

“Reasonable” or Not?

PHADA’s Comments on HUD’s Asset Management Guidance

centralized procurement
negotiated rulemaking
central office cost center
defederalization
small housing
property management fee
stop-loss
asset management fee
fees-for-service
project-based
bookkeeping fee
property management fee
central office cost center
excess cash
QHWRA
project-based a
Capital Fund
fees-for-service
centralized procurement
project-based management
negotiated rulemaking
maximum flexib
management fee
bookkeeping fee
project-based accounting
FHA database

“Reasonable” or Not?

PHADA’s Comments on HUD’s Asset Management Guidance

Comments submitted November 6, 2006
in response to Federal Register Notice 5099-N-01



Public Housing Authorities Directors Association

PHADA Executive Board

Jon Gutzmann, President

St. Paul (MN) Public Housing Agency

John Johnson, Senior Vice President

Oklahoma City (OK) Housing Authority

J. Richard Parker II, Immediate Past President

Athens (GA) Housing Authority

P. Curtis Hiebert, Vice President—Legislation

Keene (NH) Housing Authority

Stephanie Cowart, Vice President—Professional Development

Niagara Falls (NY) Housing Authority

John Harmon, Vice President—Housing

Bellingham/Whatcom Co. (WA) Housing Authority

Sheri Lee, Vice President—Membership Services

Glasgow (KY) Housing Authority

L. DeWitt Boosel, Treasurer

Mercer County (PA) Housing Authority

Nancy Walker, Parliamentarian

Laurinburg (NC) Housing Authority

Paula Ledford, Secretary

Dyersburg (TN) Housing Authority

Richard Murray, Sergeant at Arms

East Baton Rouge Parish (LA) Housing Authority

Author: Ted Van Dyke

Designer: Katherine Senzee

PHADA Executive Director: Tim Kaiser

Copyright © 2006, Public Housing Authorities Directors Association.

Suggested citation:

Public Housing Authorities Directors Association (PHADA). 2006. *“Reasonable” or not? Comments submitted November 6, 2006 in response to Federal Register Notice 5099-N-01*. Washington, DC: PHADA.



Public Housing Authorities Directors Association
511 Capitol Court NE, Washington, DC 20002
(202) 546-5445 www.phada.org

Contents

Foreword..... vii

Introduction 1

Section One: Property Management Fees..... 3

- A. Field office fee schedules.....3
- B. 80th percentile of a portion of the FHA database.....3
 - 1. Limited dividend properties.3
 - 2. Characteristics of properties in FHA database.....4
 - 3. Add-ons.5
 - 4. Twenty-four regulatory and operating environment differences.....6
- C. Using market data and scope of work to develop a fee7
- D. Property management fee schedules should not be implemented until 201110
- E. HUD must inflate fees annually12
- F. Property management fees should be provided for “limited vacancy” units14
- G. Proposed changes to HUD’s methodology15
- H. Other reasonable fees15
 - 1. Using mixed-finance method based on 6 percent of imputed tax-credit rent.....15
 - 2. Use FHA database to base fee on percentage of property’s operating cost.....16

Section Two: Bookkeeping Fees 20

- A. HUD’s \$3.50 PUM for accounting is based on unreliable data20
- B. HUD should not use the median in the FHA database as a cap for public housing.....23
- C. Developing an accurate amount for the cost of accounting25
- D. Information technology costs26
- E. Human resources costs27

Section Three: Asset Management Fees..... 29

- A. Asset management responsibilities29
- B. Costing out asset management responsibilities.....31
 - 1. The project-based Section 8 contract administrators.....31
 - 2. Methods described in the Harvard cost study.....31

3. Limited dividend property payouts and partnership management fees.....	33
C. Requirements placed by HUD on charging properties an asset management fee	34
Section Four: Capital Fund.....	36
A. QHWRA permits capital funds eligible for operations to be used for administrative expenses.....	36
B. Additional Capital Fund issues.....	37
1. Payment of the 10 percent management fee.....	37
2. Capital Fund Financing Program	38
3. Front-line costs vs. management fees.....	38
4. Non-dwelling equipment.....	39
5. Management improvements.....	39
Section Five: Assignment of Costs	40
A. The language in the rule itself.....	40
B. Explanations provided during negotiated rulemaking.....	42
C. Procurement.....	43
D. Maintenance supervisors.....	44
E. Administrative supervisors	47
F. Inspections and other issues.....	47
G. Board training, stipends and travel	49
Section Six: Excess Cash.....	50
A. Excess cash should not depend on a specific reserve level for every property.....	50
B. The rule allows excess cash to be used for central office costs	51
Section Seven: Small PHAs.....	53
A. Additional work is needed to establish thresholds for administrative costs	53
B. Small PHAs with single AMPs should not have to differentiate between central and other costs	54
Section Eight: Need for flexibility to cope with funding shortfalls	55
A. Effect of a 74 percent proration in 2007	55
B. Extend the exemption from asset management to housing authorities with 500 units or fewer	57

C. Reserves for the central office cost center58

Section Nine: Rulemaking through notices..... 59

 A. Formal notice and comment required.....59

 B. Defederalization.....59

Section Ten: PHAS..... 61

Conclusion..... 63

Index 65

Foreword

PHADA asks that you review the comments it submitted on HUD's asset management guidance. For the past year, PHADA worked diligently with the Department to develop effective guidelines, and to its credit, HUD has incorporated a number of the ideas presented by housing authorities. Unfortunately, HUD's guidance falls short of getting it right in many areas: HUD's process for developing these guidelines has been severely deficient, and in some cases possibly illegal; the guidelines are overly prescriptive and micromanage PHA operations in new and unhelpful ways; and the Department continues to request insufficient levels of funding which erodes PHAs' ability to fulfill their missions. PHADA has long maintained that HUD should be flexible in its asset management guidelines in order to allow housing authorities to maximize insufficient resources. Stated another way, the Department simply must abide by *its* own "maximum flexibility" dictum as spelled out in its rule especially when *it* seeks to fund housing authorities at only 75 cents on the dollar (HUD's 2007 budget submission).



*Jon Gutzmann
PHADA President
St. Paul (MN) PHA*

PHADA's comments describe these shortcomings. We are sending them to you so that you can see for yourself if HUD is ready to implement asset management. Housing authorities need your help in convincing the Department to slow down, evaluate industry suggestions thoroughly, and carry out research when needed. PHADA hopes you will take the time to discover how much remains to be done.

Housing authorities need your help in convincing the Department to slow down, evaluate industry suggestions thoroughly, and carry out research when needed.

Very briefly, the proposed management fees jeopardize housing authorities' ability to fulfill their mission because they do not meet the rule's standard of being "reasonable." The fees are not "reasonable" because they neither treat public housing comparably to private owners nor provide the extra resources to carry out public housing's unique responsibilities.

The guidance violates the Quality Housing and Work Responsibility Act (QHWRA) by not permitting capital funds available for operations to be used for administration.

In addition, HUD has not followed the rule's clear enunciation that front-line management services can be performed centrally and still be expensed to the project, placing an even greater burden on the already overstretched management fees.

PHADA asks that the Department take the time available under the rule, which does not mandate asset management until 2011, to develop guidance that follows the

rule's "maximum flexibility" language and the law, and treats housing authorities similarly to their private counterparts upon which the system is based.

I want to thank all the PHADA staff for their hard work in representing its members on this important issue, especially Executive Director Tim Kaiser, who has insisted HUD develop its guidance with the input of housing authorities, Ted Van Dyke, who penned these comments, and Katherine Senzee, who designed this booklet.

A handwritten signature in black ink, appearing to read "Jon Gutzmann". The signature is fluid and cursive, with a large initial "J" and "G".

