
 CHAPTER 1. INTRODUCTION

1-1. PURPOSE

This handbook replaces earlier instructions to mortgagors entitled Handbook of FHA Requirements Governing Financial Operations and Accounting Procedures for Insured Multifamily Projects. This chapter provides an overview of the objectives of the handbook as the principal guide for financial and accounting operations for HUD-held and HUD-insured multifamily projects. The handbook incorporates accounting standards and principles promulgated by the General Accounting Office (GAO), appropriate AICPA Generally Accepted Accounting Principles (GAAP), Office of Management and Budget (OMB), and HUD.

1-2. SCOPE

The handbook applies to multifamily rental projects under a charter or regulatory agreement permitting HUD to exercise control over project administration and operation. This handbook applies to insured, co-insured, and HUD-held projects. It does not apply to cooperatives, condominiums, or certain Section 608 projects outside HUD control, even though the project may be encumbered by a mortgage insured or held by HUD.

The primary users of this handbook are accountants, mortgagors, management agents and their employees. It has been prepared in the interest of providing complete and uniform financial information related to maintaining operations of the following HUD projects:

- o 202 Direct Loans for Housing for the Elderly or Handicapped
- o 207M Mobile Home Courts
- o 207 Multifamily Rental Housing, Pre-War Legislation and Formerly HUD-held mortgages sold with insurance)
- o 207/223(c) Formerly HUD-owned Projects
- o 213S Sales and Investor Cooperatives
- o 213M Management Cooperatives

- o 213(i) Consumer Cooperatives
- o 220 Urban Renewal/Declining Area Rental Housing

- o 221(d)(3) Market Rate, Moderate Income Families
- o 221(d)(4) Market Rate, Moderate Income Families
- o 221(d)(5) Below Market Interest Rate (BMIR)
- o 221(h) Rehab. Sales Projects
- o 223(e)/220 Rehab./Refinance Existing, Declining Neighborhood
- o 223(f)/207 Purchase/Refinancing Existing Housing
- o 231 Housing for the Elderly
- o 232 Nursing Homes, Intermediate Care Facilities
- o 233 Experimental Housing
- o 236 Housing for Lower Income Families
- o 241 Supplemental Loans (Capital Improvement/Equity Takeout
- o 242 Hospitals
- o Title XI Group Practice Facilities

1-3. HUD CONTROL

Prior to 1961, project control was implemented mainly through the issuance of preferred stock to the FHA under provisions of a corporate charter. Since 1961, however, FHA/HUD has exercised control through provisions of a Regulatory Agreement including:

- A. The regulatory agreement provides that the project owner shall not, without prior written approval of HUD:
 - 1. Convey, transfer, or encumber any of the mortgaged property, or permit conveyance, transfer, or encumbrance of such property.
 - 2. Assign, transfer, dispose of, or encumber any personal property of the project, including rent, or pay out funds, except for reasonable operating expenses and necessary repairs, from any project source other than "surplus cash."

- 3. Convey, assign, or transfer any beneficial interest in any trust holding title to the property, or the interest of any general partner owning the property, or any right to manage or receive the rents and profits thereof, unless the transferees or assignees assume the obligations of the Regulatory Agreement through a written instrument satisfactory to the Secretary.

4. Remodel, add to, reconstruct, or demolish any part of the mortgaged property, or subtract from any real or personal property of the project.
 5. Except for natural persons, engage in any other business or activity, including the operation of any other rental project, or incur any liability or obligation not in connection with the project.
 6. Permit use of the project for any purpose except the use originally intended, or permit commercial use to a greater extent than originally approved by the Secretary.
- B. The regulatory agreement sets forth specific requirements on the establishment and maintenance of various funds (i.e. security deposits, residual receipts, replacement reserves).
 - C. The regulatory agreement defines the requirements necessary for tenant application, eligibility and recertification.
 - D. The regulatory agreement establishes the requirements of the project management and administration including maintenance of accounting records in accordance with HUD's guidance.
 - E. The regulatory agreement sets forth provisions for non-discrimination.

