      OR

    - Three years of averaged historical data on utility usage and cost per unit of utility used using the HUD Multifamily protocol for Utility Analysis (please see the June 2011 memorandum titled *Clarification Utility Allowance Regulations* issued by Carol J. Galante, Federal Housing Administration (FHA) Commissioner—Assistant Secretary for Housing); including a justification of how the average was determined.

2. At annual contract renewal, take the baseline cost determined in step one and multiply the baseline cost of each utility by the Utility Allowance Factor (UAF) found on the HUDUser website[1] or the HUD Operating Cost Adjustment Factor (OCAF) if the UAF is not available. The UAF is determined by considering state specific average retail price of electricity, natural gas, water, and oil/propane for residential customers from the U.S. Energy Information Administration. This data will be used to determine the utility allowance adjustment factors for each utility. Multifamily Housing will publish the UAF for each state annually. Sum the individual utility costs into a total adjusted utility cost.

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[1] Please note that at the time of the publication of this memo, the UAF is not on the HUDUser website. The UAF will be published within the next year. The UAF provides a more accurate adjustment for utility costs, but the OCAF should be used until the UAF is available.

3. Calculate usage and cost per unit of the utility for the most recent year (the year for which you are trying to estimate the savings).
4. Subtract the number calculated in step number three from that calculated in step number two and the resultant number is the energy and water costs averted for that year. This number should be included on the Fuel Oil/Coal budget line (Acct. No. 6420) of Form HUD-92547-A.

The total line item expense entered into the Fuel Oil/Coal budget line cannot exceed the calculated amount of energy and water usage cost averted from the established baseline.

Part 4: Support for Savings

Owner/Agents will be required to support the energy and water costs averted amount included on the Fuel Oil/Coal line item on Form HUD-92547-A with documentation of energy savings at the time of the annual PRAC contract renewal.

In order for those PRAC properties that are still in the original term of the PRAC contract to realize this incentive, an annual budget worksheet must be submitted at the contract anniversary date to reflect the energy savings to ensure the Owner/Agent will realize the savings prior to the official renewal date. In both cases, support for savings should be provided using the process defined in Part 3, steps one to four.

Owner/Agents are responsible for completing all energy/water improvements and meeting any related terms of any third party contracts entered into for the completion of such work. Owner/Agents must submit documentation of work completed at the time of the request for the inclusion of the energy and water costs averted in the property's budget worksheet (see Appendix B). If additional improvements are made during the 12 year incentive period, but after the initial request, the Owner/Agent must submit an updated Appendix B at the annual contract renewal. The additional energy and water costs averted should be reflected on Form HUD-92547-A.

The Department will not provide additional funding to the Owner/Agent for the energy/water retrofits, though releases from the Reserve for Replacement are available to help facilitate energy/water retrofits and improvements (please see the Multifamily Memorandum dated June 12, 2014). Owner/Agents should work with the Multifamily Hub/PC to ensure the Reserve for Replacement account is adequately funded to meet future capital repair needs.

In order to document the energy/water retrofit work completed, the Owner/Agent must:

1. Submit a narrative of the scope of work compared to the work completed (a sample narrative is attached—Appendix B). The scope of work does not have to remain the same throughout the incentive period. If the scope of work changes, the Owner/Agent should notify the Multifamily Hub/Program Center by submitting a modified or new scope of

work as needed/applicable. In the case where the scope of work is modified, it is assumed that the estimated cost averted line item would also change to incorporate the newly estimated costs averted. The change in energy and water costs averted should be reflected in a revised Form HUD-92457-A submitted at the time of annual contract renewal.

AND

2. Accommodate requests from the Multifamily Hub/Program Center for additional information.

Part 5: Submission and Review Process

The Owner/Agent should submit the above (outlined in Parts Three and Four) for each property for which the Owner/Agent would like to realize the PRAC Shared Savings incentive at the time of contract renewal (or the contract anniversary date if the contract is still in the initial term), and copy the Office of Multifamily Housing Programs at MFBBC@HUD.gov, attention Lauryn Alleva.

The submitted request should include a print out of the participating BBC Multifamily Partner's profile page from the Better Buildings Challenge website (http://www4.eere.energy.gov/challenge/) and a short description of the applying entity's relationship to the Partner. Please see Appendix C for instructions on printing and submitting the Partner's profile page.

The Multifamily Hub/Program Center will review the above information and if approved allow the energy and water costs averted to be included on the Fuel Oil/Coal line item of the property's budget worksheet (Form HUD-92457-A). If there are noted deficiencies in the Owner/Agent's documentation, the Multifamily Hub/Program Center will notify the Owner/Agent and provide them with thirty days to cure any deficiencies.