Jon Gutzmann
PHADA President

Introduction

November 6, 2006

Office of the General Counsel
Rules Docket Clerk
Department of Housing and Urban Development
451 Seventh St., S.W.
Room 10276
Washington, D.C. 20410-0001

Re: Docket Number FR-5099-N-01, Public Housing Operating Fund Program: Guidance on Implementation of Asset Management

Notice PIH 2006-33, Changes in Financial Management and Reporting Requirements for Public Housing Agencies Under the New Operating Fund Rule (24CFR Part 990); Interim Instructions

To Whom It May Concern:

PHADA submits these comments on behalf of its approximately 1,900 members. PHADA has worked closely with the Department on the development of asset management guidance. Although a good deal of progress was made, PHADA believes that discussion of many of these issues was ended prematurely and that HUD has published this guidance without fully taking into account many important concerns PHADA shared with the Department. PHADA is prepared to continue working with the Department to reach satisfactory conclusions on these outstanding issues and asks the Department, after receiving these comments, to reopen a dialogue with housing authorities and the industry groups which represent them.

The accumulated weight of the evidence presented should give the Department pause and lead it to conclude that it is not yet ready to implement these regulations.

PHADA realizes that HUD may not agree with each and every one of its comments. It believes, though, that the accumulated weight of the evidence presented should give the Department pause and lead it to conclude that it is not yet ready to implement these regulations. Hopefully, as the Department reviews these comments it will keep in mind that the rule states that “PHAs must be in compliance with... asset management in 2011,” five years from now. There is more than enough time for the Department to get the conversion to asset management right. PHADA appreciates the Department’s attention to these comments.

Section One: Property Management Fees

The rule calls for property management fees to be “reasonable.” HUD has proposed three separate methods a housing authority could use to determine its property management fee.

A. Field office fee schedules

The first method is to use the field office multifamily program fee schedules. Although PHADA agrees that they should be used as one “reasonable” method, it also concurs with the Department that these schedules alone cannot be considered a “reasonable” property management fee. The Department has demonstrated that a) in many cases the field office fee schedules are not even available; b) they are not updated every two years as required and in some cases have not been updated for more than a decade; c) there is no uniform and reliable method for calculating the fees; d) there is neither a consistent method for determining what add-ons are eligible nor for determining their worth; and e) there is no consistent method used to develop a cap.

B. 80th percentile of a portion of the FHA database

As a result of these deficiencies the Department developed a second method for setting “reasonable” management fees. This method pegs them at the 80th percentile of a segment of the FHA database properties, which is approximately 120 percent of the mean, the system used to develop property management fees in the multifamily program. Unfortunately, the notice and supplement to the Financial Management Handbook differ on what segment HUD is using, variably describing it as “all for-profit and unlimited dividend” FHA properties (notice), “all profit-motivated and limited dividend” FHA properties (p. 33 of the supplement) and “unlimited dividend and non-profit” properties (Attachment A, p. 52 supplement). Therefore, it is impossible at present to know on what basis public housing’s property management fees are set using this method.

1. Limited dividend properties. It is clear, though, that HUD has excluded some properties in the FHA database that were used in the Harvard cost study to develop the property expense levels. PHADA does not agree that properties, such as the limited dividend ones, assuming that Attachment A is accurate, should be excluded from developing property management fees and it asks the Department to include them.

First of all, as mentioned, these limited dividend properties were included in creating the PELs. Therefore, public housing costs are based on these properties. It is not fair at this point to exclude the property management and bookkeeping fees for these properties, because it now means that these fees no longer pay for these costs. Without including all the properties, there is no direct correlation between the fees and the costs.

Secondly, there is no logical reason to exclude one group, such as the limited dividend properties, while including another group, such as the non-profit ones. In each of these cases, the owners have restrictions on how they can expend excess cash, so it does not make sense to exclude one and not the other. Furthermore, it is not likely that a limited dividend owner would put excess money into fees. The owner would be more likely to place excess cash into the properties, so that the value of the property

would be enhanced, rather than spend it on a property management company for which the owner will see no return.

Thirdly, the Management Agent Handbook authorizes the use of limited dividend properties, when there are not enough unlimited dividend ones to develop a sample. In fact, the field offices are supposed to use limited dividend ones before they use non-profit ones.

Finally, PHADA supports the inclusion of limited dividend properties as in the best interests of its members, since these properties have the highest average property management fees.

2. Characteristics of properties in FHA database. In addition, for over 10 months PHADA has asked HUD for a variety of information on these properties without a satisfactory response. PHADA has requested information on the operating cost, the resident income, the average age, average bedroom size, neighborhood poverty level, percentage elderly and percentage in the central city. This information is critical in evaluating whether or not the FHA database is comparable to public housing. It is certainly not right for a governmental agency such as HUD to establish a public policy, such as property management fees, without sharing the basis for that policy in a fully transparent way with the public.

The Management Agent Handbook 4381.5, rev. 2, acknowledges that the factors for which PHADA seeks information affect the property management fee. It states that “agents managing projects with long-term project characteristics/conditions that require additional management effort beyond the activities covered by the residential management fee” are entitled to add-ons. Add-ons which are eligible include whether or not the property is assisted, whether it has a high portion of three or more bedroom units, the neighborhood condition, whether the property is non-profit or not and whether the development is a family one.

Since the project characteristics/conditions affect property management costs, it is vital to know what the characteristics of the FHA database are and, if they are not similar to those of public housing, it is vital to provide a cost adjustment to compensate public housing authorities for managing properties with these different characteristics.

The Management Agent Handbook states that “agents managing projects with long-term project characteristics/conditions that require additional management effort beyond the activities covered by the residential management fee” are entitled to add-ons.

The Management Agent Handbook has used a very analogous situation to the one HUD is faced with in developing a property management fee for public housing authorities. In section 3.21(a)(2) it says, “...if the projects used to establish the residential fee range were all unassisted, HUD-insured projects, allowing an Add-on for subsidy contract administration could be appropriate.” Therefore, according to the

handbook, an add-on could be appropriate based on the differences between the properties used to establish the residential range and the properties which will be using the range.

One-third or more of the FHA database properties do not even serve any assisted families or serve very few. The properties are considerably newer; they have a lower average per-unit bedroom size; they have a higher percentage of elderly households; they are in neighborhoods with lower poverty; the average operating cost is considerably lower; and the average resident income is higher.

Although HUD has not provided a response to the questions PHADA has posed concerning the characteristics of the FHA database, there is enough information from the Harvard cost study and other sources to be able to reach some conclusions. First of all, we know that 1/3 or more of the properties do not even serve any assisted families or serve very few. We also know the properties are considerably newer; they have a lower average per-unit bedroom size; they have a higher percentage of elderly households; they are in neighborhoods with lower poverty; the average operating cost is considerably lower; and the average resident income is higher.

Therefore, these properties are quite dissimilar to public housing, and since these are the very factors which drive operating and property management costs, it is not “reasonable” simply to take the property management fee from these properties and apply it to public housing. As the Management Agent Handbook states, additional funding must be provided to properties with these long term characteristics/conditions to account for the differences between them and the properties used to establish the range.

3. Add-ons. HUD, however, has not made any add-ons available to housing authorities to adjust its property management fee schedule even though these add-ons are specifically authorized for the multifamily program upon which asset management is supposed to be based.

According to statements made by the director of the public housing financial management division, Greg Byrne, no add-ons are provided to housing authorities because he feels they are already included in the multifamily property management fees.

Undoubtedly, if a multifamily property receives an add-on, it is included in its fees. There are two flaws with HUD’s position, however. First of all, it relies on the field office fee schedules which it itself acknowledges are seriously compromised. As mentioned, there is no consistency from field office to field office as to what add-ons are permitted, nor is there any method or transparency as to how the amount of the add-ons is calculated. Finally, most field offices include an overall cap on the amount of add-ons which can be included, even though this cap is never mentioned and therefore never authorized in the Management Agent Handbook. Therefore, whatever add-

ons might be included in multifamily property management fees cannot be relied upon to be used in the public housing program. Housing authorities cannot be sure there was an add-on; they cannot be sure the add-on amount is appropriate; and they cannot be sure the add-on was not reduced improperly by the cap.

