

**DEPARTMENT OF HOUSING AND  
URBAN DEVELOPMENT****24 CFR Part 990****[Docket No. FR-4425-I-12]****RIN 2577-AB88****Allocation of Operating Subsidies  
Under the Operating Fund Formula**

**AGENCY:** Office of the Assistant Secretary for Public and Indian Housing, HUD.

**ACTION:** Interim rule.

**SUMMARY:** This interim rule implements an interim Operating Fund Formula for determining the payment of operating subsidies to public housing agencies (PHAs). The interim rule follows publication of a July 10, 2000 proposed rule, and takes into consideration the public comments received on the proposed rule. As required by statute, the July 10, 2000 proposed rule was developed through negotiated rulemaking procedures. The policies and procedures described in the interim rule will govern the determination of funding distributions to PHAs under the Operating Fund until a final rule, reflecting the results of a Congressionally requested public housing cost study, is developed and published.

**DATES:** *Effective Date:* April 30, 2001.  
*Comments Due Date:* May 29, 2001.

**ADDRESSES:** Interested persons are invited to submit comments regarding this interim rule to the Rules Docket Clerk, Room 10276, Office of General Counsel, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410. Comments should refer to the above docket number and title. A copy of each comment submitted will be available for public inspection and copying during regular business hours at the above address. Facsimile (FAX) comments are not acceptable.

**FOR FURTHER INFORMATION CONTACT:** Steve Sprague, Funding and Financial Management Division, Office of Public and Indian Housing, Room 4216, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410; telephone (202) 708-1872 (this telephone number is not toll-free). Hearing or speech-impaired individuals may access this number via TTY by calling the toll-free Federal Information Relay Service at 1-800-877-8339.

**SUPPLEMENTARY INFORMATION:****I. Background—The July 10, 2000  
Proposed Rule**

On July 10, 2000 (65 FR 42488), HUD published for public comment a proposed rule to implement an Operating Fund Formula for determining the payment of operating subsidies to public housing agencies (PHAs). As required by statute, the July 10, 2000 proposed rule was developed through negotiated rulemaking procedures. The proposed rule was the first stage in the rulemaking process that will establish a final Operating Fund Formula.

HUD currently uses a formula approach called the Performance Funding System (PFS) to distribute operating subsidies to PHAs. HUD's regulations implementing the PFS can be found at 24 CFR part 990. On October 21, 1998, the Congress enacted the Quality Housing and Work Responsibility Act of 1998 (Pub. L. 105-276) (QHWRA). Section 519 of QHWRA establishes an Operating Fund for the purpose of making assistance available to PHAs for the operation and management of public housing. Further, section 519 requires that the assistance to be made available from that fund be determined using a formula developed through negotiated rulemaking procedures as set forth in subchapter III of chapter 5 of title 5, United States Code, commonly referred to as the Negotiated Rulemaking Act of 1990.

On March 16, 1999 (64 FR 12920), HUD published a notice announcing the establishment of its Negotiated Rulemaking Committee on Operating Fund Allocation (the "Committee"). The Committee membership included representatives of PHAs; the three national organizations representing PHAs—PHADA, CLPHA, and NAHRO; resident organizations; low-income housing groups; and HUD. Additionally, two representatives from the Federal Mediation and Conciliation Service served as facilitators.

The July 10, 2000 proposed rule was the product of the Committee's successful negotiations, and reflected the consensus decisions reached over nearly a year's worth of deliberations. The proposed rule thus represented a partnership among HUD, the PHAs, public housing residents, and advocates of public housing.

The July 10, 2000 proposed rule set forth several important modifications to the existing PFS regulations. These modifications were designed to address, to the extent feasible under data available to the public, several specific proposals considered important by

members of the Committee. The proposed rule also contained several clarifying and technical changes to the PFS regulations and to remove several obsolete provisions.

The most significant changes to the current PFS regulations that were contained in the July 10, 2000 proposed rule are described below. The July 10, 2000 rule proposed to:

1. Modify the method by which "small PHAs" are funded in order to assure an adequate minimum level funding, based on nationally averaged operating costs for multifamily housing projects insured by the Federal Housing Administration (FHA), adjusted for unit size differences and locational cost differences;

2. Implement statutory changes permitting PHAs to retain certain rental and non-rental income without offset against operating subsidy;

3. Retain the current method of estimating utility expenses, require that the comparison of actual and estimated utility costs be reported to HUD within 45 days after the end of the fiscal year, but then have the PHA incorporate the adjustment into the operating subsidy calculation for the second, rather than the first PHA fiscal year following the year being adjusted;

4. In order to encourage energy efficiency, replace the current 50-50 split of savings or increase in cost due to changes in utilities consumption to a 75-25 split between PHAs and HUD, respectively;

5. Require each PHA to include in its operating subsidy calculation, \$25 per occupied unit per year for resident participation activities as an add on expense component for subsidy eligibility; and

6. Include flood insurance costs in the computation of the Allowable Expense Level (AEL) by permitting a one-time permanent adjustment to reflect this cost.

The preamble to the July 10, 2000 proposed rule provides additional details regarding the proposed amendments to 24 CFR part 990.

**II. This Interim Rule; Development of  
Final Rule**

This interim rule makes effective the policies and procedures contained in the July 10, 2000 proposed rule, and takes into consideration the public comments received on the proposed rule. This interim rule will govern the determination of funding distributions to PHAs under the Operating Fund until a final rule, reflecting the results of a Congressionally requested public housing cost study, is developed and published.

Following and based upon the findings and recommendations of the completed cost study and QHWRA, HUD will develop the final rule implementing the Operating Fund Formula, using the procedures of the Negotiated Rulemaking Act of 1990, subject to compliance with applicable legal requirements prerequisite to the establishment of a negotiated rulemaking committee for such purpose.

### III. The Operating Cost Study

The Conference Report to the FY 2000 HUD Appropriations Act (Public Law 106-74, approved October 20, 1999) states, in part, that “\* \* \* before a proposed rule is published in the **Federal Register**, the conferees direct HUD to contract with the Harvard University Graduate School of Design to conduct a study of the cost incurred in operating well-run public housing and provide the results to the negotiated rulemaking committee and the appropriate congressional committees \* \* \*.” (Congressional Record of October 13, 1999, H10007).

HUD has entered into a cooperative agreement with Harvard University. The research design for the study is under development. HUD has directed Harvard University, as the cost study contractor, to provide public opportunities (such as periodic forums, status reports, and other means) for interested persons and organizations to be informed of the study’s research design, methodologies, and progress, and to provide input and feedback for consideration in the development of the study. Harvard University will also consult with interested individuals and organizations in developing the cost study findings and recommendations. In addition, Harvard University will receive and consider the public comments on the July 10, 2000 proposed rule as part of its work on the cost study.

### IV. Differences Between This Interim Rule and the July 10, 2000 Proposed Rule

The differences between this interim rule and the July 10, 2000 proposed rule are described below. HUD has made three non-substantive changes to the proposed rule for purposes of clarity and to remove an obsolete reference. The proposed rule represented the consensus decisions reached by the members of the Negotiated Rulemaking Committee, including current residents of public housing, individual PHAs, national PHA associations, and a number of public interest groups. Further, this interim rule is a temporary regulatory measure until completion of

the Congressionally mandated cost study and subsequent publication of the final rule. Accordingly, HUD believes it would not be appropriate to make substantive revisions to the proposed rule at this interim rule stage.

HUD is deferring consideration of major modifications to the policies and procedures contained in the proposed rule until completion of the cost study. Harvard University will receive and consider the public comments on the proposed rule during development of the public housing operating cost study. The cost study will form the basis of HUD’s final rule implementing the Operating Fund. The suggestions made by the commenters will be reevaluated at the final rule stage (along with the public comments submitted on this interim rule), and may be reflected in the substance of the final rule.

The changes made by this interim rule are as follows:

1. *Removal of obsolete reference to the Turnkey IV program (§ 990.103(c)).* The interim rule revises § 990.103(c) (which lists several HUD programs to which the Operating Fund does not apply) to remove an obsolete reference to the Turnkey IV program.

2. *Clarification of applicability of Operating Fund Formula to non-PFS PHAs (§ 990.103(d)(2)).* This interim rule revises § 990.103(d)(2) to clarify the applicability of the Operating Fund Formula to housing owned by the PHAs of the Virgin Islands, Puerto Rico, Guam and Alaska (the “non-PFS PHAs”). Section 990.103(d)(1) lists the provisions of the 24 CFR part 990 that apply to these PHAs. Section 990.103(d)(2) states that, otherwise, the Operating Fund Formula is not applicable to the non-PFS PHAs. This interim rule clarifies that the provisions of 24 CFR part 990 apply to the non-PFS PHAs, to the extent required to give full effect to the provisions identified in § 990.103(d)(1).

3. *Correction of typographical error regarding PHA retention of increased rental revenue (§ 990.109(b)(1)(iii)).* In response to public comment, this interim rule corrects a typographical error at § 990.109(b)(1)(iii), which states the method for calculating increases in rental revenue. The correction is necessary to clarify that PHAs may retain 50 percent of increased rental revenue.

### V. Discussion of the Public Comments Received on the July 10, 2000 Proposed Rule

The public comment period for the July 10, 2000 proposed rule closed on August 9, 2000. By close of business on this date, HUD had received 19 public

comments. Comments were submitted by PHAs; the three main organizations representing PHAs—PHADA, CLPHA, and NAHRO; resident organizations, advocates for low-income housing, other housing experts; and other organizations and individuals.

This section of the preamble presents a summary of the significant issues raised by the public commenters, and HUD’s responses to the comments. The summary of comments that follows presents the major issues and questions raised by the commenters. The underlined headings present the issue or question, and are followed by a brief description of the commenter’s reasoning and HUD’s response to the comments.

#### *A. Comments Regarding the FHA-Based AEL (FHAEL) Adjustments for Small PHAs (§ 990.105(e))*

The July 10, 2000 proposed rule would modify the method by which “small PHAs” are funded in order to assure an adequate minimum level funding based on nationally averaged operating costs for multifamily housing projects insured by the Federal Housing Administration (FHA), adjusted for unit size differences and locational cost differences. Small PHAs with under 250 units would use the higher of their current Allowable Expense level (AEL) or 85% of the FHA-Based AEL (referred to as the FHAEL). AELs for small PHAs with 250–500 units would be set at the higher of the small PHA’s current AEL or 70% of the FHAEL. The cost of these increases would be achieved by reducing the AELs of PHAs with more than 500 units. The July 10, 2000 proposed rule would provide an exception to this determination for small PHAs with AELs that are greater than 120% of the FHAEL, in which case the small PHAs would use an AEL equivalent to 120% of the FHAEL.

*Comment: Support for FHAEL adjustments.* One commenter supported the proposed FHAEL adjustment for small PHAs. The commenter wrote that these adjustments will help small PHAs to make up for backlogged maintenance, deal with the need for improvements in computer automation, and perhaps hire more staff to administer to the needs of their residents. The commenter, however, also wrote that many PHAs—small and large alike—will not receive adequate funding under the proposed rule. “This is another reason why the rule must be temporary; housing authorities should not be expected to perform their mission with a level of funding that no other housing provider (such as FHA insured providers) would expect or accept.”

*HUD Response.* The rule is being published as an interim rule in recognition that a study of public housing operating costs is needed before a final operating subsidy formula can be developed. HUD entered into a Cooperative Agreement with Harvard University in May 2000 for such a study.

*Comment: FHAEL adjustment factor is inadequate.* One commenter wrote that the proposed calculation of the FHAEL is "fair and reasonable." However, the commenter wrote that proposed FHAEL adjustments would continue the perceived inequities in funding for small PHAs. Accordingly, the commenter recommended that small PHAs with 250–500 units be permitted to use 80% of the FHAEL (rather than the proposed 70%). The commenter also suggested that all PHAs (small and large) who use less than 70% of the FHAEL should receive an additional one-time funding bonus in fiscal year 2001.

*HUD Response.* The commenter remarks that using FHA multifamily operating costs appears to be fair and reasonable. While the Committee agreed to use the data as a reference point for having PHAs raise or lower their AELs, however, there was no consensus that the FHA data should be treated as a standard. As noted above, this interim rule is a temporary regulatory measure until completion of a Congressionally mandated cost study and subsequent publication of a final rule. The question of what are appropriate operating costs for public housing is the subject of the cost study, which is being undertaken by Harvard University's Graduate School of Design under a Cooperative Agreement with HUD. HUD has decided to defer consideration of major revisions to the policies and procedures contained in the proposed rule until completion of the cost study. Harvard University will review the public comments on the July 10, 2000 proposed rule during the development of the cost study. The suggestions made by the commenters will be reevaluated at the final rule stage (along with the public comments received on this interim rule), and may be reflected in the substance of the final rule.

*Comment: FHAEL adjustments should be made for all PHAs.* One commenter recommended that, rather than limit FHAEL adjustment to small PHAs, HUD should make a one-time adjustment for all PHAs to raise their AELs to the FHAEL level.

*HUD Response.* HUD has not adopted the suggestion made by the commenter. As noted above, this interim rule is a temporary regulatory measure until

completion of the Congressionally mandated cost study and subsequent publication of the final rule. HUD believes it would not be appropriate to make substantive revisions to the proposed rule at this interim rule stage. Accordingly, HUD is deferring consideration of major changes to the policies and procedures contained in the proposed rule until completion of the cost study. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggestions made by the commenters will be reevaluated at the final rule stage (along with the public comments submitted on this interim rule), and may be reflected in the substance of the final rule.

*Comment: Large PHAs should not be required to subsidize FHAEL adjustment for small PHAs.* Two commenters wrote that addressing funding deficiencies for small PHAs should not result in reduced AEL levels for large PHAs. The commenters wrote that there is "incontrovertible evidence that large and medium-sized PHAs are also woefully underfunded."

*HUD Response.* The decision to make a one-time, permanent adjustment of 1.36% to the AELs of PHAs with 500 or more units was achieved through consensus among Committee members. When all the changes contained in the interim rule are taken into account, however, including changes in the treatment of investment, dwelling rental, and non-rental income, all but a relatively small number of medium and large PHAs are expected to receive increased subsidy support. Whether PHAs are under- or over-funded is a question that will be addressed in the public housing operating cost study being undertaken by Harvard University.

*Comment: Proposed FHAEL adjustments are based on inadequate data.* One commenter wrote that "FHA data have clear limitations that should be noted in any discussion of how the new AELs are calculated." According to the commenter, the FHA data used by the Committee was insufficient for the urban markets where most large PHAs operate. "These discrepancies in data speak loudly to the need to conduct a fresh study of public housing costs."

*HUD Response.* The Committee did recognize that there were limitations on the use of the FHA multifamily operating cost data and agreed that the data would be used as a reference point and not as a standard.

*Comment: HUD should publish FHAEL data and formulas for each PHA.* Three commenters suggested that

HUD should publish the data and formulas used to calculate the FHAEL for each PHA. The commenters wrote that publication of this information is necessary so that PHAs can assess the impact of the proposed FHAEL adjustments on their operations.

*HUD Response.* Data was presented to the Committee and later made available to the public housing community that modeled what the impact would be on individual PHAs if the changes agreed to by the Committee, including FHAEL adjustments, had been implemented in 1998. HUD will publish FHAEL factors for review and use by individual PHAs before they submit their subsidy calculations for their respective fiscal years beginning in 2001.

*Comment: How can the FHAEL be made applicable in FY 2001 using FY 2000 data, when the year 2000 has not yet been completed or the necessary data compiled?* One commenter posed this question.

*HUD Response.* AELs for a particular year are established at the start of a PHA's fiscal year and normally remain unchanged for the entire year. For calendar year 2000, the factors needed by PHAs to determine their AELs for their fiscal years beginning in 2000 (i.e., January 1, 2000, April 1, 2000, July 1, 2000, and October 1, 2000), have been available since February 2000. Under this interim rule, a PHA will compare its current HUD-approved AEL for 2000 with its FHAEL for a possible adjustment upwards or downwards depending on its size. That adjusted AEL will then become the starting AEL for its 2001 fiscal year and will be further adjusted for a local inflation factor and a factor reflecting the aging of its housing stock.