The energy and water costs averted will be included in the budget worksheet (Form HUD-92457-A) on the designated Fuel Oil/Coal line item every year from the first year that energy and water improvements result in savings, for no more than 12 years from the first year the energy and water costs averted are included in the budget. For each year after the initial year, the line item should be adjusted by the UAF/OCAF to reflect changes in utility costs. The Owner/Agent will reflect any increase in energy and water costs averted in the annual budget worksheet (Form HUD-92457-A) if the Owner/Agent chooses to undertake additional energy/water retrofits during the 12-year incentive period. For these additional costs averted, the Owner/Agent may only add to the cost averted line item for 12 years less the number of years that have passed since their initial request for use of the incentive. Please see Appendix B for further explanation of this concept.

The Department will continue to evaluate this policy and will make adjustments as needed to support the goals of the BBC. We have attempted to expedite this memo in order to facilitate the use of the "pay for success" concept, and we welcome your feedback. Specifically, the Department is interested in feedback on the administrative process of this incentive. Please send feedback to the attention of Lauryn Alleva at MFBBC@HUD.gov.

Appendix A

Form HUD-92457-A:

Budget Worksheet
Income and Expense Projections

U.S. Department of Housing and Urban Development
Office of Housing
Federal Housing Commissioner

OMB Approval No. 2502-0324 (exp. 12/31/2014)

Public reporting burden for this collection of information is estimated to average 1.5 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number.

This information is collected in accordance with Title II of the National Housing Act which requires that HUD regulate rents for certain cooperative and subsidized rental projects. The Department formulated the processes by which owners could request increases. The requiremen for tenant participation in the rent increase process, which is included in Section 202(b) of the HCD Amendments of 1978, necessitated that the Department design procedures to give consideration to tenant comments. The information gathered is not of a confidential nature. The information is required in order to obtain benefits.

Project Number	Name of Project

Description of Account		Acct.No	Statement of Profit/Loss FY__	Current FY (no. of mos.)	Budget from ( ) to ( )
Rental Income 5100	Rent Revenue - Gross Potential	5120			
	Tenant Assistance Payments	5121			
	Rent Revenue - Stores and Commercial	5140			
	Garage and Parking Spaces	5170			
	Flexible Subsidy Revenue	5180			
	Miscellaneous Rent Revenue	5190			
	Excess Rent	5191			
	Rent Revenue/ Insurance	5192			
	Special Claims Revenue	5193			
	Retained Excess Income	5194			
	Total Rent Revenue Potential at 100% Occupancy	5100T			

Specific line items for the PRAC Shared Savings incentive for BBC Multifamily Partners:

Description of Account		Acct.No	Statement of Profit/Loss FY__	Current FY (no. of mos.)	Budget from ( ) to ( )
Utilities 6400	Fuel Oil/Coal	6420	**Energy and Water Costs Averted Here**		
	Electricity	6450			
	Water	6451			
	Gas	6452	**Combine Fuel Oil/Coal and Gas Expenses Here**		
	Sewer	6453			
	Total Utilities Expense	**6400T**			
Operating & Mainten. Expenses 6500	Payroll	6510			
	Supplies	6515			
	Contracts	6520			
	Operating and Maintenance Rent Free Unit	6521			
	Garbage and Trash Removal	6525			
	Security Payroll/Contract	6530			
	Security Rent Free Unit	6531			
	Heating/Cooling Repairs and Maintenance	6546			
	Snow Removal	6548			
	Vehicle & Maint. Equip. Oper. and Repair	6570			
	Misc. Operating & Maintenance Expenses	6590			
	Total Operating & Maintenance Expenses	**6500T**			
Taxes and Insurance 6700	Real Estate Taxes	6710			
	Payroll Taxes (Project's share)	6711			
	Property and Liability Insurance (Hazard)	6720			
	Fidelity Bond Insurance	6721			
	Workmen's Compensation	6722			

Appendix B

Sample Narrative

Project Green plans to complete the following improvements to realize utility savings at Project Green as part of their participation in the Better Buildings Challenge:

Utility Savings Type	**Energy/water Retrofit Measure Implemented**	**Anticipated Savings Over 12 Year Period, starting in <u>FY15</u>** **(Estimated Annual Amount Saved x 12 beginning on the date of the first budget worksheet submission)**
Electric		
	Replace non-Energy Star appliances with Energy Star appliances	$6,000
	Add lines as needed.	
Water		
	Replace toilets with low-flush toilets	$10,000
	Install low-flow showerheads and aerators	$3,000
	Add lines as needed.	
Gas		
	Install a central high-efficiency heating plant (boiler, furnace)	$12,000
	Add lines as needed.	
Total:		**$31,000**

These improvements will be completed over the course of five years and funded by reserve for replacement funds and realized utility savings.

Appendix B continued.