The second flaw relates to a previous comment—no one in the public knows the characteristics of the properties used by HUD to develop the property management fee schedules. Therefore, there is no way to tell whether or not they are comparable to public housing properties. If they are not, and evidence available to PHADA indicates that they are not, then the add-ons included in the multifamily fees will not be reflective of the add-ons which should be available to public housing properties.

The multifamily properties used to develop the property management fee schedule are simply not representative of the public housing properties which must use this schedule.

To take a simple example, imagine that the multifamily properties in field office X all have an average bedroom size of 2.5 bedrooms per unit or smaller. Imagine this field office provides an add-on of \$3 PUM for properties which average 3 bedrooms or larger per unit. None of the properties used to calculate the field office property management fee would include this add-on, and so the average property management fee would not reflect the add-on. Therefore, the add-on is not available in any way to public housing properties in that field office which average 3 or more bedrooms per unit.

If half of the public housing properties in this field office fall into this category, not a single one will receive an add-on perfectly eligible in the multifamily program. As a result, every one of these public housing properties will be inadequately funded for their property management responsibilities based on HUD’s methodology.

This example can be repeated over and over again, with other characteristics for which add-ons are available. The multifamily properties used to develop the property management fee schedule are simply not representative of the public housing properties which must use this schedule. Since they are not representative, housing authorities are not provided access to the add-ons which are available in the multifamily program. This situation is not acceptable as it means that HUD has not provided a “reasonable” fee for public housing properties. Housing authorities must be provided an opportunity to receive adequate funding for their properties’ characteristics, an opportunity not provided under these guidelines.

4. *Twenty-four regulatory and operating environment differences.* Another reason the HUD fee schedules do not provide a “reasonable” fee is that they do not take into account the 24 regulatory and operating environment differences which distinguish public housing from the multifamily program. These differences are identified in the Harvard cost study itself.

They are not trivial and consist of such major program requirements as PHAS, the annual plan, the lease and grievance procedures, rent calculations, annual inspections,

procurement, Section 3, community service, pets, tenant participation requirements and mixing young disabled with elderly populations along with such important operating environment differences as information technology requirements, security, organization and work rules, legal and the costs of being a public entity.

These are differences between public housing and other assisted properties. OMB Circular A-87 defines how to arrive at “reasonable costs.” It states that “in determining reasonableness of a given cost, consideration shall be given to... the restraints or requirements imposed by... Federal... laws and regulations....” Therefore, in determining a “reasonable” property management fee HUD must take the cost of complying with these federal regulations into account.

Yet, as mentioned, HUD is basing its property management fee on many properties which do not even serve assisted families or serve very few. It is unclear what percentage of the properties fall into this category, since HUD has not consistently defined which properties are included in its database. It is a large percentage, though, and one can be fairly confident that it must be 1/3 or more.

For these properties, it is not simply a question of the difference between rent calculation rules for project-based Section 8 and public housing—these properties do not have to perform any rent calculations at all. It is no secret how time consuming and difficult income certification is for housing authorities, and how diligent property managers must be to ensure this work is done correctly. Yet 1/3 or more of the properties upon which public housing’s property management fee is based do not even have to check income or perform rent calculations. It must be obvious to all that it is not appropriate to base the property management fee of agencies such as housing authorities that are so minutely regulated and inspected so regularly on those of agencies which have none of these regulations or inspections.

One-third or more of the properties upon which public housing’s property management fee is based do not even have to check income or perform rent calculations.

As with the add-ons, this example could be repeated over and over. To quote a cliché, HUD is comparing apples to oranges. It is simply not “reasonable” on the part of the Department, nor does it follow OMB guidelines, to base public housing’s property management fee on this group of properties without adjusting for the extremely important differences between the two.

C. Using market data and scope of work to develop a fee

PHADA believes, then, that neither of HUD’s two methods provides a “reasonable” property management fee. The Department has offered a third method which appears somewhat more flexible. At present, though, it is very uncertain exactly what this method is.

According to the notice, housing authorities may develop a fee that “is appropriate for the scope of work, specific circumstances of the property, and local or national market for the services provided.” The notice goes on to say that “PHAs are... en-

couraged to consult with HUD on fees that may depart from this guidance prior to charging the fees.”

The Handbook supplement, which is to be regarded as regulation though, says a PHA may develop another fee based on “other compelling data reflecting property management fees in the local market.” Differing from the notice, it follows up by saying, “Prior to the establishment and use of reasonable fees based on ‘other compelling data,’ PHAs will need the Department’s approval.”

These two standards are very different and leave a great deal unexplained. If the language from the notice holds true, it appears as if a PHA could develop a fee just as PHADA has outlined. It could take the local or national market number provided by HUD, and then adjust it for the scope of work, including the 24 regulatory and operating differences, and then include the add-ons to take into account the specific circumstances of the property, such as its bedroom size average, location, age, and tenant population.

An agency which developed a property management fee according to this method is encouraged to share the information with the Department. There is no description, however, of what happens if the Department disagrees with the housing authority. How will these differences be resolved? Will the independent auditors make this determination? On page 9 of the supplement, it says, “...auditors need to ensure that... fees meet the reasonableness guidelines established by the Department.” Will the auditor make this determination during the annual audit and if so on what basis? Will the determination wait until the final evaluation of asset management is conducted in 2011? Or will HUD itself rule a fee as not meeting its understanding of reasonableness after a PHA has finished its consultation with the Department, as indicated in the Handbook supplement? Housing authorities need answers to these questions in order to evaluate the viability of this third method.

If the language from the notice holds true, it appears as if a PHA could develop a fee just as PHADA has outlined. It could take the local or national market number provided by HUD, and then adjust it for the scope of work, including the 24 regulatory and operating differences, and then include the add-ons to take into account the specific circumstances of the property, such as its bedroom size average, location, age, and tenant population.

Although it appreciates the Department’s attempt to provide additional flexibility in regard to property management fees, PHADA has two major points to make in regard to this third option. The first is that HUD’s two main fee schedules are so flawed that they are not appropriate for many housing authorities. The Department should not try to rectify proposals with such structural flaws by offering individual PHAs the chance to request a different fee amount. That method places the burden of correcting the Department’s mistakes on the individual PHA.

Instead, the Department itself should correct the structural flaws in its proposals. It should adopt its own language, as well as the suggestions made in these comments by PHADA, and develop a fee schedule based on “the scope of work, the specific circumstances of the property and local or national market for the work provided.” Once it has developed a fee schedule on this basis, it should then have a third method for those rare instances where special circumstances might require a fee outside the guidelines.

The Department should adopt its own language, as well as the suggestions made in these comments by PHADA, and develop a fee schedule based on “the scope of work, the specific circumstances of the property and local or national market for the work provided.”

The second point that PHADA would like to make is that based on the Department’s reactions to comments PHADA has raised over the course of the discussions on property management fees, it does not have complete confidence in the Department’s objectivity in determining whether a fee developed by a housing authority would be considered “reasonable” or not.

First of all, as mentioned, the Department has not responded to repeated requests by PHADA for the data demonstrating the basis of the fees put forth in the Handbook supplement. Thus, it cannot really determine what the “national market” is for property such as the ones it operates. If, as mentioned, all the properties in field office X have fewer than 2.5 bedrooms per unit on average, a housing authority cannot know what the “national market” is for properties which average 3 bedrooms per unit. Thus, HUD’s reluctance to share this data has reduced PHADA’s confidence in its willingness to evaluate property management fees objectively.