*B. Comments Regarding the Treatment of Non-Rental Income—Exclusion of Investment Income and Revised Definition of Other Income (§§ 990.102, 990.109, and 990.110)*

The amount of operating subsidy received by a PHA is generally calculated by determining the difference between projected expenses and projected income. Projected income is categorized as being either dwelling rental income, investment income, or "other income." The July 10, 2000 proposed rule would revise the definition of other income (for purposes of calculating subsidy) to only include income from: (1) Rents billed for dwelling units rented for non-dwelling purposes; and (2) charges to residents for excess utility consumption of PHA supplied utilities. Under the proposed definition, investment income would

not be used to determine operating subsidy eligibility.

*Comment: Support for revised definition of "other income".* Three commenters expressed support for these provisions. The commenters wrote that these changes begin to remove the disincentives faced by PHAs and reward activities that will ultimately benefit public housing residents and their communities.

*HUD Response.* The changes in the treatment of investment and other income represent the Committee's response to QHWRA's requirement that a PHA that receives income from nonrental sources be able to retain and use such amounts without any decrease in the amounts received from the Operating Fund.

*Comment: Success of this provision depends on full funding for the Operating Fund Formula.* One commenter cautioned that "this provision is only beneficial to the extent that HUD requests—and Congress provides—sufficient funding for the" Operating Fund Formula. The commenters urged HUD not to reduce its operating subsidy requests on the grounds that PHAs may now keep more of their investment and other income. According to the commenter, such an action would "undermine the incentives envisioned in both the rule and the underlying statute."

*HUD Response.* HUD recognizes the importance of adequate funding levels for operating subsidies.

### C. Comments Regarding the Computation of Projected Monthly Dwelling Rental Income (§ 990.109)

The July 10, 2000 proposed rule would amend § 990.109 to revise the method for calculating projected monthly dwelling rental income. Under the proposed rule, a PHA would determine its average monthly dwelling charge for the month that is six months before the start of its budget year (the "current year average") as well as the average monthly charge for the comparable month of its two previous years. An average would be computed for these three amounts (the "three year average") and compared with the current year average. If the current year average is not higher than the three-year average, rental income has not increased and the current year average will be used to calculate projected rental income.

If the current year average is higher than the three year average, the PHA shall be allowed to retain 50% of any increases in dwelling rental income, so long as the PHA uses the increased revenue for the provision of resident-

related improvements and services as described in new § 990.116. The retained income will not be recognized in the PHA's calculation under the Interim Operating Fund Formula. The projected dwelling rental income for PHAs with increased rental income will be based on the three-year average plus 50% of the increase.

A change factor of 3% will then be applied. HUD intends to revise the 3% adjustment factor, for the duration of the interim rule, beginning in FY 2002, to more accurately reflect the inflationary pressure on the projection of monthly dwelling rental income. In determining such a factor for FY 2002, HUD will also take into consideration any negative impacts on incentives for PHAs to increase resident earned income, relevant and available indices of rental income inflation, historical trends in rental income changes, and the proportion and amount of increased income retained by PHAs using the rolling base method. There will be consultation with the appropriate stakeholders regarding the methodology for determining change factors to be used by HUD followed by publication of written notice and an opportunity for public comment.

*Comment: Support for revised computation of projected monthly dwelling rental income.* Four commenters supported the proposed changes to the computation of projected monthly dwelling rental income. The commenters wrote that the proposed revisions would prevent unusually high or low rental income years from drastically impacting projections of rental income. One of the commenters wrote that this "incentive based approach is in the spirit of [QHWRA] and supports entrepreneurial initiatives that will ultimately improve the lives of residents."

*HUD Response.* HUD agrees with the commenters that the dwelling rental income approach adopted by the Committee is responsive to the QHWRA provision that the formula contain an incentive to encourage a PHA to facilitate increases in earned income by families in occupancy.

*Comment: This provision will not succeed unless the Operating Fund is fully funded.* One commenter wrote, "this approach will not succeed unless the Operating Fund is fully funded." The commenter wrote that HUD "must accurately estimate 100% of the Operating Fund need and HUD must request an appropriation for full funding of operating subsidies." According to the commenter, HUD has consistently underestimated operating subsidy need. The commenter urged "HUD to consult

with its public housing partners in advance of the appropriations request to discuss and revise these estimates."

*HUD Response.* Budget forecasting is not an exact science and HUD continually tries to improve the data sources and techniques used for its projections. For example, HUD has agreed to review the current rental change factor for a possible change in FY 2002. Any changes to this factor will be done in consultation with HUD's public housing partners and will be followed by written notice and an opportunity for public comment.

*Comment: PHAs should be required to certify that they have complied with the statutory earned income disregard under 42 U.S.C. 1437a(d) and HUD's implementing regulation at 24 CFR 960.255.* Two commenters wrote that the proposed provision allowing PHAs to retain 50% of increased rental revenues may unintentionally create a disincentive for PHAs to implement the statutory earned income disregard. PHAs that comply with the required disregard will have lower dwelling rental income than if they count all resident earnings in determining rental income. The commenters suggested that PHAs should be required to certify that they have fully implemented the mandatory earned income disregard. One of the commenters suggested that this certification should accompany the PHA's operating budget submission to HUD. This commenter also recommended that the PHA's policy regarding the mandatory earned income disregard and the rent certification forms used by the PHA to implement the mandatory disregard should be attached to the certification. The second commenter wrote that if HUD does not have a simple administrative means to verify the validity of the PHA's certification (through MTCS data or otherwise), the PHA should be required to submit data concerning the number of families receiving the benefit of the mandatory disregard.

*HUD Response.* HUD does not believe that the treatment of dwelling rental income adopted by this interim rule may unintentionally create a disincentive for PHAs to implement the statutory earned income disregard. With regard to the commenters' suggestion that PHAs be required to certify that they have fully implemented the mandatory earned income disregard, HUD already requires that a PHA separately certify when submitting its Operating Budget and/or subsidy calculation that "all regulatory and statutory requirements have been met" and that "all proposed rental charges and expenditures will be consistent

with the provisions of law.” These certifications clearly encompass the requirement on a PHA to fully implement the earned income disregard. HUD has a broad range of enforcement actions from which it can draw, including withholding of assistance or ordering corrective action, in the event the certifications are violated.

*Comment: The proposed retention of increased rental revenues should be designed to reward PHAs that encourage and support increased earnings for existing public housing residents—and not to encourage the recruiting of new residents with higher incomes.* Five commenters wrote that the proposed rule inappropriately fails to distinguish between increased rents due to admission of higher income families and higher rent charges resulting from the increased earnings of current residents. Two of the commenters wrote that section 519(e)(2)(B) of QHWRA (entitled “Incentives to Increase Certain Rental Income”) requires the Operating Fund Formula to create an incentive for PHAs to increase the earnings of “families in occupancy” (emphasis added). According to the commenters, the proposed rule creates an inappropriate financial incentive to admit the highest income applicants. “Moreover, the formula places the incentive to increase the income of current tenants on a par with the incentive to seek out new tenants with higher income. Congress did not intend such a result.”

*HUD Response.* HUD believes that the dwelling rental income methodology developed by the Committee is both appropriate and responsive to the Congressional directive that the formula contain an incentive to PHAs that would facilitate increases in earned income by families in occupancy. It is appropriate because the proposal was developed using negotiated rulemaking, as required by QHWRA, and the approach represented a consensus among a broad range of interests that included current residents of public housing, individual public housing agencies, national PHA associations, and a number of public interest groups. It is responsive because the Committee decided that the benefits resulting from increased income would not be used for general low-income purposes, as permitted by the incentive, but rather would be used for the provision of resident-related improvements and services, including the funding of optional earned income exclusions. The uses must be developed with front-end resident participation and be made part of the PHA plan submission.

HUD supported and helped shape this compromise because of its relative administrative simplicity and its ability to provide resources that PHAs can use to help residents already in occupancy increase their earned incomes. Because the statute speaks specifically of an incentive to facilitate increases in earned income by families in occupancy, HUD will reexamine at the final rule stage whether there is a way to provide this incentive that is just as effective and not administratively burdensome.

*Comment: Earnings of newly admitted residents should be excluded from the determination of the “current year” and “three year” averages.* Related to the preceding comment, one commenter wrote that it would not be administratively difficult to narrow the retained revenue incentive to apply only to the increased earnings of existing residents. The commenter suggested that the rent paid by households admitted to the PHA’s public housing program in the “current year” should be excluded from the determination of the “current year average dwelling rental charge” under proposed § 990.109(b)(1). For a fair comparison, rents paid by newly admitted families in each year used to determine the “three year average” would also be excluded. After the initial year of admission, all rents (and therefore incomes) would be included in the PHA’s average rental charge calculations. In this way, increases in families’ income beginning in the year after they are admitted to public housing would be captured to determine whether a PHA’s average rental revenue has increased and the amount of revenue the PHA is permitted to retain.

*HUD Response.* HUD has not adopted the suggestion made by the commenter. As noted above, this interim rule is a temporary regulatory measure until completion of the Congressionally mandated cost study and publication of the final rule. HUD has decided to defer consideration of major changes to the policies and procedures contained in the proposed rule until completion of the cost study. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggestion made by the commenter will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

*Comment: The interim rule should establish a base amount of income for every tenant and only allow the PHA to retain increases in income if the tenant’s income increases above the base.* One commenter made this suggestion to

narrow the scope of the retained rental revenue incentive. The commenter wrote that PHAs must already calculate every tenant’s income and report that income to HUD as part of the MTCS. The commenter suggested that the base for all current residents should be established on the effective date of the interim rule. The base for all new tenants would be determined on their date of admission to public housing. If a tenant’s income increases above the base, PHAs would be allowed to retain 50% of the increased rental revenue. The commenter also suggested that a family’s base be adjusted due to changes in family composition.

*HUD Response.* HUD has not adopted the suggestion made by the commenter. As noted, HUD does not believe it would be appropriate to make substantive revisions to the proposed rule at this interim rule stage. HUD is deferring consideration of major changes to the policies and procedures contained in the proposed rule until completion of the operating cost study. The study will form the basis for HUD’s final rule implementing the Operating Fund Formula. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggestion made by the commenter will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

*Comment: Suggested correction of typographical error.* Paragraph (b)(1)(iii) of § 990.109 prescribes the method for calculating the amount of increased rental revenue that may be retained. This paragraph provides that the “annual amount of increased revenue retained by the PHA is calculated by subtracting the three year average from the current year average and multiplying the result by the projected occupancy percentage \* \* \* and the unit months available \* \* \*.” One commenter suggested that the phrase “50 percent of” should be inserted following the word “multiplied” in order to clarify that PHAs may retain 50 percent of increased rental revenue.

*HUD Response.* HUD agrees with the commenter that the suggested change would improve the clarity of the rule. This interim rule contains the corrected language.

*Comment: Opposition to 3% adjustment factor.* Four commenters questioned the continued use of the 3% adjustment factor. One of the commenters wrote that HUD should not assume that rental income would increase in the new budget year. According to the commenter, this is a false assumption that simply lowers the

amount of operating subsidy provided to a PHA. The commenters were appreciative of HUD's agreement to revise the factor to more accurately reflect the projection of monthly dwelling rental income in FY 2002 and beyond.

**HUD Response.** As noted above, HUD has agreed to review the current rental change factor for a possible change in FY 2002. Any changes to this factor will be done in consultation with HUD's public housing partners and will be followed by written notice and an opportunity for public comment.

*D. Comments Regarding the Use of Increases in Dwelling Rental Income (§ 990.116)*

The July 10, 2000 proposed rule would replace the current § 990.116 (which concerns three year incentive adjustments) with a new section concerning the eligible uses of increases in dwelling rental income, as calculated under § 990.109. A PHA would be required to describe the uses of the retained income in the PHA's Plan submissions under 24 CFR part 903. PHAs would also be required to develop the uses for the retained income with front-end resident participation and ongoing input. The July 10, 2000 proposed rule provides several examples of eligible uses for the retained income, including, but not limited to: physical and management improvements that benefit residents; resident self-sufficiency services; maintenance operations; resident employment and training services; resident safety and security improvements and services; and optional earned income exclusions.

**Comment:** PHAs should be required to use at least 20% of retained rental income for resident services and resident councils. One commenter made this suggestion.

**HUD Response.** HUD has not adopted the suggestion made by this commenter. HUD has decided to defer consideration of major changes to the proposed rule until completion of the operating cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The commenter's suggestion will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

**Comment:** Retained income provisions will impose an undue administrative burden. One commenter supported the use of retained rental revenues for resident-related improvements and services. However, the commenter was concerned about the monitoring and tracking of expenditures

from the retained income. The commenter wrote that both HUD funding and retained income are currently placed in the PHA's general operating fund, and funds are used for approved budget items. The commenter wrote that separating retained income from the general operating fund would create excessive account handling and recordkeeping burdens.

**HUD Response.** HUD agrees that separating, tracking, and monitoring the expenditures of the retained dwelling income would create excessive accounting and recordkeeping burdens. Neither the July 10, 2000 proposed rule, nor this interim rule, would require the PHA to separately account for, monitor, track, or report on the retained income beyond the requirement to identify the proposed uses of the estimated amount of retained income in the Annual Plan.

*E. Comments Regarding Utility Adjustments (§§ 990.107 and 990.110)*

The July 10, 2000 proposed rule would retain the current method of estimating utility expenses. In addition, the proposed rule would also continue to require that the comparison of actual and estimated utility costs be reported to HUD within 45 days after the end of the fiscal year, but would then have the PHA incorporate the adjustment into the operating subsidy calculation for the second (rather than the first PHA fiscal year following the year being adjusted). Further, in order to encourage energy efficiency, the July 10, 2000 proposed rule would replace the current 50–50 split of savings or increases in cost due to changes in utilities consumption to a 75–25 split between PHAs and HUD, respectively.

**Comment:** Support for changes in utility calculations. Two commenters expressed support for the proposed changes to the utility calculations. The commenters wrote that the proposed rule would encourage PHAs to conserve energy. One of the commenters also wrote that the proposed rule is “balanced in its approach in that risks associated with increased utility costs will continue to be absorbed by HUD while, in return, any savings will accrue to HUD.”

**HUD Response.** HUD agrees the changes will encourage PHAs to conserve energy.

**Comment:** Required conforming change to utility rate provisions of § 990.107. Two commenters noted that § 990.107(b)(2) continues to provide that if a PHA takes certain actions to reduce utility rates, it “may be permitted to retain one-half the annual cost savings” (emphasis added). The commenters suggested that the word “may” should be revised to

“shall,” in order to conform to the utility adjustment provisions of § 990.110.

**HUD Response.** HUD has not adopted the suggested change. As noted, HUD has decided to defer consideration of major changes to the proposed rule until completion of the cost study and development of the final rule. The recommendation made by the commenter will be reevaluated at the final rule stage.

**Comment:** Interim rule should provide clarification and/or examples of allowable energy conservation strategies. One commenter agreed that energy cost reduction and energy conservation efforts should be included in the Annual and Five-Year Plans, but would like clarification and/or examples of allowable energy conservation strategies.

**HUD Response.** One source of the guidance requested by the commenter is provided in HUD's 1998 publication, “Energy Conservation for Housing—A Workbook,” which is available by calling the HUD Public and Indian Housing (PIH) Information and Resource Center at 1–800–955–2232. Another source is the 1992 joint HUD/U.S. Department of Energy publication, “Energy Performance Contracting for Public and Indian Housing: A Guide for Participants” available from the HUD user web site at <http://huduser.org:80/publications/hsgfin/energy.html>.

**Comment:** A percentage of any utility savings realized by the PHA should be used for the provision of resident services. Two commenters made this suggestion.