NOTE: Owners, sponsors, management, and independent public accountants shall refer to the Regulatory Agreement and to other controlling documents for specific provisions, requirements, and restrictions applicable to the specific project.

1-4. LEGISLATIVE AUTHORITY

- A. Sections 207, 213, 220, 221, 223, 231, 232, 233, 236, 241, 242, and Title XI of the National Housing Act as Amended, Section 8 of the U.S. Housing Act of 1937, and Section 202 of the Housing Act of 1959. Provisions of these acts include the following:
 1. HUD insures mortgages made by private lending institutions to build or rehabilitate multifamily rental or cooperative housing a) for

moderate income or displaced families (Section 221); b) suited to the needs of the elderly or handicapped (Section 231); and c) to accommodate 20 or more patients requiring skilled nursing care and related medical services (Section 232); d) for the treatment of persons who require medical care furnished only, or most effectively, by hospitals (Section 242); e) for group practice medical facilities to relieve overburdened hospitals and nursing homes (Title XI); f) experimental housing projects (Section 233); and g) by private or public developers that contain at least five dwelling units (Section 207).

2. HUD provides direct long term loans to eligible, private or not-for-profit sponsors to finance rental or cooperative housing facilities for occupancy by elderly or handicapped persons (Section 202).
3. HUD insures mortgages to purchase or refinance existing projects originally financed with or without Federal mortgage insurance (Section 223).

4. The Secretary is authorized to make periodic interest reduction payments on behalf of the owner of a project designed for lower income families (Section 236).
5. HUD insures loans made by private lending institutions to pay for improvements to apartment projects, nursing homes, hospitals, or group practice facilities that carry HUD-insured mortgages (Section 241).
6. Public Housing Agencies (PHAs) and HUD administer a program to assist very low-income families in obtaining decent safe and sanitary housing by selecting landlords to lease properties that meet certain safety and sanitation standards (Section 8). The various assistance programs authorized under this Section include Lower Income Rental Assistance, Existing Housing Voucher, Certificate Programs, New Construction, Substantial Rehabilitation, Special Allocations (Loan Management Set Aside), Farmer's Home

(515), and Section 202/8 programs. Of these, this handbook applies only to projects whose mortgages are insured or held by HUD.

- B. Sections 2 and 4 of the Inspector General Act of 1978. The HUD Inspector General (IG) has the statutory responsibility to conduct, supervise, and coordinate audits and investigations relating to HUD's programs and operations. The IG also provides leadership and recommends policies designed to promote the economy, efficiency, and effectiveness and to prevent fraud and abuse.
- C. Section 42, Internal Revenue Code of 1986, as amended, Low Income Housing Tax Credits. This section authorizes tax credits for low income housing meeting certain criteria. Current and prospective owners may not receive excessive profits or subsidies or create undue mortgage insurance risks by combining

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Low Income Housing Tax Credits (LIHTC) with other HUD programs. HUD requires a pre-commitment review of all cases that use LIHTCs.

- D. Section 416 and 421 of the Housing and Community Development Act of 1987, Misuse and diversion of Funds. These sections impose specific sanctions and penalties for the misuse and diversion of funds and for the violation of regulatory agreements and other applicable regulations. Penalties may include 1) a fine of up to \$250,000 or imprisonment for up to five (5) years, or both, or 2) requesting the U.S. Attorney General to recover any assets or income of the violator.
- E. Section 108 of the HUD Reform Act of 1989. The Secretary may impose a monetary penalty on any mortgagor of a multifamily property who has agreed to use non-project funds to pay project liabilities or make cash contributions to the project for payments due under the mortgage but who fails to fulfill that agreement. A monetary penalty may also be imposed for any violation of the regulatory agreement, including failure to maintain books and accounts of the project in accordance with requirements prescribed by the Secretary.