Secondly, the Department has failed to act on numerous suggestions made repeatedly by PHADA in developing property management fees. Despite the language in option number 3, it has steadfastly refused to provide any adjustment for the 24 regulatory and operating environment differences. How then, can PHADA have any confidence that when a housing authority says its property management fee needs to be higher because of these differences, HUD will agree with the housing authority? Similarly, HUD has refused to inflate the 2004 amounts to 2007 when they will be used. It has not made any attempt to analyze the presence or non-presence of add-ons in the property management fee schedules to determine whether public housing is being offered the same opportunities as multifamily properties. It has excluded whole sections of properties from the FHA database, such as limited dividend ones, even though they were used in the Harvard cost study and their fees must be reasonable since HUD has approved them for more than four decades.

Thus, HUD’s offer to allow a PHA to develop its own fee based on the language in the notice is suspect, since it has refused to acknowledge the validity of these legitimate points in the fee schedules it has developed.

In addition, PHADA made additional specific suggestions of other methods of determining fee reasonableness which the Department has rejected without any explanation. One of these, the use of 6 percent of the imputed tax credit rent, is actually a method developed by HUD itself and used for public housing units in the mixed finance program. It is not clear to PHADA how a fee developed by the Department for managing public housing units could not be considered “reasonable,” especially when these units are generally brand-new and are occupied by tenants who have gone through stricter screening than other public housing residents.

Agencies are not required to comply with project-based management in 2007 under the rule.

PHADA believes another proposal it has made in writing to the Department which would base the property management fee on the operating cost of the property also meets the standard of “reasonable” and should be included as an option for housing authorities to use. Again, even though this proposal mirrors multifamily’s property management fee approach and takes into account a property’s specific circumstances, the Department has not even provided PHADA with the courtesy of an explanation of why it does not meet its standard of “reasonable.”

Thus, although there is some potential merit in HUD’s third proposal, based on the Department’s own behavior over the past year in developing property management fee schedules, PHADA is not convinced that housing authorities can count on an objective evaluation by the Department. Therefore, it is not a substitute to developing an accurate property management fee schedule in the first place.

D. Property management fee schedules should not be implemented until 2011

PHADA has several additional remarks to make in regards to the property management fees. First of all is the question of when they should be applied. According to the supplement, housing authorities will be required to comply with the property management fee schedules during their second year of project-based accounting, or starting July 1, 2008 for PHAs whose fiscal years end June 30.

PHADA does not believe this decision complies with the operating fund rule. According to the rule, PHAs must comply with project-based accounting in 2007 and project-based management in 2011.

It is true that the reference in the rule to “reasonable” property management fees comes in the section of project-based accounting. Therefore, one could say that the “reasonable” property management fees must be effective in 2007. The Department itself, though, has not taken this interpretation, because it has stated that housing authorities need not comply with its property management fee schedules until 2008 at the earliest, and not until 2009 for housing authorities with fiscal year ends of March 31.

The rule states that PHAs must comply with asset management, comprising project-based management in 2011. Agencies are not required to comply with project-based management in 2007 under the rule. Project-based management is defined in

section 990.275 of the rule. It says, “Under PBM, these property management services are arranged, coordinated, or overseen by management personnel who have been assigned responsibility for the day-to-day operations of that property and who are charged with direct oversight of operations of that property.”

In other words, housing authorities do not need to implement this management system until 2011, according to the rule. This is the management system on which its property management fee schedules are based, though. In other words, the properties in the FHA universe operate in this manner, and they do so using the management fees that serve as the basis of HUD’s property management fee schedule. It is clearly not fair, then, to require a housing authority to operate under a fee schedule based on that type of management, when the rule does not require housing authorities to adopt that type of management until 2011. A housing authority, during the years between 2008 and 2011, may not be able to live within that property management fee schedule, because it has not completely adopted the multifamily property management model. This housing authority’s organization would be completely acceptable under the rule and completely understandable given the complexity of converting to project-based management.

Therefore, it is clear that HUD’s property management fee schedule should not apply to housing authorities before the year 2011. The key word in developing a property management fee is “reasonable.” Since housing authorities are not required to adopt project management until 2011, it is not “reasonable” to make them adopt a property management fee based on that model prior to 2011.

It is clearly not fair to require a housing authority to operate under a fee schedule based on that type of management, when the rule does not require housing authorities to adopt that type of management until 2011.

PHADA believes, therefore, that HUD should not implement a property management fee schedule based on the FHA properties prior to 2011. It believes that applying such a fee schedule in 2011 would meet the rule’s requirement that PHAs be in compliance with project-based management by that year.

This decision would be consistent with the Department’s own actions, since it has shown that it does not believe it is reasonable that PHAs be in compliance with its fee schedule in 2007.

The multifamily program has a method of handling a situation such as this that HUD could adopt. Special fees are permitted in the multifamily program. Section 3.23 of the Management Agent handbook explains when a special fee is warranted:

- “(1) The agent did not cause the problem that the fee is designed to address.
- (2) The fee is tied to the correction of specific problems or the accomplishment of specific tasks.

- (3) The fee is structured so that it is payable only if the agent completes the required actions or obtains the required results.
- (4) The fee does not include services that are covered by residential, commercial, or miscellaneous management fees, or by other sources of compensation.
- (5) The fee is reasonably related to the time, effort and expertise required of the agent.
- (6) The fee is paid only for a limited period of time. The length of this period should be no longer than the time required to resolve a specific problem or complete a certain task.”

These six conditions aptly describe the situation housing authorities find themselves in in regard to their conversion to project-based management. They did not cause the fact that they currently manage their properties on an authority-wide model. They will be correcting this situation during the period between 2007 and 2011 as permitted in the rule. The fee is paid for a limited period of time—through 2011.

HUD, therefore, could comply with the rule and the norms of the multifamily program by permitting housing authorities to receive a special fee through 2011 to cover the costs it incurs as it converts to property management. These costs would include central office costs the authority pays as it makes the transition to “property management services... arranged, coordinated, or overseen by management personnel who have been assigned responsibility for the day-to-day operations of that property and who are charged with direct oversight of operations of that property.”

E. HUD must inflate fees annually

The second additional issue PHADA wishes to raise in regard to property management fees is the question of when they should be updated. The supplement only calls for them to be updated “regularly” with no more specific time frame. This position is untenable for housing authorities.

Currently, HUD has proposed property management fee schedules based on 2004 data that will at least be used to evaluate stop-loss agencies during the period from April–June 2007. In other words, housing authorities will be expected to operate with a property management fee in 2007 that was available to private owners in the FHA universe in 2004. That decision clearly seems unfair.

Housing authorities will be expected to operate with a property management fee in 2007 that was available to private owners in the FHA universe in 2004. That decision clearly seems unfair.

In addition, multifamily properties receive their property management fee as a percentage of revenue and the Management Agent Handbook specifically states that this method has been adopted in order to “help offset increases in the agent’s cost due to inflation” (p. 3-2). Thus multifamily management agents are entitled to an increase in the property management fee each year based on an increase in revenue.

Finally, the Management Agent Handbook says that when calculated ranges must use yields in effect at the time the ranges are established (p. 3-26) and that “ranges must be reviewed and updated every two years... If the ranges are not reviewed and published by an Area Office at the two year interval, they will automatically be adjusted by the Services Consumer Price Index (CPI) for the total of the 2 years” (p. 3-24).

Therefore, the multifamily program handles the issue of updating property management fees much differently than HUD has proposed for public housing. All existing properties in the multifamily program, which are the vast majority, are entitled to an annual increase based on their revenue. New properties entering the program which must have their fees evaluated are entitled to have them based on data at most two years old, and very likely much fresher. In an extreme situation, if an FHA property entering the program in 2004 had its fee based on two-year-old data, it would mean that when this amount was used as a basis for public housing fees in 2007, it would already be five years old.

Since the vast majority of FHA property owners are entitled to increased property management fees annually, housing authorities ought to be afforded that same privilege.