**HUD Response.** HUD has not adopted the changes recommended by the commenters. As noted, HUD has decided to defer consideration of major changes to the proposed rule until completion of the cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggested changes will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

**Comment:** “Conversion to a less costly utility source” should be added to the examples of utility rate reductions eligible for the utility rate reduction incentive at § 990.110(b)(1). One commenter made this suggestion.

**HUD Response.** HUD has not adopted the change recommended by the commenter. As noted, HUD has decided to defer consideration of major changes to the proposed rule until completion of the cost study and development of the

final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggestion made by the commenter will be reevaluated at the final rule stage.

*F. Comments Regarding Resident Participation (§ 990.108(e))*

The July 10, 2000 proposed rule would make several amendments designed to promote resident participation in the operation of public housing. Specifically, the proposed rule would require each PHA to include, in its operating subsidy eligibility calculation, \$25 per occupied unit per year for resident participation activities. These activities include (but are not limited to) those described in 24 CFR part 964. The proposed rule would also authorize HUD to approve the use of vacant rental units for resident participation purposes and allow PHAs to receive subsidy support for those units.

*Comment: Support for proposed annual \$25 allocation for occupied units.* Four commenters supported the proposed annual \$25 allocation for occupied units. According to the commenters, this provision sends a strong message that HUD and PHAs are committed to meaningful resident participation. The commenters wrote that the proposed allocation would remove uncertainty about funding and enable resident organizations to fully participate in PHA policy decision affecting their homes.

*HUD Response.* HUD agrees that this change, along with other changes brought about by QHWRRA (such as requiring that PHAs, with certain exceptions, include a resident on their governing board), underscores the importance of resident participation to the success of public housing.

*Comment: The proposed \$25 allocation may be inadequate.* One commenter expressed concern that the proposed allocation “will not adequately fund those initiatives that are most important to \* \* \* residents.” According to the commenter, PHAs “may have to choose between income exclusions and maintenance or economic development programs.”

*HUD Response.* The \$25 is for funding of resident participation activities and not for income exclusions and maintenance or economic development programs. Income retained by PHAs as a result of increases in dwelling rental income may be a source of funds for income exclusions and maintenance or economic development programs.

*Comment: The interim rule should clarify that the \$25 allocation for*

*occupied unit is an “add-on” cost to the AEL.* Five commenters wrote that the interim rule should clarify that the \$25 allocation is calculated as an “add-on” cost to the PHA’s AEL.

*HUD Response.* This interim rule (as did the July 10, 2000 proposed rule) includes the \$25 per occupied unit as one of several “other costs” for which the PHA may receive additional subsidy eligibility. HUD believes that the interim rule language makes clear that the \$25 allocation is a calculation separate from the AEL and that the total subsidy eligibility for a PHA is the sum of all the component parts of the interim formula.

*Comment: The interim rule should provide that the annual \$25 allocation is meant to supplement any resources currently being invested by the PHA in resident participation activities, and is not meant to be in lieu of such resources.* Three commenters made this suggestion.

*HUD Response.* HUD has not adopted the changes suggested by the commenters. HUD has decided to defer consideration of substantive changes to the proposed rule until completion of the operating cost study and development of the final rule. However, HUD urges PHAs not to reduce any support now being made for resident participation activities. Furthermore, Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggested change will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

*Comment: The interim rule should clarify that the annual \$25 allocation must be used for resident participation activities and not resident services.* Two commenters wrote that while proposed § 990.108(e) specifies that the \$25 allocation is for resident participation activities, it also indicates that these activities would include those identified in 24 CFR part 964. The commenters wrote that part 964 uses the terms “resident participation” and “resident services” interchangeably. The commenters suggested that the interim rule should clarify that the funds must be used for resident participation activities and not for resident services.

*HUD Response.* The language of the July 10, 2000 proposed rule and this interim rule make clear that the \$25 is for funding of resident participation activities.

*Comment: Interim rule should describe the formula for pro-rating funding for resident participation activities.* Proposed § 990.108(e) provides that if “in any fiscal year

appropriations are not sufficient to meet all funding requirements under (part 990), the \$25 will be subject to pro-ration.” One commenter wrote that the interim rule should clarify that funding for resident participation activities will be prorated in proportion to the percentage of funding PHAs receive to meet their AEL. The commenter also suggested that the interim rule provide an example illustrating the operation of the pro-ration formula.

*HUD Response.* The pro-rating will be of the PHA’s total subsidy eligibility. HUD will provide examples of how pro-rating will impact the amount of subsidy support received for resident participation activities in separate guidance material that will be issued to PHAs.

*Comment: The interim rule should require PHAs to reflect both the calculation and allocation of the \$25 requirement as a separate line item in all relevant budget documents.* The commenter also suggested that the calculation and allocation should be reflected on a development-by-development level.

*HUD Response.* The forms to be used by PHAs to reflect the calculation of subsidy eligibility will include a separate calculation of the resident participation funding. The commenter’s suggestion that the documents also reflect the allocation of the \$25 is outside the scope of this interim rule. The Committee reached a consensus that this interim rule itself would not specify what constitutes eligible resident participation activities or how the funds received by a PHA should be allocated to the PHA and/or the resident organizations. Instead, the Committee agreed that such issues should more appropriately be considered as part of future revisions to HUD’s resident participation regulations at 24 CFR part 964.

*Comment: The interim rule should provide greater specificity regarding the eligible uses and apportionment of the \$25 allocation.* Several commenters recommended that the interim rule should establish regulatory procedures governing the eligible uses and apportionment of the \$25 resident participation allocation. For example, three commenters suggested that the interim rule should specify that the \$25 allocation must be provided to the duly elected resident council or the jurisdiction-wide resident council (if one exists). Other commenters suggested that PHAs should be required to describe in their Annual Plan the method they will use to transfer the funding to the resident organization.



*HUD Response.* As noted above, suggested revisions regarding the eligible uses and apportionment of the \$25 resident participation allocation are outside the scope of this rulemaking. The Committee agreed that such issues should more appropriately be considered as part of future revisions to HUD's resident participation regulations (24 CFR part 964).

*G. Comments Regarding the Use of Vacant Units for Resident Participation Purposes (§ 990.108(E)(2))*

*Comment: Support for proposed use of vacant rental units.* Two commenters supported the policy of providing operating subsidies for vacant units used for resident participation purposes. The commenters wrote that this policy would enhance the ability of residents to plan and implement programs that improve the quality of life in their communities.

*HUD Response.* HUD agrees that the use of vacant rental units for resident participation activities will help promote resident involvement.

*Comment: Operating subsidies should also be provided to vacant units that are used for non-dwelling purposes to promote economic self-sufficiency and anti-drug activities.* One commenter wrote that providing operating subsidies for these purposes is appropriately limited to uses that are directed toward the benefit of residents.

*HUD Response.* The interim rule makes no change to the existing policy that permits continued subsidy support, under certain circumstances, for units that are used for non-dwelling purposes to promote economic self-sufficiency and anti-drug activities.

*H. Comments Regarding the Flood Insurance Adjustment to AEL (§ 990.105(f))*

*Comment: Support for proposed adjustment.* One commenter supported the inclusion of flood insurance costs in the calculation of the AEL under a one-time and permanent adjustment.

*HUD Response.* HUD agrees that this change will simplify the subsidy calculation.

*I. Comments Regarding the Treatment of Utility and Waste Management Savings*

The preamble to the July 10, 2000 proposed rule noted that section 519 of QHWA requires that "the treatment of utility and waste management costs under the (Operating Fund) formula shall provide that a public housing agency shall receive the full financial benefit from any reduction in the cost of utilities or waste management resulting from any contract with a third party to

undertake energy conservation improvements in one or more of its public housing projects" (42 U.S.C. 1437g(e)(2)(C)). The preamble explained that the proposed rule would address this statutory requirement by retaining the current PFS provisions at § 990.107(f), which describes PHA incentives for non-HUD financed energy conservation improvements. With regard to waste management, these costs are treated as a maintenance expense (not a utilities expense) under the PFS and the July 10, 2000 proposed rule. Accordingly, should a PHA be able to reduce its waste management costs below the amount assumed in its AEL, the PHA would retain all of the savings. (The preamble discussion is located at 65 FR 42492, first and middle columns.)

*Comment: Interim rule should specify that energy incentives apply to tenant-supplied utilities.* Two commenters suggested that the interim rule should permit PHAs with "tenant-supplied" utilities to take advantage of the energy conservation incentives described in § 990.107. The first commenter wrote that HUD had been addressing this issue through the issuance of regulatory waivers. The commenter wrote that the waiver process in long and arduous, and is "necessary only because the regulations do not provide for the inclusion of such PHAs." The second commenter wrote that residential utility customers are generally at an economic disadvantage compared with larger commercial accounts serviced by a utility provider. The commenter was concerned that ongoing Federal and State utility deregulation efforts would only increase these cost differences. Accordingly, the commenter urged that HUD address this issue by extending the incentives provided under § 990.107 to tenant-supplied utilities.

*HUD Response.* As the first commenter wrote, HUD has been addressing this concern through the issuance of regulatory waivers. While the suggestion of the commenter that the policy be codified in the new interim rule is appreciated, HUD recognizes that this issue was not addressed by the Committee. HUD has decided to defer consideration of substantive changes to the proposed rule until completion of the operating cost study and development of the final rule. Accordingly, HUD has not adopted the requested change. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The requested change will be reevaluated at the final rule stage, and may be reflected in the substance of the final rule.

*J. Comment Regarding "Moving to Work" PHAs*

*Comment: The proposed rule provisions regarding Moving to Work (MTW) PHAs has the potential to undermine the effectiveness of the Operating Fund formula.* Proposed § 990.104(d) provides that the calculation of operating subsidy for a PHA in the MTW demonstration program shall be made in accordance with the applicable Moving to Work Agreement, and any amendments to such agreements, as may be approved by HUD. One commenter wrote that if HUD "begins hand-tailoring the operating subsidies received by individual PHAs \* \* \* the proposed rule \* \* \* will become meaningless, since any increases for individual PHAs will simply come out of the pot available for other PHAs, potentially distorting the process and making obsolete any rule for allocating the available funds on a systemic basis."

*HUD Response.* HUD does not agree with the commenter's premise that the MTW demonstration program has the potential to distort and make this interim rule obsolete. The demonstration is limited in scope and duration, and subsidy eligibility for these PHAs is roughly what would have been determined regardless of MTW participation. If Congressional appropriations are not sufficient to meet program requirements, MTW agencies are subject to the same subsidy proration as other PHAs.

*K. Comments Regarding Vacant Units*

*Comment: The interim rule should discourage the maintenance of vacant units.* One commenter wrote that the proposed definition of "unit months available" at § 990.102 allows the payment of operating subsidies for units vacant up to one year. The commenter wrote that the interim rule should discourage the maintenance of vacancies that are within the control of the PHA and should encourage PHAs to reduce the time that it takes to rent a unit. The commenter wrote that the time required to rent a unit vacant due to circumstances within a PHA's control should be less than one month. However, to accommodate unforeseen circumstances, the commenter suggested that the interim rule allow for operating subsidies to continue for a period not to exceed three months. The commenter wrote that reducing the time that vacant units are eligible for operating subsidies will encourage effective maintenance and management practices to minimize the number of units off-line, reduce turn overtime for



vacant units, and reduce the time to renovate units.

**HUD Response.** HUD has not adopted the requested change. HUD has decided to defer consideration of major changes to the proposed rule until completion of the operating cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggestion made by the commenter will be reevaluated at the final rule stage.

**Comment: Required documentation of occupancy status should be expanded.** One commenter wrote that § 990.117(c) requires PHAs to maintain documentation on the occupancy status of all units, including various categories of vacant units, such as long term vacancies, vacant units undergoing modernization and units vacant due to circumstances beyond the PHA's control. The commenter suggested that the information PHAs are required to document should be expanded. The commenter recommended that the interim rule should require PHAs to document the size of a unit by bedroom size, dates of vacancy, and the plan to return the unit to occupancy (including the source of any required funds and the planned date for re-occupancy). The commenter wrote that such information should be made available to the Resident Advisory Board and the public through the PHA Plan process.

**HUD Response.** HUD has not adopted the suggested change. HUD has decided to defer consideration of substantive changes to the proposed rule until completion of the public housing operating cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The change requested by the commenter will be reevaluated at the final rule stage.

#### *L. Comments Regarding Flat Rents/Ceiling Rents*

**Comment: The proposed rule fails to clarify that the difference between flat rents and costs will be subsidized by HUD.** One commenter wrote that PHAs are statutorily required to adopt flat rents. According to the commenter, these flat rents should be based upon the rental value of the units and designed not to discourage employed tenants from staying in public housing. The commenter wrote that to achieve these dual objectives, it is possible that flat rents will not cover the operating expenses for the unit. The commenter suggested that the proposed rule be revised to provide that if there is a

shortfall, PHAs will be held harmless and not be required to subsidize the difference between the flat rents and operating cost.

**HUD Response.** The rent charged for a unit and the allowable expense level (AEL), which generally represents the non-utility operating expenses for a unit, are two distinct and separate factors in determining operating subsidy eligibility. If a flat rent is established appropriately and is less than the AEL, the PHA will be eligible for operating subsidy in an amount that represents the difference between the flat rent and the AEL.

**Comment: Proposed rule fails to acknowledge that ceiling rents will be subsidized for the next three years.** One commenter wrote that QHWA provides that PHAs may use ceiling rents to attract and keep public housing residents who are employed. The commenter wrote that § 960.253(d) of HUD's Admission and Occupancy final rule (65 FR 16727, March 29, 2000) provides that a PHA may use the ceiling rent as the flat rent for the next three years. According to the commenter, the July 10, 2000 proposed rule is deficient because it does not specify how ceiling rents will be handled in the next three years. "Will the difference between ceiling rents and the cost of the unit be set off by operating subsidies?" The commenter wrote that operating subsidy should be provided to cover any shortfall resulting from implementation of the ceiling rents. "If operating subsidies do not cover the shortfall, PHAs will be subject to immense pressure to do away with ceiling rents immediately. This pressure will be even more substantial because PHAs may now retain 50% of all increases in rents."

**HUD Response.** HUD does not believe that the proposed rule was deficient in its treatment of ceiling rents. The definition of dwelling rent in § 990.102 makes reference to § 960.253, *Choice of Rents*. These choices include ceiling rents that were authorized and established before October 1, 1999. Those ceiling rents may be used for a period of three years from October 1, 1999.

#### *M. Comments Regarding Optional Income Exclusions*

**Comment: The definition of "dwelling rent" should reflect decreases resulting from PHA implementation of optional income exclusions.** Two commenters made this recommendation. The proposed definition of "dwelling rent" does not reflect decreases resulting from the PHA's implementation of any optional earned income exclusions.

According to the commenters, this will discourage PHAs from implementing such optional exclusions. The commenters suggested that the interim rule should provide that, for purposes of determining subsidy eligibility, the total dwelling rental income of the PHA will not be decreased more than 5% resulting from the PHA's implementation of any optional earned income exclusion. Further, the commenters suggested that HUD provide increased operating funds accordingly.

**HUD Response.** HUD has not adopted the recommended change. As noted above, HUD has decided to defer consideration of major changes to the proposed rule until completion of the cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The suggested change will be reevaluated at the final rule stage.

**Comment: The interim rule should minimize administrative burden in order to encourage PHAs to adopt optional income exclusions.** Proposed § 990.109(b)(2)(iii) provides that the Rent Roll used for calculating the projected operating income level will not reflect decreases resulting from the PHA's implementation of an optional earned income exclusion. One commenter wrote that HUD should make implementation of this requirement as simple as possible. "PHAs should be encouraged in every way to adopt optional [earned income exclusions]. That encouragement should not be diminished by cumbersome administrative requirements."

**HUD Response.** HUD believes that the new formula will encourage the adoption of optional earned income exclusions by giving PHAs a new source of funds that can be used for the provision of resident-related services and improvements. The new source of funds is the retention of 50% of increases in dwelling rental income.