As of the date of this budget worksheet (Form HUD-92457-A), the following have been completed to achieve this goal. This resulted in $1,600 in utility cost savings in the first year:

	Energy/Water Improvement	**Actual Energy/Water Costs Averted in Year Reporting: 2014** ***(Identify the Year Here)***
Electric		
	Replace non-Energy Star appliances with Energy Star appliances	$400
Subtotal Electric:		((base year's electric cost X UAF for electricity)-current year's electric cost) = $400
Water		
	Replace toilets with low-flush toilets	$100
	Install low-flow showerheads and aerators	$100
Subtotal Water:		((base year's water cost X UAF for water)-current year's water cost) = $200
Gas		
	Install a central high-efficiency heating plant (boiler, furnace)	$1,000
Subtotal Gas:		((base year's gas cost X UAF for gas)-current year's gas cost) = $1,000
Total:		**$1,600**

The total $1,600 should be recorded on Form HUD-92457-A on the Fuel Oil/Coal line item (Acct. No. 6420) for the budget year that begins in 2015. For the following 11 years (total of 12 years allowed), the utility savings from the first year should be broken out by utility and each utility adjusted by the UAF for that specific utility or adjusted by OCAF if the UAF is not available. The separate adjusted utility savings should be summed and included on the Fuel Oil/Coal line item for that budget year. If there are additional changes made that are expected to generate additional savings, an updated narrative should be submitted and the costs averted line item should be updated to reflect the savings generated from the additional improvements.

Please see the following page for an example of how the savings would be reported for 12 years.

Appendix B, continued—Example:

Project Green undergoes energy/water retrofit per schedule above in 2014. The contract renewal date is April 22, 2015 (Earth Day!). Upon submittal of the budget for the period April 22, 2015 to April 21, 2016 and the subsequent 11 years, the Owner/Agent's line 6240 would look like this:

	Contract year ending 2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
6240	$1,600	Split the $1,600 utility savings out by utility and multiply by the UAF for each utility. Enter the sum of the adjusted utilities here.	Repeat 2017 Process										$0

If Project Green undergoes further renovation in 2020, they would need to submit a second narrative explaining the work completed in 2020.

Updated Narrative:

Utility Savings Type	Energy/water Retrofit Measure Implemented	Anticipated Savings Over 12 Year Period, starting in <u>FY15</u> (Estimated Annual Amount Saved x 7 beginning on the date of the amended budget worksheet submission)
Electric		
	Replace non-Energy Star appliances with Energy Star appliances	$6,000
Added in 2020	Install timers on lights in common areas	$700
Water		
	Replace toilets with low-flush toilets	$10,000
	Install low-flow showerheads and aerators	$3,000
	Add lines as needed.	
Gas		
	Install a central high-efficiency heating plant (boiler, furnace)	$12,000
Added in 2020	Install timer on boiler	$1,400
Total:		**$33,100**

	Energy/Water Improvement	Actual Energy/Water Costs Averted in Year Reporting: 2014 (*Identify the Year Here)*
Electric		
	Replace non-Energy Star appliances with Energy Star appliances	$400
Added in 2020	Install timers on lights in common areas	$100
Subtotal Electric:		((base year's electric cost X UAF for electricity)-current year's electric cost) = $500
Water		
	Replace toilets with low-flush toilets	$100
	Install low-flow showerheads and aerators	$100
Subtotal Water:		((base year's water cost X UAF for water)-current year's water cost) = $200
Gas		
	Install a central high-efficiency heating plant (boiler, furnace)	$1,000
Added in 2020	Install timer on boiler	$200
Subtotal Gas:		((base year's gas cost X UAF for gas)-current year's gas cost) = $1,200
Total:		**$1,900**

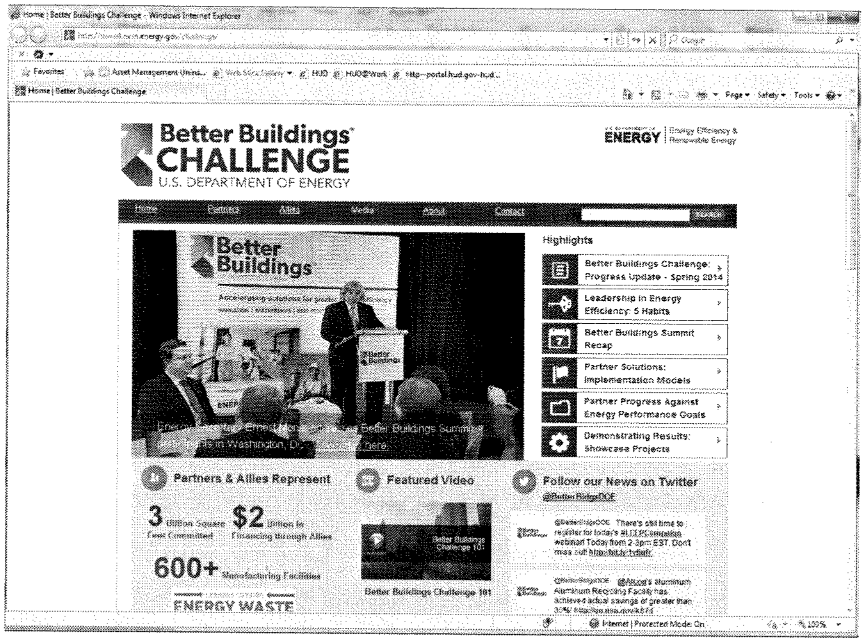
The budget report would then look like the following starting in the budget submitted for 2021.