Public housing authorities, then, should not be forced to comply with fees earned by FHA owners three or more years earlier. Since the vast majority of FHA property owners are entitled to increased property management fees annually, housing authorities ought to be afforded that same privilege. PHADA believes that HUD should take the simple step of updating the data every two years and then inflating it to take into account the inflation that has occurred between the time period the data represented and the time period for which it was going to be used by an appropriate component of the consumer price index (CPI). This step would mirror the rule’s treatment of the PELs and utilities, each of which are adjusted annually by inflation.

Thus, the 2004 data should be updated as soon as 2006 data is available and while the 2004 data is used, it should be inflated to reflect the time period for which it will be employed. For example, the 2004 data used in HUD’s property management fee schedule should be inflated by three years to be used during the April–June 2007 time period.

This method corresponds with the practice in multifamily. All of the properties on which the 2004 data is based would have been able to increase their management fee three times by 2007 based on their increases in revenue. These increases may well have exceeded the CPI during the same time period. Since the properties used to create the 2004 base will all have had the chance to inflate their fees by the time April–May 2007 has arrived, public housing authorities should have the same opportunity.

If HUD wanted to make the two programs extremely similar, it could require new public housing properties entering the program to use the HUD published data, up-

dated every two years, while utilizing the method described above for all existing housing authority properties, as is done in multifamily.

F. Property management fees should be provided for “limited vacancy” units

The third issue in regard to property management fees concerns whether or not PHAs should receive a management fee for “limited vacancy” units. These are the 3 percent of units that HUD acknowledges are routine vacancies and as such are eligible for operating subsidy.

HUD’s position is that since multifamily properties do not receive a property management fee for vacant units, public housing properties should not receive a fee for these “limited vacancy” units. HUD has already bent this position, though, for it has determined that housing authorities are entitled to property management for other vacant categories, such as units undergoing modernization. Therefore, simply saying that vacant units in multifamily do not get a property management fee is not a sufficient explanation of HUD’s action.

The operating fund rule has the concept of eligible unit months. These are units for which a housing authority receives an operating subsidy. These units include all occupied units, units that are vacant for legitimate reasons, such as being under modernization, and the “limited vacancy” units that are also vacant legitimately, because they represent routine turnover. HUD has determined that all of these units cost money to operate and therefore are entitled to operating subsidy.

It seems to PHADA that this same logic should apply to the property management fees. If a unit costs money to operate and is entitled to operating subsidy, it also costs money to manage and should be entitled to a property management fee. That appears to be the logic the Department has applied in regard to vacant units, such as those under modernization.

Under the operating fund rule the “limited vacancy” units are ones from which a housing authority receives subsidy, “receives” rent, and must perform a considerable amount of work. Since these units are thus in every way comparable to an occupied unit, providing both subsidy and “rent” to the authority, the authority should also receive a property management fee from them.

There can be no doubt that routine turnover units cost a considerable amount of money to operate and also cost money to the property management company. Ensuring that routine turnovers are returned to occupancy quickly and satisfactorily is one of the most important oversight responsibilities of the management agent. It should certainly be paid for this responsibility.

PHADA points out too, that in multifamily, owners are paid a property management fee for every unit for which they receive revenue. Their fee, in fact, is a percent-

age of revenue. HUD would therefore be consistent with this multifamily norm by providing a property management fee for “limited vacancy” units.

One further consideration is that HUD considers that as EUMs, the authority collects rent from the “limited vacancy” units. This rent, which of course is not really collected, is subtracted from operating subsidy eligibility.

Thus, under the operating fund rule the “limited vacancy” units are ones from which a housing authority receives subsidy, “receives” rent, and must perform a considerable amount of work. Since these units are thus in every way comparable to an occupied unit, providing both subsidy and “rent” to the authority, the authority should also receive a property management fee from them. There is no difference in HUD’s treatment between them and occupied units. As mentioned, in the multifamily program, every unit for which an owner receives revenue also pays a property management fee.

Therefore for the following four reasons, PHADA believes housing authorities should receive a property management fee for the “limited vacancies.” First, HUD provides the fee for other vacant units, such as those undergoing modernization. Second, these units provide subsidy and rent to the authority and are therefore comparable to an occupied unit. Thirdly, the property management company has to perform a great deal of work to manage these units. Fourthly, multifamily practice bases property management fees on revenue.

If HUD were to persist in refusing to provide a property management fee for “limited vacancy” units, it would bring into question even further its policy of considering that these units generate income through rent. If housing authorities are not entitled to a property management fee because these units are “vacant,” how can HUD assume that the authority will collect rent from such a “vacant” unit? The two policies contradict one another. Either the unit is “vacant” or it is not for policy purposes.

G. Proposed changes to HUD’s methodology

In sum, if HUD intends to use the FHA database as a means of developing one method of setting a “reasonable” property management fee, it needs to take the following additional steps.

1. It must inflate the data to reflect the time period for which the data will be used.
2. It must use all the properties in the FHA database, not just a selected portion.
3. It must adjust for the differences between the characteristics of the FHA database and the characteristics of public housing. This adjustment could be done in the form of add-ons. A sound, transparent method must be developed to decide which add-ons are eligible and how much they are worth.
4. As directed by OMB, HUD must take into account the effect of the 24 regulatory and operating environment differences between public housing and the FHA database properties.

H. Other reasonable fees

1. Using mixed-finance method based on 6 percent of imputed tax-credit rent.
PHADA believes HUD should also include other “reasonable” methods for determin-

ing property management fees. One is the method already in use by the Department in the mixed-finance program—taking 6 percent of the imputed tax credit rent.

PHADA is unclear about the effect of this notice on the continued use of this property management fee in the mixed finance program. Using a percentage of the imputed tax credit rent is not included as an option for housing authorities on page 33 of the supplement to the Financial Management Handbook. On the other hand, on page 37, it says in regard to HUD’s “The Cost Control and Safe Harbor Standards for Rental Mixed-Finance Development, Revised April 9, 2003,” “This notice supersedes that requirement (having to report actual documented costs for administration), but does not alter or eliminate any other criteria for the evaluation of mixed-finance development as outlined in that document.”

Since no other criterion in that document is altered, it appears that public housing units in mixed-finance developments can continue to use the formula of 6 percent of the imputed tax-credit rent as a safe harbor for property management fees. If PHADA’s understanding is correct, it believes HUD must also determine that this standard is “reasonable” for all public housing units. Mixed-finance units are brand-new and generally apply stricter screening standards than other public housing, meaning that the residents have a history of being especially responsible. As brand-new property with especially responsible residents, these mixed-finance units are easier to manage than other public housing units. Therefore, if this fee formula is “reasonable” for these easy-to-manage units, it certainly could not be considered unreasonable for public housing units that are more difficult to manage.

2. Use FHA database to base fee on percentage of property’s operating cost. A second proposal, made by PHADA to the Department nine months ago, is to base the property management fee for public housing on the percentage of operating cost used by FHA properties.

In the multifamily program, the management fee is a percentage of project income. For instance, in the Management Agent Handbook, 4381.5, rev. 2, it reads (p. 3.2) “Fees derived from project income *must* be quoted and calculated as a *percentage* of the amount collected by the agent. Multiplying the fee percentage by the income collected gives the actual amount of fee paid to the agent.”

Since the operating costs are similar, using the property management fee’s percentage of multifamily operating costs would appear to be a model of providing the same fee for the same work for each program.

Thus, in multifamily, the fee must be a percentage of revenue, and since it is a percentage it accounts for inflationary increases. Public housing’s revenue, though, is capped at a lower level than multifamily’s and therefore, it would not be fair simply to apply the percentages of revenue used in multifamily to the public housing program.

Unlike revenue, though, the operating costs of the properties in the FHA database and public housing are similar. In fact, public housing’s operating cost is bench-

marked on that of the multifamily program. Therefore, since the operating costs are similar, using the property management fee's percentage of multifamily operating costs would appear to be a model of providing the same fee for the same work for each program.