#### *N. Comments Regarding Family Self-Sufficiency Program*

**Comment: The interim rule should treat the administrative costs of implementing a Family Self-Sufficiency (FSS) program as costs of operating public housing.** One commenter wrote that the FSS statute (at 42 U.S.C. 1437u(h)(2)) and HUD's implementing regulations (at 24 CFR part 984) require that the reasonable and eligible administrative costs incurred by PHAs in carrying out public housing FSS programs—both mandatory and voluntary—be included in the

calculation of Federal operating subsidies. Accordingly, the commenter suggested that proposed § 990.108 (which lists the "other costs" of operating public housing") should be revised to authorize PHAs that operate a FSS program to add the reasonable administrative costs of one or more FSS case managers, depending on program size.

**HUD Response.** The interim rule makes no change to the existing policy that permits continued subsidy support, under certain circumstances, for FSS programs involving public housing residents. That policy is currently contained in Notice PIH 2000-4 (HA), issued February 3, 2000. While the suggestion of the commenter that the policy be codified in the new interim rule is appreciated, HUD recognizes that this issue was not addressed by the Committee. As noted above, HUD has decided to defer consideration of substantive changes to the proposed rule until completion of the operating cost study and development of the final rule. Accordingly, HUD has not adopted the suggestion made by the commenter. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The commenter's suggestion will be reevaluated at the final rule stage.

**Comment:** *The interim rule should specify how PHAs will be reimbursed for allowable expenses and contributions to tenant escrow accounts under the FSS program.* One commenter wrote that under the current PFS regulations PHAs can, in effect, be reimbursed for their contributions to tenant FSS escrow accounts. According to the commenter, the PHA can accomplish this by including the rent charges based on the tenants' incomes at the start of FSS participation in the determination of the projected operating income level—without consideration of the amounts deposited in the FSS escrow accounts. According to the commenter, this method will not be adequate under the proposed Operating Fund rule. The commenter wrote that if only the reduced rent charges are considered in determining dwelling rental income, PHAs would not receive credit for the increased earnings of FSS families. Absent such credit, PHAs with FSS programs would be deprived of the right to retain 50% of the revenue due to the increased earnings of such families. Accordingly, the commenter suggested that the proposed rule be modified as follows:

1. HUD should revise the calculation of dwelling rental income at § 990.109 to include the "total tenant payment"

for families enrolled in FSS. According to the commenter, this amount should include any increase in rent attributable to increased earnings while in FSS. Such increased rent is the amount defined as the "FSS credit" under 24 CFR 984.305(b).

2. The interim rule should include PHA contributions of families' credits to FSS escrow accounts as an "other cost" under § 990.108.

**HUD Response.** HUD has not adopted the suggested changes. As noted, HUD has decided to defer consideration of major changes to the proposed rule until completion of the operating cost study and development of the final rule. Harvard University will receive and consider the public comments on the proposed rule during development of the cost study. The requested changes will be reevaluated at the final rule stage.

#### *O. Comments Regarding Rulemaking Procedures*

**Comment:** *HUD should also consider public comments on prior interim rule amending PFS to which HUD has not yet responded.* One commenter suggested that HUD take the opportunity afforded by the July 10, 2000 proposed rule to also consider the public comments received on HUD's September 30, 1996 (61 FR 51178) interim rule, which made several amendments to the PFS regulations. The commenter was particularly concerned by the interim rule amendments to § 990.114, regarding the phase-down of subsidy for units approved for demolition. The commenter suggested that "consideration be given not only to the comments received on the [September 30, 1996] interim rule but to more recent experience in the context not fully anticipated at the time of the interim rule of extensive demolition in anticipation not of agency downsizing but of HOPE VI or other mixed-finance redevelopment." The commenter wrote that HUD "is well aware of the difficulties caused by the implementation of the current rule in this context, and particularly of the disproportionate and harsh impact of removing units from phasedown subsidy because of the issuance of relocation and replacement certificates or vouchers."

**HUD Response.** The suggestion made by the commenter is outside the scope of this rulemaking, which is exclusively concerned with implementation of the new Operating Fund Formula.

**Comment:** *Reduced 30-day public comment period was insufficient.* One commenter wrote that PHAs that did not participate at the negotiated rulemaking

sessions deserved adequate time to fully evaluate the proposed rule. The commenter wrote that the proposed changes would greatly affect the operation of public housing and, therefore, merited the customary full 60-day public comment period.

**HUD Response.** HUD agrees that public comment is vital to the successful development of its regulations. It is the general practice of the Department to provide a 60-day public comment period on all proposed rules. However, given the extensive involvement of affected parties in the development of the July 10, 2000 proposed rule, HUD believes that good cause existed for the provision of a reduced 30-day comment period.

The membership of the Negotiated Rulemaking Committee was selected by HUD to represent a wide range of affected interests and parties. As required by the Negotiated Rulemaking Act, the public was afforded an opportunity to comment on the proposed Committee membership, and to submit nominations for membership. The final membership of the Committee included representatives of small, medium and large PHAs; public housing residents; the three main national organizations representing PHAs; advocates for low-income housing; and other housing experts. The proposed rule was the result of the Committee's successful negotiations, and represents the consensus decisions reached by over a year's worth of substantive deliberations.

In addition to the participation of the Committee members, the proposed rule reflected the input of many other affected parties not directly involved in the negotiated rulemaking process. Many of the Committee members (such as the national PHA organizations, the resident groups and others) served as representatives of larger constituencies. These organizations routinely consulted with their membership regarding the status of the negotiations and the substance of the proposed regulatory text. Moreover, all of the Committee meetings were announced through prior **Federal Register** notice and were open to the public. Members of the public were provided with the opportunity to make statements during the meetings, and to file written comments for the Committee's consideration.

For the above reasons, HUD believes that this interim rule has been developed with substantive public participation, and that the reduced 30-day period did not restrict the ability of the public to comment on the proposed rule. The Department also notes that public participation in the development

of the Operating Fund regulations is a continuing process. This rule provides the public with an additional 60-days to submit written comments on the interim regulatory requirements. All public comments will be considered in the development of the final rule. As noted, HUD will issue the final rule following the completion of a Congressionally mandated public housing cost study. HUD has directed the cost-study contractor to consult with interested individuals and organizations in the development of the study. HUD also intends to develop the final rule with the active participation of affected parties and using the procedures of the Negotiated Rulemaking Act.

*Comment: Any procedural changes required under § 990.108(c) or § 990.109(d) should be subject to notice and comment rulemaking procedures.* Section 990.108(c) provides that:

In the event that HUD determines that enactment of a Federal law or revision in HUD or other Federal regulation has caused or will cause a significant increase in expenditures of a continuing nature above the Allowable Expense Level and Utilities Expense Level, HUD may in HUD's sole discretion decide to prescribe a procedure under which the PHA may apply for or may receive an increase in operating subsidy.

In addition, § 990.109(d) provides that:

After implementation of the provisions of any legislation enacted or any HUD administrative action taken subsequent to the effective date of these regulations, which affects rents paid by residents of Projects, HUD may adjust the projected average monthly dwelling rental charge per unit to reflect such change. HUD also shall have complete discretion to reduce or increase the operating subsidy approved for the PHA current fiscal year in an amount equivalent to the change in the rental income.

One commenter wrote that any such changes "should be made through reasonable procedures spelled out in regulation and with input from experts, from PHAs and from public housing residents." The commenter wrote that this process should not be left to HUD's sole discretion. "It must go through normal rulemaking procedures."

*HUD Response.* The regulatory language cited by the commenter was agreed upon through the consensus decisionmaking of the Committee. As noted, HUD has decided to defer consideration of major changes to the proposed rule until the completion of the cost study and development of the final rule. Accordingly, HUD has not adopted the suggestion made by the commenter. The requested change will be reevaluated at the final rule stage.

#### *P. Miscellaneous Comments*

*Comment: When was the implicit deflator for the purchase of goods and services removed from the computation of the local inflation factor in § 990.105(c)(2)?* One commenter posed this question.

*HUD Response.* Section 990.105(c)(2) defines the Local Government Wage Rate Index and was added to the PFS regulation as one of five factors in the Revised AEL Formula published in the **Federal Register** on February 4, 1992. The definition of Local Government Wage Rate Index has not changed.

*Comment: Is the differential added onto the top of the range in § 990.105(d)(2)(ii)?* One commenter posed this question.

*HUD Response.* The regulation clearly states in § 990.105(d)(2) that the amounts calculated under (d)(2)(i) and (d)(2)(ii) are added to the top of the range.

*Comment: Paragraphs (c)(2) and (d) of § 990.107 should be removed.* One commenter made this suggestion. These paragraphs concern the determination of the utilities consumption and expense levels where the necessary data is not available. The commenter asked whether these provisions were needed. "It would seem impossible that any PHA would have failed to accumulate the required utility data after twenty years of having been required to do so."

*HUD Response.* There are some new PHAs which come in for subsidy each year. It is possible that they would not have the required data available.

#### **VI. Findings and Certifications**

##### *Information Collection Requirements*

The information collection requirements contained in 24 CFR part 990 have been approved by the Office of Management (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520). While this interim rule makes several modifications to the existing regulatory requirements, the rule does not increase the total reporting and recordkeeping burden related to the payment of operating subsidies to PHAs. The information collection requirements contained in §§ 990.104, 990.105, 990.107, 990.108, 990.110, 990.111, and 990.117 of this interim rule correspond to information collections contained in HUD's current part 990 regulations. These information collection requirements have been assigned OMB control numbers 2577–0029 (expiration date May 31, 2001), 2577–0026 (expiration date June 30, 2001), and 2577–0066 (expiration date September 30, 2002). 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.

##### *Environmental Impact*

A Finding of No Significant Impact with respect to the environment was 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. 4223). That Finding of No Significant Impact remains applicable to this interim rule and is available for public inspection between the hours of 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC.

##### *Regulatory Planning and Review*

The Office of Management and Budget (OMB) has reviewed this interim rule under Executive Order 12866, *Regulatory Planning and Review*. OMB determined that this interim rule is a "significant regulatory action" as defined in section 3(f) of the Order (although not economically significant, as provided in section 3(f)(1) of the Order). Any changes made to this rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection during regular business hours (7:30 a.m. to 5:30 p.m.) in the Office of the General Counsel, Rules Docket Clerk, Room 10276, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410.

##### *Regulatory Flexibility Act*

The Secretary has reviewed this interim rule before publication and by approving it certifies, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), that this interim rule will not have a significant economic impact on a substantial number of small entities. The interim rule implements a new system for formula allocation of funds to PHAs for their operating needs. The new system is established to provide minimum impact on all PHAs, small and large. Accordingly, the formula will not have a significant economic impact on any PHA. Notwithstanding HUD's determination that this interim rule will not have a significant economic impact on small entities, HUD specifically invites comments regarding alternatives to this interim rule that would meet HUD's objectives as described in this preamble.

### *Federalism Impact*

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial direct compliance costs on State and local governments and is not required by statute, or the rule preempts State law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This interim rule will not have federalism implications and will not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive Order.

### *Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) (UMRA) requires Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and on the private sector. This interim rule does not impose, within the meaning of the UMRA, any Federal mandates on any State, local, or tribal governments or on the private sector.

### *Catalog of Federal Domestic Assistance*

The Catalog of Federal Domestic Assistance Number for this program is 14.850.

### **List of Subjects in 24 CFR Part 990**

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

For the reasons discussed in the preamble, HUD amends 24 CFR part 990 as follows:

### **PART 990—THE PUBLIC HOUSING OPERATING FUND PROGRAM**

1. Revise the heading of part 990 to read as set forth above.
2. The authority citation for part 990 is revised to read as follows:

**Authority:** 42 U.S.C. 1437g and 3535(d).

3. Subpart A is revised to read as follows:

#### **Subpart A—The Operating Fund Formula**

Sec.

- 990.101 Purpose.
- 990.102 Definitions.
- 990.103 Applicability of the Operating Fund Formula.
- 990.104 Determination of amount of operating subsidy under the Operating Fund Formula.
- 990.105 Computation of allowable expense level.

- 990.106 Transition funding for excessively high-cost PHAs.
- 990.107 Computation of utilities expense level.
- 990.108 Other costs.
- 990.109 Projected operating income level.
- 990.110 Adjustments.
- 990.111 Submission and approval of operating subsidy calculations and budgets.
- 990.112 Payments procedure for operating subsidy under the Operating Fund Formula.
- 990.113 Payments of operating subsidy conditioned upon reexamination of income of families in occupancy.
- 990.114 Phase-down of subsidy for units approved for demolition.
- 990.116 Increases in dwelling rental income.
- 990.117 Determining actual and requested budget year occupancy percentages.
- 990.120 Audits.
- 990.121 Effect of rescission.

#### **§ 990.101 Purpose.**

This subpart implements section 9(f) of the United States Housing Act of 1937 (42 U.S.C. 1437g) (referred to as "the 1937 Act"). Section 9(f) establishes an Operating Fund for the purposes of making assistance available to public housing agencies (PHAs) for the operation and management of public housing. The assistance made available from the Operating Fund is determined using a formula developed through negotiated rulemaking procedures. This subpart describes the policies and procedures for operating subsidy calculations under the Operating Fund Formula.

#### **§ 990.102 Definitions.**

**Allowable Expense Level (AEL).** The per unit per month dollar amount of expenses (excluding Utilities and expenses allowed under § 990.108) computed in accordance with § 990.105, which is used to compute the amount of operating subsidy.

**Allowable Utilities Consumption Level (AUCL).** The amount of Utilities expected to be consumed per unit per month by the PHA during the Requested Budget Year, which is equal to the average amount consumed per unit per month during the Rolling Base Period.

**Base Year.** The PHA's fiscal year immediately preceding its first fiscal year of receipt of operating subsidy under this part (either under the Operating Fund Formula or its predecessor, the Performance Funding System (PFS)).

**Base Year Expense Level.** The expense level (excluding Utilities, audits and certain other items) for the Base Year, computed as provided in § 990.105.

**Current Budget Year.** The fiscal year in which the PHA is currently operating.

**Dwelling rent.** The amount charged monthly for a dwelling unit occupied by a resident or family eligible for public housing as determined in § 960.253 of this title. For purposes of determining subsidy eligibility, the dwelling rent will not reflect decreases resulting from the PHA's implementation of any optional earned income exclusions.

**Formula.** The revised formula derived from the actual expenses of the sample group of PHAs receiving assistance under the Operating Fund Formula, which is used to determine the Formula Expense Level and the Range of each PHA (see § 990.105(c)).

**FHA-based operating expense level (FHAEL).** The per unit per month dollar amount of expenses (excluding utilities and expenses allowed under § 990.108) computed in accordance with § 990.105(e), which is used on a one-time basis to adjust the AEL for selected PHAs.

**Formula Expense Level.** The per unit per month dollar amount of expenses (excluding Utilities and audits) computed under the Formula, in accordance with § 990.105.

**HUD Field Office.** The HUD Field Office that has been delegated authority under the U.S. Housing Act of 1937 to perform functions pertaining to this subpart for the area in which the PHA is located.

**Local Inflation Factor.** The HUD-supplied weighted average percentage increase in local government wages and salaries for the area in which the PHA is located and non-wage expenses.

**Long-term vacancy.** This term means the same as it is used in the definition of "Unit Months Available" in this section.

**Nondwelling rent.** The amount charged monthly, including utility and equipment charges, to a lessee for a dwelling unit that is being used for nondwelling purposes. For purposes of determining operating subsidy:

- (1) If the nondwelling unit has been approved for subsidy (e.g., the unit is being used for economic self-sufficiency services or anti-drug activities) at the rate of the PHA's AEL, the PHA will include all charges as nondwelling rent;
- (2) If the nondwelling unit has not been approved for subsidy, a PHA will include as nondwelling rent only that portion of the charge that exceeds the rate of the PHA's AEL.

**Operating budget.** The PHA's operating budget and all related documents, as required by HUD, approved by the PHA Board of Commissioners.