	Contract year ending 2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
6240	$1,600	Split the $1,600 utility savings out by utility and multiply by the UAF for each utility. Enter the sum of the adjusted utilities here.	Repeat 2017 Process		Sum for all utilities: (Baseline broken out by utility X UAF by utility)-current year's utility cost	Split the 2020 utility savings out by utility and multiply by the UAF for each utility. Enter the sum of the adjusted utilities here.	Repeat 2021 Process						$0

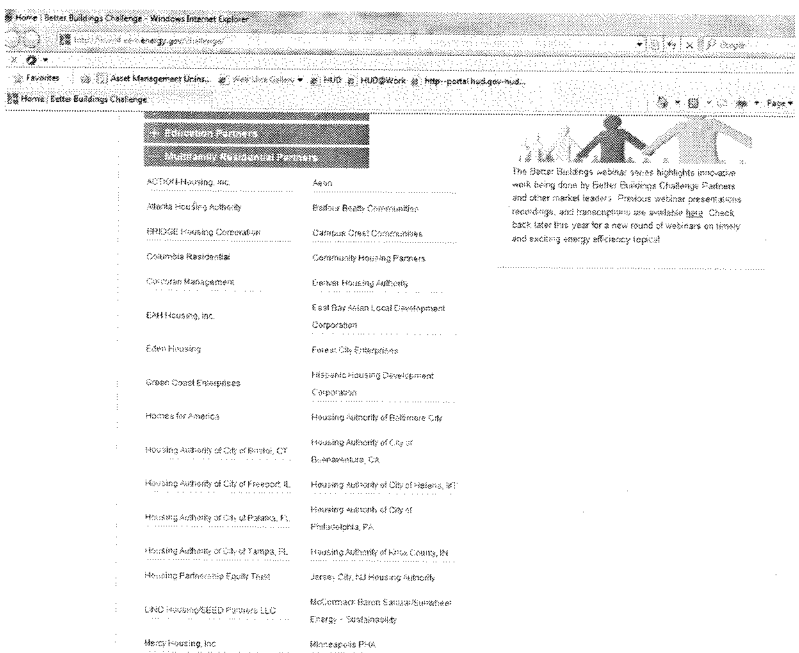
The Owner/Agent is allowed to include the costs averted for only 12 years from the initial request (the initial request is the first year of the 12 year period). If an additional request is made, the costs averted may only be included up until the initial 12 year period has been reached. Therefore, it is advantageous for the Owner/Agent to begin with the work that has the longest payback period.

Appendix C

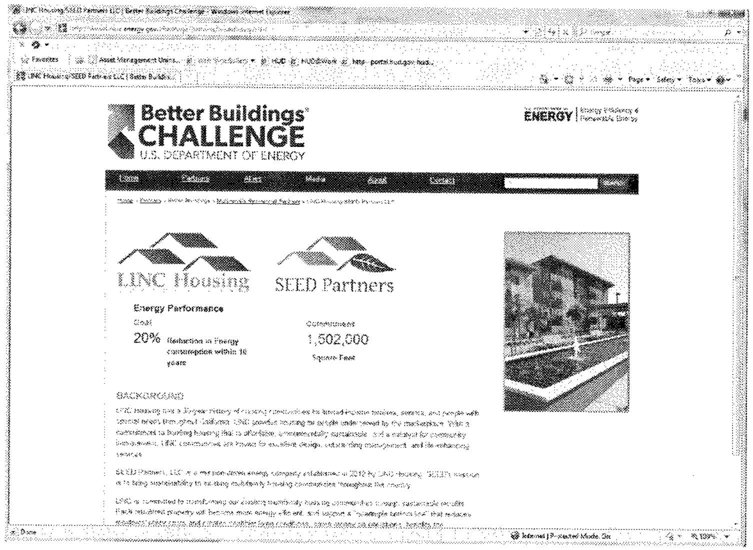
1. Navigate to the Better Buildings Challenge Homepage at http://www4.eere.energy.gov/challenge/ :



2. Scroll down to the Multifamily Residential Partners' tab:



3. Find and click on the BBC Multifamily Partner's name:



4. Include a short description of the applying entity's relationship to the BBC Multifamily Partner.