The revenue that a multifamily property collects goes to one of the following expenses: operating cost, mortgage payment, taxes, replacement reserve or profit. Other than operating cost, the property management fee appears to have little or nothing to do with the other expenses. The property management company probably has few or no responsibilities concerning paying the taxes and the mortgage, placing money in the reserve or providing the owner with his or her profit. Thus, in determining a property management fee, this revenue can essentially be discounted. The only part of the revenue which really affects the property management fee is the amount that covers the operating cost of the property. Thus, the property management fee's percentage of operating cost reflects the real relationship between the work of the property management agent and the property's revenue.

Therefore, it appears as if using the property management fee percentage of operating costs employed in the multifamily program would be a "reasonable" method of determining the property management fee for public housing. HUD could use the 80th percentile of the multifamily property management fees divided by the average operating cost per field office as a method of deriving the actual percentage.

It is clear that there is a connection between the operating cost of a property and the cost of the property management fee. The Management Agent Handbook states that "agents managing projects with long-term project characteristics/conditions that require additional management effort beyond the activities covered by the residential management fee" are entitled to add-on fees. These add-ons correspond to many of the characteristics of public housing, including whether or not the property is assisted, properties with a high percentage of units with three or more bedrooms, properties in neighborhoods with adverse conditions, properties in high cost areas and non-profit properties. Many of these characteristics are the actual coefficients used by the Harvard cost study. Thus, the same factors which drive the operating cost of property also drive the cost of the property management fee. It is, therefore, logical to base the fee as a percentage of the cost.

PHADA has criticized HUD's fee schedule in these comments for a variety of reasons, including a) the properties in the FHA database are different; b) public housing will not receive the add-ons available to multifamily; c) the 2004 data is not inflated; and d) it does not take into account the 24 regulatory and operating differences between public housing and the multifamily program.

Basing the management fee as a percentage of the operating cost would take care of a, b and c. Since the operating cost in public housing is based on the characteristics of the property, the differences between public housing and the FHA properties will be reflected in public housing's higher operating cost. Applying the same percentage to a higher operating cost will provide a higher management fee. Thus, public housing properties will receive a higher management fee than the FHA properties based on the "long term characteristics" of the property which require "additional management effort." Since the fee is based on a percentage, the management fee will be inflated automatically each year as the operating cost increases. Although HUD might have a

predetermined prejudice that public housing should not receive a higher fee in absolute terms than the multifamily properties, the connection between the cost of the property and the management fee indicates that this higher fee is merited.

Although HUD might have a predetermined prejudice that public housing should not receive a higher fee in absolute terms than the multifamily properties, the connection between the cost of the property and the management fee indicates that this higher fee is merited.

According to the Harvard cost study, in 2000 the average cost of an FHA property was \$242 PUM, while the average benchmarked cost of a public housing property was \$297 PUM. Thus, on average, because of differing property characteristics, public housing costs were 23 percent higher than FHA ones, signifying that the property management fee also should be 23 percent higher. Inflating the 2004 numbers to 2007 would add another 6–10 percent. Therefore, it appears that this method, which is modeled after the multifamily program, would increase property management fees by approximately 30 percent.

The Harvard cost study never provided any additional funding for the 24 regulatory and operating differences between public housing and the FHA properties. As a result, this extra work is not reflected in public housing's operating cost. Therefore, it must still be reflected as an add-on to the property management fee. This amount remains to be determined. As mentioned, OMB Circular A-87 states that "reasonable costs" must consider "the restraints of requirements imposed by... Federal... regulations." Including an add-on, then, for the operating and regulatory environment imposed by federal regulations to the property management fee determined by the percentage of operating cost, is a method which provides a "reasonable" property management fee and should be put into place by the Department.

PHADA believes that these comments show that HUD is not prepared to implement its property management fee schedules as it has indicated that it will do for stop-loss agencies as of April 2007. There is still a considerable amount of work to be done before the Department can arrive at a "reasonable" amount. Throughout this process, PHADA has attempted to be constructive, both in highlighting the flaws in HUD's proposals as well as offering alternatives it believes resolve areas of dispute.

PHADA commends the Department for having already responded to several of PHADA's critiques. It agreed that the multifamily fee schedules should not be considered the only "reasonable" option; it divided the FHA management fees by occupied units rather than all of them to arrive at an accurate average as PHADA illustrated should be done; and it has tried to show some flexibility by offering a third subjective fee option. Each of these decisions has improved the Department's guidance. PHADA urges the Department to consider these comments just as carefully as it considered the above-mentioned areas, because it continues to believe that by working in cooperation with the housing authorities and carefully reviewing their points of view, the De-

partment can improve these guidelines further to the point where they achieve its goals in a manner that is fair to all the parties. There is time to complete this work, because property management is not required until 2011.

Section Two: Bookkeeping Fees

A. HUD's \$3.50 PUM for accounting is based on unreliable data

HUD has proposed a bookkeeping fee of \$7.50 PUM. This amount reflects a \$3.50 PUM bookkeeping fee average in a portion of the FHA database, as well as “higher centralized information technology and human resource costs present in public housing” (p. 35 supplement to the Financial Management Handbook). Housing authorities receive a \$2 PUM add-on for information technology (IT) that is part of the \$7.50. That leaves \$5.50 PUM for the bookkeeping and human resources expenses to be paid by this fee.

PHADA has grave concerns about the method HUD has used to develop the \$3.50 PUM average and has concluded that the Department's methodology is hastily conceived, unreliable and unscientific. PHADA has informed the Department of the flaws in its method, but in spite of the overwhelming evidence it has presented, the Department has persisted in publishing this fee amount. PHADA believes HUD must change the manner in which it has developed a bookkeeping fee before it proceeds with the implementation of asset management.

PHADA has grave concerns about the method HUD has used to develop the \$3.50 PUM average and has concluded that the Department's methodology is hastily conceived, unreliable and unscientific.

In multifamily, bookkeeping expenses are a front-line cost, not a central office one. For instance, on pages 3–6 of the Management Agent Handbook, it states that “The cost of bookkeeping services for a project performed as part of a centralized bookkeeping system are treated as a project cost....” PHADA supports the idea of a simple fee for bookkeeping costs, but believes as well that a housing authority should have the option of expensing its bookkeeping costs as a fee for service or allocation, as other front-line costs are handled, if it chooses.

Since bookkeeping expenses are a front-line cost, it is not clear that all these expenses are placed in line 6351 that HUD is using for developing its average. In fact, during the February 13–14 meetings with the Department, Peter Bell, formerly HUD/REAC Director of FASS-Multifamily, acknowledged that using the average bookkeeping fee as a benchmark was only as good as the data which was input, which was not necessarily that good. He mentioned that accounting costs might be recorded in line 6350, audit expense.

As a result, PHADA asked the Department to send it information on the average bookkeeping cost for each field office. HUD's response confirmed PHADA's concerns, because it showed that thousands of FHA properties recorded no bookkeeping expenses in 6351. Since the bookkeeping expenses for these properties must be placed somewhere else on the financial statements, HUD's use of line #6351 clearly does not represent average bookkeeping costs for FHA properties. As a result, PHADA does

not believe it can be used to develop a benchmark for public housing in the manner HUD has adopted.

HUD’s response showed that thousands of FHA properties recorded no bookkeeping expenses in line #6351. Since the bookkeeping expenses for these properties must be placed somewhere else on the financial statements, HUD’s use of line #6351 clearly does not represent average bookkeeping costs for FHA properties.

HUD’s information shows that there are numerous field offices throughout the United States where most of the properties report no bookkeeping expenses at all. Therefore the FHA database is too unreliable and inconsistent to be used as a benchmark for public housing properties. The following table shows the 26 field offices in which the median bookkeeping expense falls significantly below the national average of \$3.43. The table reveals how widespread the faulty reporting is spread throughout the country.