*Other income.* Income from rent billed to lessees of dwelling units rented for nondwelling purposes, and from charges to residents for excess utility consumption for PHA supplied utilities.

*Project.* Each project under an Annual Contributions Contract to which the Operating Fund Formula is applicable, as provided in § 990.103.

*Project Units.* All dwelling units of a PHA's Projects.

*Projected Operating Income Level.* The per unit per month dollar amount of dwelling rental income plus other income, computed as provided in § 990.109.

*Requested Budget Year.* The budget year (fiscal year) of a PHA following the Current Budget Year.

*Rolling Base Period.* The 36-month period that ends 12 months before the beginning of the PHA Requested Budget Year, which is used to determine the Allowable Utilities Consumption Level used to compute the Utilities Expense Level.

*Top of Range.* Formula Expense Level multiplied by 1.15.

*Transition funding.* Funding for excessively high-cost PHAs, as provided in § 990.106.

*Unit Approved for Deprogramming.*

(1) A dwelling unit for which HUD has approved the PHA's formal request to remove the dwelling unit from the PHA's inventory and the Annual Contributions Contract but for which removal, i.e., deprogramming, has not yet been completed; or

(2) A nondwelling structure or a dwelling unit used for nondwelling purposes which the PHA has determined will no longer be used for PHA purposes and which HUD has approved for removal from the PHA's inventory and Annual Contributions Contract.

*Unit months available.* Project Units multiplied by the number of months the Project Units are available for occupancy during a given PHA fiscal year. For purposes of this part, a unit is considered available for occupancy from the date established as the End of the Initial Operating Period for the Project until the time the unit is approved by HUD for deprogramming and is vacated or is approved for nondwelling use. In the case of a PHA development involving the acquisition of scattered site housing, see also § 990.104(b). A unit will be considered a long-term vacancy and will not be considered available for occupancy in any given PHA Requested Budget Year if the PHA determines that:

(1) The unit has been vacant for more than 12 months at the time the PHA

determines its Actual Occupancy Percentage;

(2) The unit is not either:

(i) A vacant unit undergoing modernization; or

(ii) A unit vacant for circumstances and actions beyond the PHA's control, as these terms are defined in this section; and

(3) The PHA determines that it will have a vacancy percentage of more than 3% and will have more than five vacant units, for its Requested Budget Year, even after adjusting for vacant units undergoing modernization and units that are vacant for circumstances and actions beyond the PHA's control, as defined in this section. (Reference in this part to "more than five units" or "fewer than five units" shall refer to a circumstance in which five units equals or exceeds 3% of the number of units to which the 3% threshold is applicable.)

*Units vacant due to circumstances and actions beyond the PHA's control.* Dwelling units that are vacant due to circumstances and actions that prohibit the PHA from occupying, selling, demolishing, rehabilitating, reconstructing, consolidating or modernizing vacant units and are beyond the PHA's control. For purposes of this definition, circumstances and actions beyond the PHA's control are limited to:

(1) *Litigation.* The effect of court litigation such as a court order or settlement agreement that is legally enforceable. An example would be units that are being held vacant as part of a court-ordered or HUD-approved desegregation plan.

(2) *Laws.* Federal or State laws of general applicability, or their implementing regulations. Units vacant only because they do not meet minimum standards pertaining to construction or habitability under Federal, State, or local laws or regulations will not be considered vacant due to circumstances and actions beyond the PHA's control.

(3) *Changing market conditions.* For example, small PHAs that are located in areas experiencing population loss or economic dislocations may face a lack of demand in the foreseeable future, even after the PHA has taken aggressive marketing and outreach measures.

(4) *Natural disasters.*

(5) *RMC Funding.* The failure of a PHA to fund an otherwise approvable RMC request for Federal modernization funding.

(6) *Casualty Losses.* Delays in repairing damage to vacant units due to the time needed for settlement of insurance claims.

*Utilities.* Electricity, gas, heating fuel, water and sewerage service.

*Utilities expense level.* The per unit per month dollar amount of utilities expense, computed as provided in § 990.107.

*Vacant unit undergoing modernization.* A vacant unit in a project not considered to be obsolete (as determined using the indicia in § 970.6 of this chapter), when the project is undergoing modernization that includes work that is necessary to reoccupy the vacant unit, and in which one of the following conditions is met:

(1) The unit is under construction (i.e., the construction contract has been awarded or force account work has started); or

(2) The treatment of the vacant unit is included in a HUD-approved modernization budget (or its successor under the public housing Capital Fund program), but the time period for placing the vacant unit under construction has not yet expired. The PHA must place the vacant unit under construction within two Federal Fiscal Years (FFYs) after the FFY in which the modernization funds are approved.

#### **§ 990.103 Applicability of the Operating Fund Formula.**

(a) *General.* The Operating Fund Formula will be used in determining the amounts of operating subsidy payable to PHAs.

(b) *Applicability of the Operating Fund Formula.* The Operating Fund Formula is applicable to all PHA rental units under Annual Contributions Contracts. The Operating Fund Formula applies to PHAs that have not received operating subsidy payments previously, but are eligible for such payments under the Operating Fund Formula.

(c) *Inapplicability of the Operating Fund Formula.* The Operating Fund Formula, as described in this part, is not applicable to Indian Housing, the Section 23 Leased Housing Program, the Section 23 Housing Assistance Payments Program, the Section 8 Housing Assistance Payments Program, the Mutual Help Program, or the Turnkey III Homeownership Opportunity Programs.

(d) *Applicability of the Operating Fund Formula to the PHAs of the Virgin Islands, Puerto Rico, Guam, and Alaska.*

(1) The following provisions of this subpart A are applicable to housing owned by the PHAs of the Virgin Islands, Puerto Rico, Guam, and Alaska:

(i) The definition of "other income" at § 990.102;

(ii) Section 990.105 (Computation of allowable expense level). However, § 990.105(e) (Computation of FHA-based

operating expense level for application in FY 2001) does not apply to these PHAs;

(iii) Section 990.105(f) (Flood insurance adjustment for FY 2001);

(iv) Section 990.108(e) (Funding for resident participation activities);

(v) Section 990.109(b) (Computation of projected average monthly dwelling rental income);

(vi) Section 990.110(b) (Adjustments to utilities expense level); and

(vii) Section 990.116 (Increases in dwelling rental income).

(2) With the exception of the provisions listed in paragraph (d)(1) of this section, and other provisions of this part necessary to give full effect to the provisions listed in paragraph (d)(1) of this section, the Operating Fund Formula is not applicable to the PHAs of the Virgin Islands, Puerto Rico, Guam and Alaska. Operating subsidy payments to these PHAs are made in accordance with subpart B of this part.

(e) *Financial management, monitoring and reporting.* The financial management system, monitoring and reporting on program performance and financial reporting will be in compliance with 24 CFR 85.20, 85.40 and 85.41 except to the extent that HUD requirements provide for additional specialized procedures which are determined by HUD to be necessary for the proper management of the program in accordance with the requirements of the U.S. Housing Act of 1937 and the Annual Contributions Contracts between the PHAs and HUD.

#### **§ 990.104 Determination of amount of operating subsidy under the Operating Fund Formula.**

(a) The amount of operating subsidy for which each PHA is eligible shall be determined as follows: The Projected Operating Income Level is subtracted from the total expense level (Allowable Expense Level plus Utilities Expense Level). These amounts are per unit per month dollar amounts, and must be multiplied by the Unit Months Available. Transition Funding, if applicable, and other costs as specified in § 990.108 are then added to this total in order to determine the total amount of operating subsidy for the Requested Budget Year, exclusive of consideration of the cost of an independent audit. As an independent operating subsidy eligibility factor, a PHA may receive operating subsidy in an amount, approved by HUD, equal to the actual cost of an independent audit to be prorated to operations of the PHA-owned rental housing. See § 990.110 regarding adjustments.

(b) In the case of a PHA development involving the acquisition of scattered site housing, the PHA may submit, and HUD shall review and approve, a revised Development Cost Budget (or its successor under the public housing Capital Fund program) reflecting the number of units that were occupied during the previous six months, and the Unit Months Available used in the calculation of operating subsidy eligibility shall be revised to include the number of months the new/acquired units are actually occupied.

(c) A special phase-down of subsidy to PHAs is applicable when demolition of units is approved by HUD. See § 990.114.

(d) The calculation of operating subsidy for a PHA in the Moving to Work demonstration program shall be made in accordance with the applicable Moving to Work Agreement, and any amendments to such agreements, as may be approved by HUD.

#### **§ 990.105 Computation of allowable expense level.**

The PHA shall compute its Allowable Expense Level using forms prescribed by HUD, as follows:

(a) *Computation of Base Year Expense Level.* The Base Year Expense Level includes Payments in Lieu of Taxes (PILOT) required by a Cooperation Agreement even if PILOT is not included in the Operating Budget for the Base Year because of a waiver of the requirements by the local taxing jurisdiction(s). The Base Year Expense Level includes all other operating expenditures as reflected in the PHA's Operating Budget for the Base Year except the following:

(1) Utilities expense;

(2) Cost of an independent audit;

(3) Adjustments applicable to budget years before the Base Year;

(4) Expenditures supported by supplemental subsidy payments applicable to budget years before the Base Year;

(5) All other expenditures which are not normal fiscal year expenditures as to amount or as to the purpose for which expended; and

(6) Expenditures which were funded from a nonrecurring source of income.

(b) *Adjustment.* In compliance with the above six exclusions, the PHA shall adjust the AEL by excluding any of these items from the Base Year Expense Level if this has not already been accomplished. If such adjustment is made in the second or some subsequent fiscal year of receipt of operating subsidy under this part, the AEL shall be adjusted in the year in which the adjustment is made, but the adjustment

shall not be applied retroactively. If the PHA does not make these adjustments, the HUD Field Office shall compute the adjustments.

(c) *Computation of Formula Expense Level.* The PHA shall compute its Formula Expense Level in accordance with a HUD-prescribed formula that estimates the cost of operating an average unit in a particular PHA's inventory. It uses weights and a Local Inflation Factor assigned each year to derive a Formula Expense Level for the current year and the requested budget year. The formula is the sum of the following six numbers and the weights of the formula and the formula are subject to updating by HUD:

(1) The number of pre-1940 rental units occupied by poor households in 1980 as a percentage of the 1980 population of the community multiplied by a weight of 7.954. This census-based statistic applies to the county of the PHA, except that, if the PHA has 80% or more of its units in an incorporated city of more than 10,000 persons, it uses city-specific data. County data will exclude data for any incorporated cities of more than 10,000 persons within its boundaries.

(2) The Local Government Wage Rate multiplied by a weight of 116.496. The wage rate used is a figure determined by the Bureau of Labor Statistics. It is a county-based statistic, calibrated to a unit-weighted PHA standard of 1.0. For multi-county PHAs, the local government wage is unit-weighted. For this formula, the local government wage index for a specific county cannot be less than 85% or more than 115% of the average local government wage for counties of comparable population and metro/non-metro status, on a state-by-state basis. In addition, for counties of more than 150,000 population in 1980, the local government wage cannot be less than 85% or more than 115% of the wage index of private employment determined by the Bureau of Labor Statistics and the rehabilitation cost index of labor and materials determined by the R.S. Means Construction Cost Index.

(3) The lesser of the current number of the PHA's two or more bedroom units available for occupancy, or 15,000 units, multiplied by a weight of .002896.

(4) The current ratio of the number of the PHA's two or more bedroom units available for occupancy in high-rise family projects to the number of all the PHA's units available for occupancy multiplied by a weight of 37.294. For this indicator, a high-rise family project is defined as averaging 1.5 or more bedrooms per unit available for occupancy and averaging 35 or more

units available for occupancy per building and containing at least one building with units available for occupancy that is 5 or more stories high.

(5) The current ratio of the number of the PHA's three or more bedroom units available for occupancy to the number of all the PHA's units available for occupancy multiplied by a weight of 22.303.

(6) An equation calibration constant of  $-.2344$ .

(d) *Computation of Allowable Expense Level (AEL)*. The PHA shall compute its Allowable Expense Level as follows:

(1) *AEL for first budget year of operating subsidy under this part where Base Year Expense Level does not exceed the top of the range*. Every PHA whose Base Year Expense Level is less than the top of the range shall compute its AEL for the first budget year of operating subsidy under this part by adding the following to its Base Year Expense Level (before adjustments under § 990.110):

(i) Any increase approved by HUD in accordance with § 990.110;

(ii) The increase (decrease) between the Formula Expense Level for the Base Year and the Formula Expense Level for the first budget year of operating subsidy under this part; and

(iii) The sum of the Base Year Expense Level, and any amounts described in paragraphs (d)(1)(i) and (ii) of this section multiplied by the Local Inflation Factor.

(2) *AEL for first budget year of operating subsidy under this part where Base Year Expense Level exceeds the top of the range*. Every PHA whose Base Year Expense Level exceeds the top of the range shall compute its AEL for the first budget year of operating subsidy under this part by adding the following to the top of the range (not to its Base Year Expense Level, as in paragraph (d)(1) of this section):

(i) The increase (decrease) between the Formula Expense Level for the Base Year and the Formula Expense Level for the first budget year of operating subsidy under this part;

(ii) The sum of the figure equal to the top of the range and the increase (decrease) described in paragraph (d)(2)(i) of this section, multiplied by the Local Inflation Factor. (If the Base Year Expense Level is above the AEL, computed as provided above, the PHA may be eligible for Transition Funding under § 990.106.)

(3) *AEL for first budget year of operating subsidy under this part for a new project*. A new project of a new PHA or a new project of an existing PHA that the PHA decides to place

under a separate ACC, which did not have a sufficient number of units available for occupancy in the Base Year to have a level of operations representative of a full fiscal year of operation is considered to be a "new project." The AEL for the first budget year of operating subsidy under this part for a "new project" will be based on the AEL for a comparable project, as determined by the HUD Field Office. The PHA may suggest a project or projects it believes to be comparable. In determining what constitutes a "new project" under this paragraph, HUD will be guided by its public housing development regulations at 24 CFR part 941.

(4) *Adjustment of AEL for budget years after the first budget year of operating subsidy under this part*. HUD may adjust the AEL of budget years after the first year of operating subsidy under this part, in accordance with the provisions of § 990.105(b) or § 990.108(c).

(5) *Allowable Expense Level for budget years after the first budget year of operating subsidy under this part*. For each budget year after the first budget year of operating subsidy under this part, the AEL shall be computed as follows:

(i) The AEL shall be increased by any increase to the AEL approved by HUD under § 990.108(c).

(ii) The AEL for the Current Budget Year also shall be adjusted as follows:

(A) Increased by one-half of one percent (.5%); and

(B) If the PHA has experienced a change in the number of units in excess of 5% or 1,000 units, whichever is less, since the last adjustment to the AEL based on this paragraph, it shall use the increase (decrease) between the Formula Expense Level calculated using the PHA's characteristics that applied to the Requested Year when the last adjustment to the AEL was made based on this paragraph and the Formula Expense Level calculated using the PHA's characteristics for the Requested Budget Year.

(iii) The amount computed in accordance with paragraphs (d)(5)(i) and (ii) of this section shall be multiplied by the Local Inflation Factor.

(6) *Adjustment of AEL for budget years after the first budget year of operating subsidy under this part*. HUD may adjust the AEL of budget years after the first year of operating subsidy under this part, in accordance with the provisions of § 990.105(b) or § 990.108(c).

(e) *Computation of FHA-based operating expense level (FHAEL) for application in FY 2001.—(1) HUD*

*calculation of FHAEL*. For every PHA that is eligible to receive operating subsidy under the Operating Fund Formula, HUD will calculate an FHAEL (based upon FY 2000 data and for application in FY 2001) as follows:

(i) *Step 1: Calculation of average national operating cost*. HUD will calculate an FHA-based national average cost of operating a two-bedroom public housing unit, exclusive of utility costs and property taxes. The average national cost will be calculated using privately managed (FHA multifamily insured and/or assisted) rental housing financial data available to HUD for the most recent year of full reporting and adjusted to reflect a two-bedroom size by using Section 8 Fair Market Rent (FMR) relationships (i.e., increase or decrease the national average cost depending on whether the average cost-weighted bedroom size is greater or less than 2.0 bedrooms per unit). (See 24 CFR part 888 for additional information regarding FMRs.)