Field office	Unlimited dividend		Non-profit	
	Number of properties	Median cost (PUM) #6351	Number of properties	Median cost (PUM) #6351
Anchorage	3	\$0.00		
Baltimore	72	\$1.54		
Buffalo	82	\$0.00		
Charleston			57	\$0.00
Columbia	124	\$1.99	170	\$0.00
Detroit	54	\$0.00		
Fort Worth	146	\$0.65		
Grand Rapids	32	\$0.00		
Greensboro	239	\$0.62		
Honolulu	4	\$0.35	42	\$0.29
Houston	98	\$1.95		
Las Vegas	29	\$0.00		
Manchester	28	\$0.00	125	\$0.00
Minneapolis	121	\$0.00		
New Orleans	29	\$0.72		
Philadelphia			216	\$1.03
Portland	47	\$0.25		
Providence			54	\$1.49
Richmond	139	\$1.55	152	\$0.00
Sacramento	35	\$0.24		
San Antonio	124	\$0.98		
San Diego	41	\$0.00	52	\$1.53
Seattle	68	\$1.72		
Tampa	24	\$1.64	86	\$0.00
Tulsa			25	\$1.30
Washington, D.C.	105	\$0.53	117	\$0.52

HUD simply cannot claim that \$3.43 PUM is the median bookkeeping fee in the FHA database when thousands of properties do not even report a bookkeeping expense in line 6351. With such a flawed database, HUD’s proposed bookkeeping fee does not meet the rule’s standard of being “reasonable,” and it must be reconsidered.

Byrne has stated that in field offices where FHA properties do not report bookkeeping fees, it is because the bookkeeping work is done by the property management company and included in the property management fee. On the face of it, this argument does not make sense, since property management companies are profit-motivated entities, and they would be unlikely to absorb a cost in their property management fee which is an eligible front-line cost and can be expensed as such.

Furthermore, the data HUD has provided do not support this contention. The following table compares the combined property management and bookkeeping fees at field offices where the unlimited dividend median falls below \$2 PUM with the non-profit properties in those same field offices where the median exceeds \$2 PUM. According to Byrne, since he contends that the bookkeeping costs are reflected in the property management fee, the combined amount for the unlimited dividend properties should reflect the average relationship between fee costs of the unlimited dividend properties in general and the fee costs of the non-profit properties.

Field office	Median unlimited dividend management fees	Median unlimited dividend bookkeeping fees	Total	Median non-profit management fees	Median non-profit bookkeeping fees	Total
Anchorage	\$50.81	\$0.00	\$50.81	\$47.52	\$8.09	\$55.61
Baltimore	\$37.52	\$1.54	\$39.06	\$39.55	\$2.14	\$41.69
Buffalo	\$40.60	\$0.00	\$40.60	\$42.88	\$3.58	\$46.46
Detroit	\$35.72	\$0.00	\$35.72	\$37.27	\$2.16	\$39.43
Fort Worth	\$28.84	\$0.65	\$29.49	\$36.35	\$5.72	\$42.07
Grand Rapids	\$36.74	\$0.00	\$36.74	\$37.42	\$3.21	\$40.63
Greensboro	\$37.00	\$0.62	\$37.62	\$37.54	\$4.23	\$41.77
Houston	\$27.39	\$1.95	\$29.34	\$35.28	\$5.59	\$40.87
Las Vegas	\$33.34	\$0.00	\$33.34	\$36.01	\$4.01	\$40.02
Milwaukee	\$38.24	\$0.52	\$38.76	\$38.48	\$4.81	\$42.29
Minneapolis	\$40.59	\$0.00	\$40.59	\$46.42	\$3.90	\$50.32
New Orleans	\$33.98	\$0.72	\$34.70	\$36.35	\$2.50	\$38.85
Newark	\$60.93	\$0.38	\$61.31	\$46.31	\$3.74	\$50.05
Phoenix	\$26.12	\$0.63	\$26.75	\$36.55	\$5.35	\$41.90
Portland	\$29.38	\$0.25	\$29.63	\$37.39	\$5.35	\$42.74
Sacramento	\$34.56	\$0.24	\$34.80	\$45.00	\$8.02	\$53.02
San Antonio	\$29.38	\$0.98	\$30.36	\$35.32	\$3.61	\$38.93
Seattle	\$31.95	\$1.72	\$33.67	\$37.13	\$4.28	\$41.44
Average	\$36.28	\$0.57	\$36.85	\$39.32	\$4.46	\$43.78
Percent difference						18.81%

According to HUD’s data, median fee costs are 10.5 percent higher for non-profit properties than for unlimited dividend ones. However, comparing fee costs where the unlimited properties do not report an adequate bookkeeping fee to those of non-profit properties which do report a bookkeeping fee of some measurable amount, shows that in these cases the non-profit fees are 18.82 percent higher than the unlim-

ited dividend ones. Thus, HUD's data does not substantiate the fact that in the cases where unlimited dividend properties do not record an adequate bookkeeping fee, they are putting the cost into the property management fee. As a result, the bookkeeping fee is not getting recorded in either fee category for these thousands of properties, invalidating the use of this database as a measurement of the cost of bookkeeping.

Another way of looking at this table shows that the average property management fee for these unlimited dividend properties is \$36.28, while nationally the median is \$37.38. If the bookkeeping fees were being absorbed in the property management fee for these properties, the average should be significantly higher than the national median, not lower. Non-profit averages, on the other hand, of a combined property management and bookkeeping fee, are almost exactly the same as the national median.

B. HUD should not use the median in the FHA database as a cap for public housing

A second issue is HUD's decision to use the median amount in the FHA database as the basis for public housing's bookkeeping fee. When multifamily develops the property management fee for its program, it does not take the median amount of the property management fees in its area. Instead it multiplies the median by 120 percent. This is done in recognition that the median is simply not a workable amount for many agencies. By definition half of the agencies in the database spend more than the median, so it is clearly not adequate even for the base properties being used to develop a benchmark.

By definition half of the agencies in the database spend more than the median, so it is clearly not adequate even for the base properties being used to develop a benchmark.

Similarly, HUD should not use the median to develop a bookkeeping fee. In essence, HUD is taking the median for one group and making it the cap for another. It is blatantly unfair to say public housing authorities cannot spend more than \$3.50 PUM on bookkeeping expenses when far more than half of the FHA properties spend more than this amount.

Byrne has said that taking a median is what was done in the Harvard cost study. That statement, though, is a misunderstanding of the method used to develop PELs. The purpose of the regression analysis used in the study was to eliminate unexplained differences between properties. If it had been able to explain every variable, then every property would have the exact amount needed for its operation. The PEL is not a median, therefore, but the closest approximation to this exact amount possible based on the property's individual characteristics. To the extent that there are costs unexplained by the regression analysis (and there were a considerable amount) these costs are likely to be random, since they were not explained by any identifiable variable. Since they are random, it is plausible that one year they may cause costs to increase,

while in another they may cause costs to decrease. Over time, these random variables may wash each other out.

The median, though, makes no pretense to identifying the exact amount needed for each particular property. It is simply one number applied to every property in the nation, regardless of its location or particular circumstances.

The following table shows the 80th percentile amount for non-profit properties at a number of field offices.

Field office	Number of non-profit properties	Bookkeeping fee at the 80 th percentile
Anchorage	26	\$25.37
Boston	257	\$13.62
Caribbean	82	\$11.59
Cleveland	180	\$11.47
Columbus	243	\$10.09
Denver	233	\$12.17
Honolulu	42	\$17.22
Kansas City	156	\$11.58
Los Angeles	341	\$10.87
Manchester	125	\$13.60
Milwaukee	232	\$13.45
New York	315	\$11.38
Portland	138	\$13.68
Sacramento	79	\$10.51

This table demonstrates the amount of money many properties in the FHA universe need to conduct their accounting function, showing how far off HUD’s median for public housing can be. PHADA cannot say too strongly that it is not fair to provide housing authorities with \$3.50 PUM when HUD allows private sector properties to spend 8 and possibly 10 times that amount. The amount provided public housing authorities is simply not adequate to do the work needed, and it will harm the program.