(ii) *Step 2: Adjustment of average national two-bedroom operating cost for local cost differences*. HUD will adjust the average national two-bedroom operating cost for local cost differences using the location adjustment factors provided in the R.S. Means Residential Construction Costs Index.

(iii) *Step 3: Adjustment of average national operating cost for PHA-specific bedroom-size distribution*. For each PHA, HUD will further adjust the average national operating cost for the bedroom size distribution of the PHA using Section 8 FMR cost relationships (i.e., increase or decrease the average national cost depending on whether the average cost-weighted bedroom size for the PHA's inventory is greater or less than 2.0 bedrooms per unit).

(iv) *Step 4: Update of PHA-specific average operating cost to reflect FY 2000 costs*. HUD will update this PHA-specific operating cost to reflect increased FY 2000 operating costs by using the Public Housing AEL inflation factor.

(2) *Availability of FHAEL to PHA*.

HUD will make the following information available to each PHA:

(i) *FHAEL*. The FHAEL for the PHA;

(ii) *PHA bedroom distribution*. The PHA bedroom distribution used to make the PHA-specific bedroom adjustment under paragraph (e)(1)(iii) of this section; and

(iii) *Base average national cost*. The two-bedroom base average national cost calculated under paragraph (e)(1)(i) of this section.

(3) *Use of FHAEL for FY 2000 for PHAs with less than 500 units under contract*. Each PHA with less than 500



units shall review the FHAEL and bedroom distribution provided by HUD, and do the following:

(i) *The PHA will determine if the bedroom size distribution used by HUD was appropriate.*—(A) *Mandatory recalculation.* If the bedroom size distribution calculated by the PHA produces a weighted average bedroom size that differs by *more than .02* from the weighted average used by HUD, the PHA *shall* recalculate its FY 2000 FHAEL using the two-bedroom base average national operating cost provided by HUD.

(B) *Discretionary recalculation.* If the bedroom size distribution calculated by the PHA produces a weighted average bedroom size that differs by *less than .02* from the weighted average used by HUD, the PHA *may* recalculate its FY 2000 FHAEL using the two-bedroom base average national operating cost provided by HUD.

(ii) *Comparison of FHAEL to AEL.* The PHA shall compare its FHAEL with its approved FY 2000 AEL.

(iii) *If the PHA has less than 250 units.* PHAs with less than 250 units shall use the higher of their current AEL or 85% of the FHAEL. However, in no case will the PHA use an amount that exceeds 120% of its FHAEL for purposes of FY 2001 subsidy determinations under the Operating Fund Formula (see paragraph (e)(3)(v) of this section).

(iv) *If the PHA has 250–499 units.* PHAs with 250–499 units shall use the higher of their current AEL, or 70% of FHAEL. However, in no case will the PHA use an amount that exceeds 120% of its FHAEL for purposes of FY 2001 subsidy determinations under the Operating Fund Formula (see paragraph (e)(3)(v) of this section).

(v) *If the PHA with less than 500 units has an AEL greater than 120% of its FHAEL.* If a PHA with less than 500 units has an FY 2000 AEL that is greater than 120% of its FHAEL, the PHA shall use 120% of its FHAEL in place of its actual FY 2000 AEL for purposes of FY 2001 subsidy determinations under the Operating Fund Formula.

(4) *Use of FHAEL for FY 2000 for PHAs with more than 500 units under contract.* Each PHA with more than 500 units shall review the FHAEL and bedroom distribution provided by HUD and do the following:

(i) *The PHA shall determine if the bedroom size distribution used by HUD was appropriate.*—(A) *Mandatory recalculation.* If the bedroom size distribution calculated by the PHA produces a weighted average bedroom size that differs by *more than .02* from the weighted average used by HUD, the

PHA *shall* recalculate its FY 2000 FHAEL using the two-bedroom base average national operating cost provided by HUD.

(B) *Discretionary recalculation.* If the bedroom size distribution calculated by the PHA produces a weighted average bedroom size that differs by less than .02 from the weighted average used by HUD, the PHA *may* recalculate its FY 2000 FHAEL using the two-bedroom base average national operating cost provided by HUD.

(ii) *Comparison of FHAEL to AEL.* The PHA shall compare its FHAEL with its approved FY 2000 AEL.

(iii) *If the PHA's FY 2000 AEL is less than or equal to 85% of its FHAEL.* If the PHA's FY 2000 AEL is less than or equal to 85% of its FHAEL, the PHA shall use its FY 2000 AEL for purposes of FY 2001 subsidy determinations under the Operating Fund Formula.

(iv) *If the PHA's FY 2000 AEL is greater than 85% of its FHAEL.* If the PHA's FY 2000 AEL is greater than 85% of its FHAEL, the PHA shall use 98.64% of its FY 2000 AEL for purposes of calculating its FY 2001 subsidy determinations under the Operating Fund Formula.

(v) *Inapplicability of AEL reduction to certain PHAs.* The AEL reduction described in paragraph (e)(4)(iv) of this section does not apply to the PHAs of the Virgin Islands, Puerto Rico, Guam and Alaska. These PHAs will use their FY 2000 AELs for purposes of FY 2001 subsidy determinations, regardless of whether the PHA's AEL is greater than 85% of its FHAEL.

(vi) *Cap on AEL value reduction.* In no instance shall a PHA subject to an AEL reduction, reduce the FY 2000 AEL value used in calculating its FY 2001 AEL for purposes of operating subsidy determinations to a value less than 85% of its FHAEL.

(f) *Flood insurance adjustment for FY 2001.* To simplify the calculation of operating subsidy, the AEL computation for the PHA's fiscal year beginning in 2001 will include an additional step following the determination made in accordance with paragraphs (a) through (e) of this section: the AEL per unit month derived in accordance with those paragraphs is to be adjusted by adding the flood insurance charge per unit month, as reflected in the last HUD approved subsidy calculation for FY 2000. This adjustment is a one-time permanent adjustment made only in FY 2001. However, if the flood map is revised at a future date, HUD will adjust the AEL for the affected PHAs in accordance with this paragraph.

#### **§ 990.106 Transition funding for excessively high-cost PHAs.**

(a) *Eligibility.* If a PHA's Base Year Expense Level exceeds its AEL for any budget year under the Operating Fund Formula, the PHA may be eligible for Transition Funding.

(b) *Amounts.* Transition Funding shall be an amount not to exceed the difference between the Base Year Expense Level and the AEL for the Requested Budget Year, multiplied by the number of Unit Months Available.

(c) *Reduction in transition funding.* HUD shall have the right to discontinue payment of all or part of the Transition Funding in the event HUD at any time determines that the PHA has not achieved a satisfactory level of management efficiency, or is not making efforts satisfactory to HUD to improve its management performance.

#### **§ 990.107 Computation of utilities expense level.**

(a) *Computation of the utilities expense level.* The PHA's Utilities Expense Level for the requested Budget Year shall be computed by multiplying the Allowable Utilities Consumption Level (AUCL) per unit per month for each utility, determined as provided in paragraph (c) of this section, by the projected utility rate determined as provided in paragraph (b) of this section.

(b) *Utilities rates.* (1) The current applicable rates, with consideration of adjustments and pass-throughs, in effect at the time the Operating Budget is submitted to HUD will be used as the utilities rates for the Requested Budget Year, except that, when the appropriate utility commission has, prior to the date of submission of the Operating Budget to HUD, approved and published rate changes to be applicable during the Requested Budget Year, the future approved rates may be used as the utilities rates for the entire Requested Budget Year.

(2) If a PHA takes action, such as wellhead purchase of natural gas, or administrative appeals or legal action beyond normal public participation in rate-making proceedings to reduce the rate it pays for utilities (including water, fuel oil, electricity, and gas), then the PHA will be permitted to retain one-half of the cost savings during the first 12 months attributable to its actions. Upon determination that the action was cost-effective in the first year, the PHA may be permitted to retain one-half the annual cost savings, if the actions continue to be cost-effective. See also paragraph (e) of this section and § 990.110(b).

(c) *Computation of Allowable Utilities Consumption Level.* The Allowable Utilities Consumption Level used to compute the Utilities Expense Level of PHAs for the Requested Budget Year generally will be based on the availability of consumption data. For project utilities where consumption data are available for the entire Rolling Base Period, the computation will be in accordance with paragraph (c)(1) of this section. Where data are not available for the entire period, the computation will be in accordance with paragraph (c)(2) of this section, unless the project is a

new project, in which case the computation will be in accordance with paragraph (c)(3) of this section. For a project where the PHA has taken special energy conservation measures that qualify for special treatment in accordance with paragraph (f)(1) of this section, the computation of the Allowable Utilities Consumption Level may be made in accordance with paragraph (c)(4) of this section. The AUCL for all of a PHA's projects is the sum of the amounts determined using all of these subparagraphs, as appropriate.

(1) *Rolling Base Period System.* (i) For project utilities with consumption data for the entire Rolling Base Period, the AUCL is the average amount consumed per unit per month during the Rolling Base Period adjusted in accordance with paragraph (d) of this section. The PHA shall determine the average amount of each of the utilities consumed during the Rolling Base period (i.e., the 36-month period ending 12 months prior to the first day of the Requested Budget Year).

(ii) An example of a rolling base is as follows:

PHA fiscal year (affected fiscal year)		Rolling base period	
Beginning	Ending	Begins	Ends
1-1-01 .....	12-31-01 (1st year) .....	1-1-97	12-31-99
1-1-02 .....	12-31-02 (2nd year) .....	1-1-98	12-31-00

(2) *Alternative method where data is not available for the entire Rolling Base Period.* (i) If the PHA has not maintained or cannot recapture consumption data regarding a particular utility from its records for the whole Rolling Base Period mentioned in paragraph (c)(1) of this section, it shall submit consumption data for that utility for the last 24 months of its Rolling Base Period to the HUD Field Office for approval. If this is not possible, it shall submit consumption data for the last 12 months of its Rolling Base Period. The PHA also shall submit a written explanation of the reasons that data for the whole Rolling Base Period is unavailable.

(ii) In those cases where a PHA has not maintained or cannot recapture consumption data for a utility for the entire Rolling Base Period, comparable consumption for the greatest of either 36, 24, or 12 months, as needed, shall be used for the utility for which the data is lacking. The comparable consumption shall be estimated based upon the consumption experienced during the Rolling Base Period of comparable project(s) with comparable utility delivery systems and occupancy. The use of actual and comparable consumption by each PHA, other than those PHAs defined as New Projects in paragraph (c)(3) of this section, will be determined by the availability of complete data for the entire 36-month Rolling Base Period. Appropriate utility consumption records, satisfactory to HUD, shall be developed and maintained by all PHAs so that a 36-month rolling average utility consumption per unit per month under paragraph (c)(1) of this section can be determined.

(iii) If a PHA cannot develop the consumption data for the Rolling Base Period or for 12 or 24 months of the Rolling Base Period, either from its own project(s) data, or by using comparable consumption data the actual per unit per month (PUM) utility expenses stated in paragraph (d) of this section shall be used as the Utilities Expense Level.

(3) *Computation of Allowable Utilities Consumption Levels for New Projects.* (i) A New Project, for the purpose of establishing the Rolling Base Period and the Utilities Expense Level, is defined as either:

(A) A project which had not been in operation during at least 12 months of the Rolling Base Period, or a project which enters management after the Rolling Base Period and prior to the end of the Requested Budget Year; or

(B) A project which during or after the Rolling Base Period, has experienced conversion from one energy source to another; interruptible service; deprogrammed units; a switch from resident-purchased to PHA-supplied utilities; or a switch from PHA-supplied to resident-purchased utilities.

(ii) The actual consumption for New Projects shall be determined so as not to distort the Rolling Base Period in accordance with a method prescribed by HUD.

(4) *Freezing the Allowable Utilities Consumption Level.* (i) Notwithstanding the provisions of paragraphs (c)(1) and (c)(2) of this section, if a PHA undertakes energy conservation measures that are approved by HUD under paragraph (f) of this section, the Allowable Utilities Consumption Level for the project and the utilities involved may be frozen during the contract period. Before the AUCL is frozen, it

must be adjusted to reflect any energy savings resulting from the use of any HUD funding. The AUCL is then frozen at the level calculated for the year during which the conservation measures initially will be implemented, as determined in accordance with paragraph (f) of this section.

(ii) If the AUCL is frozen during the contract period, the annual three-year rolling base procedures for computing the AUCL shall be reactivated after the PHA satisfies the conditions of the contract. The three years of consumption data to be used in calculating the AUCL after the end of the contract period will be as follows:

(A) *First year:* The energy consumption during the year before the year in which the contract ended and the energy consumption for each of the two years before installation of the energy conservation improvements;

(B) *Second year:* The energy consumption during the year the contract ended, energy consumption during the year before the contract ended, and energy consumption during the year before installation of the energy conservation improvements;

(C) *Third year:* The energy consumption during the year after the contract ended, energy consumption during the year the contract ended, and energy consumption during the year before the contract ended.

(d) *Utilities expense level where consumption data for the full Rolling Base Period is unavailable.* If a PHA does not obtain the consumption data for the entire Rolling Base Period, or for 12 or 24 months of the Rolling Base Period, either for its own project(s) or by using comparable consumption data as required in paragraph (c)(2) of this

section, it shall request HUD Field Office approval to use actual PUM utility expenses. These expenses shall exclude Utilities Labor and Other Utilities Expenses. The actual PUM utility expenses shall be taken from the year-end Statement of Operating Receipts and Expenditures, Form HUD-52599, (Office of Management and Budget approval number 2577-0067) prepared for the PHA fiscal year which ended 12 months prior to the beginning of the PHA Requested Budget Year (e.g., for a PHA fiscal year beginning January 1, 2001, the PHA would use data from the fiscal year ended December 31, 1999). Subsequent adjustments will not be approved for a budget year for which the utility expense level is established based upon actual PUM utility expenses.

(e) *Adjustments.* PHAs shall request adjustments of Utilities Expense Levels in accordance with § 990.110(b), which requires an adjustment based upon a comparison between actual experience and estimates of consumption and of utility rates.

(f) *Incentives for energy conservation improvements.* If a PHA undertakes energy conservation measures (including those covering water, fuel oil, electricity, and gas) that are financed by an entity other than the Secretary, such as physical improvements financed by a loan from a utility or governmental entity, management of costs under a performance contract, or a shared savings agreement with a private energy service company, the PHA may qualify for one of the two possible incentives under this part. For a PHA to qualify for these incentives, HUD approval must be obtained. Approval will be based upon a determination that payments under the contract can be funded from the reasonably anticipated energy cost savings, and the contract period does not exceed 12 years.

(1) If the contract allows the PHA's payments to be dependent on the cost savings it realizes, the PHA must use at least 50% of the cost savings to pay the contractor. With this type of contract, the PHA may take advantage of a frozen AUCL under paragraph (c)(4) of this section, and it may use the full amount of the cost savings, as described in § 990.110(b)(2)(ii).

(2) If the contract does not allow the PHA's payments to be dependent on the cost savings it realizes, then the AUCL will continue to be calculated in accordance with paragraphs (c)(1) through (c)(3) of this section, as appropriate; the PHA will be able to retain part of the cost savings, in accordance with § 990.110(b)(2)(i); and the PHA will qualify for additional

operating subsidy eligibility (above the amount based on the allowable expense level) to cover the cost of amortizing the cost of the energy conservation measures during the term of the contract, in accordance with § 990.110(c).

#### § 990.108 Other costs.

(a) *Cost of independent audits.* (1) Eligibility to receive operating subsidy for independent audits is considered separately from the Operating Fund Formula. However, the PHA shall not request, nor will HUD approve, an operating subsidy for the cost of an independent audit if the audit has already been funded by subsidy in a prior year.

(2) A PHA that is required by the Single Audit Act (31 U.S.C. 7501-7507) (see 24 CFR part 85) to conduct a regular independent audit may receive operating subsidy to cover the cost of the audit. The actual cost of an independent audit, applicable to the operations of PHA-owned rental housing, is not included in the Allowable Expense Level, but it is allowed in full in computing the amount of operating subsidy under § 990.104, above.

(3) A PHA that is exempt from the audit requirements under the Single Audit Act (24 CFR part 85) may receive operating subsidy to offset the actual cost of an independent audit chargeable to operations (after the End of the Initial Operating Period) if the PHA chooses to have an audit.

(b)(1) Costs attributable to units that are approved for deprogramming and vacant may be eligible for inclusion, but must be limited to the minimum services and protection necessary to protect and preserve the units until the units are deprogrammed. Costs attributable to units temporarily unavailable for occupancy because the units are utilized for PHA-related activities are not eligible for inclusion. In determining operating subsidy calculations under the Operating Fund Formula, these units shall not be included in the calculation of Unit Months Available. Units approved for deprogramming shall be listed by the PHA, and supporting documentation regarding direct costs attributable to such units shall be included as a part of the Operating Fund Formula calculation in which the PHA requests operating subsidy for these units. If the PHA requires assistance in this matter, the PHA should contact the HUD Field Office.

(2) Units approved for nondwelling use to promote economic self-sufficiency services and anti-drug

activities are eligible for operating subsidy under the conditions provided in this paragraph (b)(2), and the costs attributable to these units are to be included in the operating budget. If a unit satisfies the conditions stated in paragraphs (b)(2)(i) through (v) of this section, it will be eligible for subsidy at the rate of the AEL for the number of months the unit is devoted to such use. Approval will be given for a period of no more than 3 years. HUD may renew the approval to allow payments after that period only if the PHA can demonstrate that no other sources for paying the non-utility operating costs of the unit are available. The conditions the unit must satisfy are:

(i) The unit must be used for either economic self-sufficiency activities directly related to maximizing the number of employed residents or for anti-drug programs directly related to ridding the development of illegal drugs and drug-related crime. The activities must be directed toward and for the benefit of residents of the development.

(ii) The PHA must demonstrate that space for the service or program is not available elsewhere in the locality and that the space used is safe and suitable for its intended use or that the resources are committed to make the space safe and suitable.

(iii) The PHA must demonstrate satisfactorily that other funding is not available to pay for the non-utility operating costs. All rental income generated as a result of the activity must be reported as income in the operating subsidy calculation.

(iv) Operating subsidy may be approved for only one site (involving one or more contiguous units) per public housing development for economic self-sufficiency services or anti-drug programs, and the number of units involved should be the minimum necessary to support the service or program. Operating subsidy for any additional sites per development can only be approved by HUD Headquarters.

(v) The PHA must submit a certification with its Operating Fund Formula Calculation that the units are being used for the purpose for which they were approved and that any rental income generated as a result of the activity is reported as income in the operating subsidy calculation. The PHA must maintain specific documentation of the units covered. Such documentation should include a listing of the units, the street addresses, and project/management control numbers.

(3) Long-term vacant units that are not included in the calculation of Unit Months Available are eligible for operating subsidy in the Requested

Budget Year at the rate of 20% of the AEL. Allowable utility costs for long term vacant units will continue to be funded in accordance with § 990.107.

(c) *Costs attributable to changes in Federal law or regulation.* In the event that HUD determines that enactment of a Federal law or revision in HUD or other Federal regulation has caused or will cause a significant increase in expenditures of a continuing nature above the Allowable Expense Level and Utilities Expense Level, HUD may in HUD's sole discretion decide to prescribe a procedure under which the PHA may apply for or may receive an increase in operating subsidy.

(d)(1) *Costs resulting from combination of two or more units.* When a PHA redesigns or rehabilitates a project and combines two or more units into one larger unit and the combination of units results in a unit that houses at least the same number of people as were previously served, the AEL for the requested year shall be multiplied by the number of unit months not included in the requested year's unit months available as a result of these combinations that have occurred since the Base Year. The number of people served in a unit will be based on the formula  $((2 \times \text{No. of Bedrooms}) \text{ minus } 1)$ , which yields the average number of people that would be served. An efficiency unit will be counted as a one bedroom unit for purposes of this calculation.

(2) An exception to paragraph (d)(1) of this section is made when a PHA combines two efficiency units into a one-bedroom unit. In these cases, the AEL for the requested year shall be multiplied by the number of unit months not included in the requested year's unit months available as a result of these combinations that have occurred since the Base Year.

(e) *Funding for resident participation activities.*—(1) *Funding amount.* Each PHA shall include in the operating subsidy eligibility calculation, \$25 per occupied unit per year for resident participation activities, including (but not limited to) those described in part 964 of this title. For purposes of this section, a unit may be occupied by a public housing resident, a PHA employee, or a police officer. If, in any fiscal year, appropriations are not sufficient to meet all funding requirements under this part, then the \$25 will be subject to pro-ration.

(2) *Use of vacant rental units.* If there is no community or rental space available for providing resident participation activities, HUD may approve, at the request of the PHA, the use of one or more vacant rental units

for resident participation purposes. A unit that satisfies the following conditions will be eligible for operating subsidy at the rate of the AEL for the number of months the unit is devoted to such use:

(i) The PHA must demonstrate that safe and suitable space for the resident participation activities is not otherwise readily available;

(ii) One or more contiguous units may be used for resident participation activities. However, the units must be located on a single site per public housing development. Further, the number of units involved must be the minimum necessary to support the resident participation activities;

(iii) The PHA must submit a certification with its Operating Fund Formula calculation that the units are being used for the purpose for which they were approved and that any rental income generated as a result of the activity is reported as income in the operating subsidy calculation; and

(iv) The PHA must maintain specific documentation of the units covered. Such documentation must include a listing of the units, the street addresses, and project/management control numbers.

#### **§ 990.109 Projected operating income level.**

(a) *Policy.* The Operating Fund Formula determines the amount of operating subsidy for a particular PHA based in part upon a projection of the actual dwelling rental income and other income for the particular PHA. The projection of dwelling rental income is obtained by computing the average monthly dwelling rental charge per unit for the PHA, and applying an upward trend factor (subject to updating). This amount is then multiplied by the Projected Occupancy Percentage for the Requested Budget Year. There are special provisions for projection of dwelling rental income for new projects.

(b) *Computation of projected average monthly dwelling rental income.*—(1) *General.* The projected average monthly dwelling rental income per unit for the PHA is calculated as follows:

(i) *Step 1: Calculation of the current year and three year averages.* The PHA calculates:

(A) The average monthly dwelling rental charge per unit for the current budget year (the "current year average" calculated in accordance with paragraph (b)(2) of this section); and

(B) The average monthly dwelling rental charge per unit for the current budget year and the immediate past two budget years (the "three year average"

calculated in accordance with paragraph (b)(3) of this section).

(ii) *Step 2: Adjustment for any increase in dwelling rental income.* If the current year average is greater than the three year average, the PHA has increased dwelling rental income. If a PHA has increased dwelling rental income, it shall perform the following calculation. The PHA shall:

(A) Subtract the three year average from the current year average;

(B) Divide the result by 2; and

(C) Add this sum to the three year average.

(iii) *Step 3: Calculating the amount of increased rental revenue that may be retained.* PHAs shall be allowed to retain 50% of any increases in dwelling rental income, so long as the PHA uses the increased revenue for the provision of resident-related improvements and services as described in § 990.116. The retained income will not be recognized in the PHA's calculation under the Operating Fund Formula. The annual amount of increased revenue retained by the PHA is calculated by subtracting the three year average from the current year average, dividing the result by two, and multiplying the result by the projected occupancy percentage (see § 990.109(b)(6)), and the unit months available (see § 990.102).

(iv) *Step 4: Applying the rental income adjustment factor.* The lower of the amount calculated under paragraph (b)(i)(A) or (b)(ii) of this section is then adjusted by the dwelling rental income adjustment factor described in paragraph (b)(5) of this section.

(2) *Average monthly dwelling rental charge per unit.* (i) The average monthly dwelling rental charge per unit shall be computed using the total dwelling rental charges for all Project Units, as shown on the Tenant Rent Rolls which the PHA is required to maintain, for the first day of the month which is six months before the first day of the Requested Budget Year. However, if a change in the total of the Rent Rolls has occurred in a subsequent month which is before the beginning of the Requested Budget Year, and before the submission of the Requested Budget Year calculation of operating subsidy eligibility, the PHA may use the latest changed Rent Roll for the purpose of the computation.

(ii) This aggregate dollar amount shall be divided by the number of occupied dwelling units as of the same date.

(iii) The Rent Roll used for calculating the projected operating income level will not reflect decreases resulting from the PHA's implementation of an optional earned income exclusion

authorized by the explanation of "annual income" in 24 CFR 5.609.

(3) *Three year average monthly dwelling rental charge per unit.* The three year average monthly dwelling rental charge shall be computed by averaging the amounts calculated under paragraph (b)(2) of this section for the current budget year and the immediate past two budget years.

(4) *Changes in supply of utilities.* The PHA must adjust the rent rolls used for purposes of the calculations described in paragraphs (b)(2) and (b)(3) of this section to reflect any change from PHA-paid utilities to resident-paid utilities, or vice versa, between the rent roll date and the projected budget year.

(5) *Dwelling rental income adjustment factor.* An adjustment factor will be applied to the calculations described in paragraphs (b)(2) and (b)(3) of this section. In FY 2001, the inflation factor will be 3%. In subsequent years, the average monthly dwelling rental charge per unit will be increased for inflation using a HUD supplied adjustment factor for the requested budget year to obtain the projected average monthly dwelling rental charge per unit of the PHA for the Requested Budget Year.

(6) *Projected occupancy percentage.* The PHA shall determine its projected percentage of occupancy for all Project Units (Projected Occupancy Percentage), as follows:

(i) *General.* Using actual occupancy data collected before the start of the budget year as a beginning point, the PHA will develop estimates for its Requested Budget Year (RBY) of: How many units the PHA will have available for occupancy; how many of the available units will be occupied and how many will be vacant, and what the average occupancy percentage will be for the RBY. The conditions under which the RBY occupancy percentage will be used as the projected occupancy percentage for purposes of determining operating subsidy eligibility are described below.

(ii) *High Occupancy PHA—No adjustments necessary.* If the PHA's RBY Occupancy Percentage, calculated in accordance with § 990.117, is equal to or greater than 97%, the PHA's Projected Occupancy Percentage is 97%. If the PHA's RBY Occupancy Percentage is less than 97%, but the PHA demonstrates that it will have an average of five or fewer vacant units in the requested budget year, the PHA will use its RBY Occupancy Percentage as its projected occupancy percentage.

(iii) *Adjustments in determining occupancy.* If the PHA's RBY Occupancy Percentage is less than 97% and the PHA has more than 5 vacant

units, the PHA will adjust its estimate of vacant units to exclude vacant units undergoing modernization and units that are vacant due to circumstances and actions beyond the PHA's control. After making this adjustment, the PHA will recalculate its estimated vacancy percentage for the RBY.

(A) *High Occupancy PHA after adjustment.* If the recalculated vacancy percentage is 3% or less (or the PHA would have five or fewer vacant units), the PHA will use its RBY Occupancy Percentage as its projected occupancy percentage.

(B) *Low Occupancy PHA—adjustment for long-term vacancies.* If the recalculated vacancy percentage is greater than 3% (or the PHA would have more than 5 vacant units), the PHA will then further adjust its RBY Occupancy Percentage by excluding from its calculation of Unit Months Available (UMAs), those unit months attributable to units that have been vacant for longer than 12 months that are not vacant units undergoing modernization or are not units vacant due to circumstances and actions beyond the PHA's control.

(iv) *Low Occupancy PHA after all adjustments.* A PHA that has determined its RBY Occupancy Percentage in accordance with paragraph (b)(6)(iii)(B) of this section will be eligible for operating subsidy as follows:

(A) Long-term vacancies removed from the calculation of UMAs will be eligible to receive a reduced operating subsidy calculated at 20% of the PHA's AEL.

(B) If the recalculated RBY Occupancy Percentage is 97% or higher, the PHA will use 97%.

(C) If the recalculated RBY Occupancy Percentage is less than 97%, but the vacancy rate after adjusting for vacant units undergoing modernization and units that are vacant due to circumstances and actions beyond the PHA's control is 3% or less (or the PHA has five or fewer vacant units), the PHA may use its recalculated RBY Occupancy Percentage as its projected occupancy percentage.

(D) If the recalculated RBY Occupancy Percentage is less than 97% and the vacancy percentage is greater than 3% (or the PHA has more than five vacant units) after adjusting for vacant units undergoing modernization and units that are vacant due to circumstances and actions beyond the PHA's control, the PHA will use 97% as its projected occupancy percentage, but will be allowed to adjust the 97% by the number of vacant units undergoing modernization and units that are vacant due to circumstances and actions

beyond the PHA's control. For a small PHA using five vacant units as its occupancy objective for the RBY, the PHA will determine what percentage five units represents as a portion of its units available for occupancy and subtract that percentage from 100%. The result will be used as the PHA's projected occupancy percentage, but the PHA will be allowed to adjust the projected occupancy percentage by vacant units undergoing modernization and units that are vacant for circumstances and actions beyond the PHA's control.

(c) *Projected average monthly dwelling rental charge per unit for new Projects.* The projected average monthly dwelling rental charge for new Projects which were not available for occupancy during the budget year prior to the Requested Budget Year and which will reach the End of the Initial Operating Period (EIOP) within the first nine months of the Requested Budget Year, shall be calculated as follows:

(1) If the PHA has another Project or Projects under management which are comparable in terms of elderly and nonelderly resident composition, the PHA shall use the projected average monthly dwelling rental charge for such Project or Projects.

(2) If the PHA has no other Projects which are comparable in terms of elderly and nonelderly resident composition, the HUD Field Office will provide the projected average monthly dwelling rental charge for such Project or Projects, based on comparable Projects located in the area.

(d) *Estimate of additional dwelling rental income.* After implementation of the provisions of any legislation enacted or any HUD administrative action taken subsequent to the effective date of these regulations, which affects rents paid by residents of Projects, HUD may adjust the projected average monthly dwelling rental charge per unit to reflect such change. HUD also shall have complete discretion to reduce or increase the operating subsidy approved for the PHA current fiscal year in an amount equivalent to the change in the rental income.

(e) *PHA's estimate of other income.* All PHAs shall estimate Other Income based on past experience and a reasonable projection for the Requested Budget Year, which estimate shall be subject to HUD approval. The estimated total amount of Other Income, as approved, shall be divided by the number of Unit Months Available to obtain a per unit per month amount.

(f) *Projected operating income level.* The projected average dwelling rental income per unit (calculated under

paragraphs (b), (c), and (d) of this section) shall be added to the estimated Other Income (calculated under paragraph (e) of this section) to obtain the Projected Operating Income Level. This amount shall not be subject to the provisions regarding program income in 24 CFR 85.25.

#### **§ 990.110 Adjustments.**

Adjustment information submitted to HUD under this section must be accompanied by an original or revised calculation of operating subsidy eligibility.

(a) *Adjustment of base year expense level.*—(1) *Eligibility.* A PHA with projects that have been in management for at least one full fiscal year, for which operating subsidy is being requested under the Operating Fund Formula for the first time, may, during its first budget year under the Operating Fund Formula, request HUD to increase its Base Year Expense Level. Included in this category are existing PHAs requesting subsidy for a project or projects in operation at least one full fiscal year under separate ACC, for which operating subsidy has never been paid, except for independent audit costs. This request may be granted by HUD, in its discretion, only where the PHA establishes to HUD's satisfaction that the Base Year Expense Level computed under § 990.105(a) will result in operating subsidy at a level insufficient to support a reasonable level of essential services. The approved increase cannot exceed the lesser of the per unit per month amount by which the top of the Range exceeds the Base Year Expense Level.

(2) *Procedure.* A PHA that is eligible for an adjustment under paragraph (a)(1) of this section may only make a request for such adjustment once for projects under a particular ACC, at the time it submits the calculation of operating subsidy eligibility for the first budget year under the Operating Fund Formula. Such request shall be submitted to the HUD Field Office, which will review, modify as necessary, and approve or disapprove the request. A request under this paragraph must include a calculation of the amount per unit per month of requested increase in the Base Year Expense Level, and must show the requested increase as a percentage of the Base Year Expense Level.

(b) *Adjustments to Utilities Expense Level.* A PHA receiving operating subsidy under § 990.104, excluding those PHAs that receive operating subsidy solely for independent audit (§ 990.108(a)), must submit an adjustment regarding the Utility Expense Level approved for operating

subsidy eligibility purposes. This adjustment, which will compare the actual utility expense and consumption for the PHA fiscal year to the estimates used for subsidy eligibility purposes, shall be submitted on forms prescribed by HUD. This adjustment, applicable to PHA fiscal years beginning on or after January 1, 1999, shall be submitted to the HUD Field Office within 45 days after the close of the PHA fiscal year that is being adjusted. Failure to submit the required adjustment of the Utilities Expense Level by the due date may, in the discretion of HUD, result in the withholding of approval of future obligation of operating subsidies and/or a delay in the recognition of the adjustment. Adjustments under this section normally will be made in the operating subsidy calculation for the second PHA fiscal year following the year being adjusted, unless a repayment plan is necessary as noted in paragraph (d) of this section.

(1) *Rates.* A change in the Utilities Expense Level because of changes in utility rates—to the extent funded by the operating subsidy—will result in an adjustment of future operating subsidy payments. However, where the rate reduction covering utilities, such as water, fuel oil, electricity, and gas, is directly attributable to action by the PHA, such as wellhead purchase of natural gas, or administrative appeals or legal action beyond normal public participation in rate-making proceedings, then the PHA will be permitted to retain one-half of the cost savings attributable to its actions for the first year and, upon determination that the action was cost-effective in the first year, for as long as the actions continue to be cost-effective, and the other one-half of the cost savings will be deducted from operating subsidy otherwise payable.

(2) *Consumption.* (i) Generally, 75% of any decrease in the Utilities Expense Level attributable to decreased consumption after adjustment for any utility rate change, will be retained by the PHA; 25% will be offset by HUD against subsequent payment of operating subsidy.

(ii) However, in the case of a PHA whose energy conservation measures have been approved by HUD as satisfying the requirements of § 990.107(f)(1) (regarding non-HUD financed incentives for energy conservation improvements), the PHA operating fund eligibility shall reflect the retention of 100% of the savings from decreased consumption after payment of the amount due the contractor until the term of the financing agreement is completed. The

decreased consumption is to be determined by adjusting for any utility rate changes and may be adjusted, subject to HUD approval, using a heating degree day adjustment for space heating utilities. The savings realized must be applied in the following order:

(A) Retention of up to 50% of the total savings from decreased consumption to cover training of PHA employees, counseling of residents, PHA management of the cost reduction program and any other eligible costs; and

(B) Prepayment of the amount due the contractor under the contract.

(iii) 25% of an increase in the Utilities Expense Level attributable to increased consumption, after adjustment for any utility rate change, will be reflected in the operating subsidy eligibility for the second PHA fiscal year following the year being adjusted, in accordance with § 990.111.

(iv) PHAs are encouraged to:

(A) Provide conservation incentives and training to residents in order to realize increased utility savings;

(B) Share information with residents regarding changes in utility costs related to rate changes and to changes in consumption; and

(C) Explain to residents conservation benefits and impacts of excess consumption on the operating budget.

(3) *Documentation.* Supporting documentation substantiating the requested adjustments shall be retained by the PHA pending HUD audit.

(c) *Energy conservation financing.* If HUD has approved an energy conservation contract under § 990.107(f)(2), then the PHA is eligible for additional operating subsidy each year of the contract to amortize the cost of the energy conservation measures under the contract, subject to a maximum annual limit equal to the cost savings for that year and a maximum contract period of 12 years.

(1) Each year, the energy cost savings would be determined as follows:

(i) The consumption level that would have been expected if the energy conservation measure had not been undertaken would be adjusted for any change in utility rate and may be adjusted, subject to HUD approval, using a heating degree day adjustment for space heating utilities;

(ii) The actual cost of energy (of the type affected by the energy conservation measure) after implementation of the energy conservation measure would be subtracted from the expected energy cost, to produce the energy cost savings for the year. (See also paragraph (b)(2)(i) of this section for retention of consumption savings.)

(2) If the cost savings for any year during the contract period is less than the amount of operating subsidy to be made available under this paragraph (c) to pay for the energy conservation measure in that year, the deficiency will be offset against the PHA's operating subsidy eligibility for the PHA's next fiscal year.

(3) If energy cost savings are less than the amount necessary to meet amortization payments specified in a contract, the contract term may be extended (up to the 12-year limit) if HUD determines that the shortfall is the result of changed circumstances rather than a miscalculation or misrepresentation of projected energy savings by the contractor or PHA. The contract term may only be extended to accommodate payment to the contractor and associated direct costs.

(d) *Additional HUD-initiated adjustments.* Notwithstanding any other provisions of this subpart, HUD may at any time make an upward or downward adjustment in the amount of the PHA's operating subsidy as a result of data subsequently available to HUD which alters projections upon which the approved operating subsidy was based. If a downward adjustment would cause a severe financial hardship on the PHA, the HUD Field Office may establish a recovery schedule which represents the minimum number of years needed for repayment.

**§ 990.111 Submission and approval of operating subsidy calculations and budgets.**

(a) *Required documentation.* (1) Prior to the beginning of its fiscal year, the PHA shall prepare an operating budget in a manner prescribed by HUD. The Board of Commissioners shall review and approve the budget by resolution. Each fiscal year, the PHA shall submit to the HUD Field Office, in a time and manner prescribed by HUD, the approved board resolution and the required operating subsidy eligibility calculation forms. The PHA shall submit revised calculations in support of any adjustments based on procedures prescribed by HUD.

(2) HUD may direct the PHA to submit its complete operating budget if the PHA has failed to achieve certain specified operating standards, or for other reasons which in HUD's determination threaten the PHA's future serviceability, efficiency, economy, or stability.

(b) *HUD operating budget review.* (1) The HUD Field Office will perform a detailed review on operating budgets that are subject to HUD review and approval. If the HUD Field Office finds

that an operating budget is incomplete, includes illegal or ineligible expenditures, mathematical errors, errors in the application of accounting procedures, or is otherwise unacceptable, the HUD Field Office may at any time require the submission by the PHA of further information regarding an operating budget or operating budget revision.

(2) When the PHA no longer is operating in a manner that threatens the future serviceability, efficiency, economy, or stability of the housing it operates, HUD will notify the PHA that it no longer is required to submit a complete operating budget to HUD for review and approval.

(c) *Compliance with environmental review requirements.*—(1) *General.* Operating subsidy funds made available to a PHA to support the operation and management of public housing are generally for activities that are not subject to environmental review requirements. A PHA, however, may use public housing program resources (including operating subsidy funds, rental and nonrental income, and operating reserves) to carry out non-routine maintenance and capital expenditure activities that may require an environmental review, as those activities are defined in HUD's prescribed Chart of Accounts.

(2) *Initial operating budget.* The ACC requires that operating expenditures may not be incurred except pursuant to an approved operating budget. Before the funding of non-routine maintenance and capital expenditure activities may be incorporated into the PHA's initial operating budget, and before the PHA may commit any funds to such activities, the PHA must obtain either:

(i) An environmental review from the Responsible Entity and submit and receive HUD approval of a Request for Release of Funds under part 58 of this title, or, in cases where HUD has determined to do an environmental review under part 50 of this title, the PHA must obtain an environmental approval from HUD; or

(ii) A determination from the Responsible Entity under part 58 of this title that the PHA's proposed non-routine maintenance and capital expenditure activities are exempt from environmental review in accordance with § 58.34(a)(12) of this title.

(3) *Revisions to operating budget.* If subsequent to adoption of its initial operating budget, a PHA determines to undertake a new non-routine maintenance or capital expenditure activity, the PHA must obtain an environmental review and release of funds, HUD environmental approval, or

an exemption from such review, as described in paragraph (c)(2) of this section, before the funding of the activity may be incorporated into a revised operating budget and before the PHA may commit any funds to such activities.

(4) *Determination of exempt activities.* If the Responsible Entity documents that a proposed non-routine maintenance or capital expenditure activity is an exempt activity, as described in paragraph (c)(2)(ii) of this section, no further action is required from the PHA and the activity may be incorporated into the PHA's initial or revised operating budget, as appropriate.

**§ 990.112 Payments procedure for operating subsidy under the Operating Fund Formula.**

(a) *General.* Subject to the availability of funds, payments of operating subsidy under the Operating Fund Formula shall be made generally by electronic funds transfers, based on a schedule submitted by the PHA and approved by HUD. The schedule may provide for several payments per month. If a PHA has an unanticipated, immediate need for disbursement of approved operating subsidy, it may make an informal request to HUD to revise the approved schedule. (Requests by telephone are acceptable.)

(b) *Payments procedure.* In the event that the amount of operating subsidy has not been determined by HUD as of the beginning of a PHA's budget year under this part, annual or monthly or quarterly payments of operating subsidy shall be made, as provided in paragraph (a) of this section, based upon the amount of the PHA's operating subsidy for the previous budget year or such other amount as HUD may determine to be appropriate.

(c) *Availability of funds.* In the event that insufficient funds are available to make payments approvable under the Operating Fund Formula for operating subsidy payable by HUD, HUD shall have complete discretion to revise, on a pro rata basis or other basis established by HUD, the amounts of operating subsidy to be paid to PHAs.

**§ 990.113 Payments of operating subsidy conditioned upon reexamination of income of families in occupancy.**

(a) *Policy.* The income of each family must be reexamined at least annually. PHAs must be in compliance with this reexamination requirement to be eligible to receive full operating subsidy payments.

(b) *PHAs in compliance with requirements.* Each submission of the original calculation of operating subsidy



eligibility for a fiscal year shall be accompanied by a certification by the PHA that it is in compliance with the annual income reexamination requirements and that rents have been or will be adjusted in accordance with current HUD requirements.

(c) *PHAs not in compliance with requirements.* Any PHA not in compliance with annual income reexamination requirement at the time of the submission of the calculation of operating subsidy eligibility shall furnish to the HUD Field Office a copy of the procedure it is using to attain compliance and a statement of the number of families that have undergone reexamination during the twelve months preceding the date of the Operating Budget submission, or the revision thereof. If, on the basis of such submission, or any other information, the Field Office Director determines that the PHA is not substantially in compliance with the annual income reexamination requirement, he or she shall withhold payments to which the PHA might otherwise be entitled under this part, equal to his or her estimate of the loss of rental income to the PHA resulting from its failure to comply with those requirements.

**§ 990.114 Phase-down of subsidy for units approved for demolition.**

(a) *General.* Units that have both been approved by HUD for demolition and been vacated in FY 1995 and after will be excluded from a PHA's determination of Unit Months Available when vacated, but they will remain eligible for subsidy in the following way:

(1) For the first twelve months beginning with the month that a unit meets both conditions of being approved for demolition and vacant, the full AEL will be allowed for the unit.

(2) During the second twelve-month period after meeting both conditions, 66% of the AEL will be allowed for the unit.

(3) During the third twelve-month period after meeting both conditions, 33% of the AEL will be allowed for the unit.

(b) *Special case for long-term vacant units.* Units that have been vacant for longer than 12 months when they are approved for demolition are eligible for funding equal to 20% of the AEL for a 12-month period.

(c) *Treatment of units replaced with Section 8 Certificates or Vouchers.* Units that are replaced with Section 8 Certificates or Vouchers are not subject to the provisions of this section.

(d) *Treatment of units replaced with public housing units.* When replacement

conventional public housing units become eligible for operating subsidy, the demolished unit is no longer eligible for any funding under this section.

(e) *Determination of what units are "replaced."* For purposes of this section, replacements are applied first against units that otherwise would fall in paragraph (a) of this section; any remaining replacements should be used to reduce the number of units qualifying under paragraph (b) of this section.

(f) *Treatment of units combined with other units.* Units that are removed from the inventory as a result of being combined with other units are not considered to be demolished units for this purpose.

**§ 990.116 Increases in dwelling rental income.**

(a) *General.* As described in § 990.109(b)(1), PHAs shall be allowed to retain 50% of any increases in dwelling rental income, so long as the PHA uses the increased income for the provision of resident-related improvements and services. The retained income will not be recognized in the PHA's calculation under the Operating Fund Formula.

(b) *Eligible uses for increased rental revenue.* The uses for the retained income must be developed with front end resident participation and ongoing input and shall be made part of the PHA plan submission. (See 24 CFR part 903). Examples of eligible uses for the retained income include, but are not limited to:

- (1) Physical and management improvements that benefit residents;
- (2) Resident self-sufficiency services;
- (3) Maintenance operations;
- (4) Resident employment and training services;
- (5) Resident safety and security improvements and services; and
- (6) Optional earned income exclusions.

**§ 990.117 Determining actual and requested budget year occupancy percentages.**

(a) *Actual occupancy percentage.* When submitting Operating Fund Formula calculations for Requested Budget Years, the PHA shall determine an Actual Occupancy Percentage for all Project Units included in the Unit Months Available. The PHA shall have the option of basing this option on either:

- (1) The number of units occupied on the last day of the month that ends 6 months before the beginning of the Requested Budget Year; or
- (2) The average occupancy during the month ending 6 months before the

beginning of the Requested Budget Year. If the PHA elects to use an average occupancy under this paragraph (a)(2), the PHA shall maintain a record of its computation of its Actual Occupancy Percentage.

(b) *Requested budget year occupancy percentage.* The PHA will develop a Requested Budget Year Occupancy Percentage by taking the Actual Occupancy Percentage and adjusting it to reflect changes up or down in occupancy during the Requested Budget Year due to HUD-approved activities such as units undergoing modernization, new development, demolition, or disposition. If after the submission and approval of the Operating Fund Formula calculations for the Requested Budget Year, there are changes up or down in occupancy because of modernization, new development, demolition or disposition that are not reflected in the Requested Budget Year Occupancy Percentage, the PHA may submit a revision to reflect the actual change in occupancy due to these activities.

(c) *Documentation required to be maintained.* The PHA must maintain and, upon HUD's request, make available to HUD specific documentation of the occupancy status of all units, including long-term vacancies, vacant units undergoing modernization, and units vacant due to circumstances and actions beyond the PHA's control. This documentation shall include a listing of the units, street addresses, and project/management control numbers.

**§ 990.120 Audit.**

PHAs that receive financial assistance under this part shall comply with the audit requirements in 24 CFR part 85.26. If a PHA has failed to submit an acceptable audit on a timely basis in accordance with that part, HUD may arrange for, and pay the costs of, the audit. In such circumstances, HUD may withhold, from assistance otherwise payable to the PHA under this part, amounts sufficient to pay for the reasonable costs of conducting an acceptable audit, including, when appropriate, the reasonable costs of accounting services necessary to place the PHA's books and records into auditable condition. The costs to place the PHA's books and records into auditable condition do not generate additional subsidy eligibility under this part.

**§ 990.121 Effect of rescission.**

If there is a rescission of appropriated funds that reduces the level of funding under the Public Housing Capital Fund

program, to the extent that the PHA can document that it is not possible to complete all the vacant unit rehabilitation in the PHA's approved Annual Statement, the PHA may seek and HUD may grant a waiver for 1 fiscal

year to permit full eligibility under the Operating Fund Formula for those units approved but not funded. (See part 905 of this title for additional information regarding the Capital Fund program.)

Dated: March 7, 2001.

**Mel Martinez,**

*Secretary.*

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