PHADA cannot say too strongly that it is not fair to provide housing authorities with \$3.50 PUM when HUD allows private sector properties to spend 8 and possibly 10 times that amount.

It is quite simple to understand this point. If a 2,000-unit public housing authority had \$3.50 PUM to perform its accounting function, it would be provided \$84,000 per year. Since it will not receive funding for “limited vacancy” units, it would receive \$81,480 if it were 97 percent occupied. (PHADA incorporates its comments on the payment of fees for “limited vacancy” units that it made in the section on property management fees and believes that bookkeeping fees should also be provided for “limited vacancy” units.)

If benefits take up 30 percent of compensation for a housing authority employee, this \$81,480 would be able to provide \$57,036 in salary costs. In some expensive mar-

kets, such as New York, California or Boston, this amount might not even be enough to attract one full-time financial professional to handle this authority's accounting function. Assigning all the revenue to salaries and benefits also means this authority could not purchase any equipment, replenish any supplies, employ any consultants, hire any temporary employees, receive any training or update any software.

It must be clear that a bookkeeping fee which neither provides enough funding for one full-time employee nor allows the purchase of any supplies or support would not be enough to pay for all of the bookkeeping and accounting responsibilities at a 2,000-unit public housing authority. PHADA hopes that this simple, common sense example is enough to rest its case that HUD's method of developing a bookkeeping fee is irredeemably flawed. If not, actual cost evidence such as the \$21.50 PUM reported by the St. Paul, Minnesota HA supports PHADA's point by the experience of a well-run housing authority.

It must be clear that a bookkeeping fee which neither provides enough funding for one full-time employee nor allows the purchase of any supplies or support would not be enough to pay for all of the bookkeeping and accounting responsibilities at a 2,000-unit public housing authority.

PHADA has made several additional comments on HUD's bookkeeping fee as well. It has pointed out that one national number does not adequately take into account geographic and market differences. After all, HUD calculated property management fees by field office. Its own data shows median bookkeeping fees ranging from \$0.00 PUM in Columbia, S.C. to \$8.50 in the Caribbean field office. If its data is reliable enough to use, it should inform the housing authorities in the Columbia, S.C. field office that their bookkeeping fee is \$0.00 PUM based on comparable FHA properties.

Similarly, housing authorities have more financial work to do than a FHA property. They will continue to have to report authority-wide financial statements, and HUD has not been clear as to whether authority-wide budgets will also be necessary. Since housing authority properties are not genuinely stand-alone units developed to be self-supporting, PHAs will have to transfer money back and forth between them. None of this additional work is supported by HUD's methodology based on FHA costs.

C. Developing an accurate amount for the cost of accounting

HUD needs to go back to the drawing board in terms of bookkeeping costs for public housing authorities. There is too much empiric evidence showing that the FHA data is simply too unreliable to be used. It is also evident that the use of the median will shortchange housing authorities to the point that they cannot fulfill their responsibilities.

PHADA believes there is a very simple solution to how HUD should develop bookkeeping fees, and it is one it has offered to the Department before. Despite whatever some HUD officials might think about public housing central office costs, it appears unlikely that they could make a case that public housing's accounting and bookkeeping costs are unusually high. Work is likely to be performed professionally and cost-effectively and the costs are reliable enough to be used as a benchmark. Therefore, PHADA believes that simply looking directly at what housing authorities spend on their bookkeeping function is the best method of developing a bookkeeping fee.

HUD could easily access this information from a scientifically valid number of agencies. It could examine any it considered anomalies more carefully through selected case studies. In a relatively short amount of time and at little expense, the Department could have a usable estimate of the amount of money it takes for housing authorities to perform their accounting duties. Although it would not be benchmarked on the private sector, PHADA believes, as mentioned, that public housing accounting expenses will not be found to be bloated, padded or otherwise unnecessarily high. HUD should remember, after all, that the Harvard cost study found that public housing was operating its properties more efficiently than those in the FHA database and overall was entitled to additional funding.

PHADA urges the Department to take this straightforward route and develop a bookkeeping fee that will be genuinely satisfactory for the work it requires of housing authorities.

D. Information technology costs

The \$7.50 bookkeeping fee is also supposed to cover “the higher centralized information technology and human resource costs present in public housing.” As mentioned, at least \$2 PUM of the \$4 difference between the \$3.50 accounting fee and the \$7.50 total is attributable to IT which is given a \$2 PUM add-on.

In the multifamily world, it appears as if virtually all IT expenses are front line. For instance, Figure 6-2 in the Management Agent Handbook describes the following under a “cost paid from project account”: “Includes prorated costs on a per-unit basis for centralized accounting systems, including hardware, software, and technical support. Agent can be reimbursed for the prorated cost to the project of personnel providing property specific accounting and computer services.”

Thus, in multifamily, all the computer costs are front-line. The \$2 PUM, then, provided in the \$7.50 PUM bookkeeping fee is not only to pay for the “higher centralized... costs” but to pay for the entire IT function.

As the Harvard cost study made clear, though, this \$2 PUM neither pays for the cost of IT in the multifamily world nor for the difference between the cost of IT in the FHA universe and the cost in public housing. According to the study, “GSD’s surveys would lead one to conclude that private operators might incur somewhat less than \$1.50–\$3.00 PUM in on-going central IT costs whereas PHAs frequently spend upwards of \$8–\$10 PUM or higher.” Thus, even in 2000, \$2 PUM would not have paid for IT costs in multifamily, much less the difference between multifamily and public housing. PHADA is concerned as well that HUD’s data on computer costs may be as unreliable as its data on bookkeeping fees.

The cost study made an attempt to analyze why such a large difference should exist between the two programs. In essence, it attributed it to centralized functions, such as procurement, warehouse and maintenance. PHADA does not believe, though, that its analysis fully resolved the question of why this large a difference in costs exists between public housing and the FHA properties. By simply providing the \$2 PUM, however, HUD is clearly funding IT inadequately, and considering its finding that PHAs spend \$8–\$10 PUM the Department is placing public housing’s IT component at serious risk.

Again, a 2,000-unit housing authority at 97 percent occupancy would have \$46,560 for its IT costs at a \$2 PUM amount. With 30 percent applied to benefits, the salary for this authority if it wanted to hire one IT professional would be \$32,592. This amount seems insufficient for all of the IT work necessary at an agency of this size, especially as it is also supposed to cover hardware and software.

According to the Harvard cost study, PHAs frequently spend upwards of \$8–\$10 PUM or higher in ongoing central IT costs.

PHADA believes a more thorough examination of this issue needs to be conducted. The base amount is not enough, and the difference between the programs is too great to dismiss as unnecessary without a more systematic evaluation of its causes. HUD must conduct a more thorough study of the reasons for PHA information technology costs and whether or not they will change as agencies transition to asset management. Since conversion need not be completed until 2011, HUD has more than enough time to conduct this study and can hold agencies harmless on their IT costs until it is completed, either through a special fee, an allocation method or a fee for service.

E. Human resources costs

HUD has provided no information on how it calculated the approximately \$2 PUM that is provided for human resource costs to pay for “higher centralization.” PHADA appreciates the Department providing additional money for human resources, because it frequently explained to the Department many of the complications which exist for housing authorities which do not exist in the private sector.

In particular, many housing authorities have to deal with the issue of operating in a unionized environment. The Harvard cost study found that public housing was unionized to a far greater extent than the properties in the FHA database.

No one can question that personnel and human resource issues are far more complex and time-consuming in a unionized environment. Housing authorities with unions can undertake virtually no personnel matter without consulting the unions. Disciplinary action is a highly structured process with appeals reaching up to state appointed labor boards at which housing authorities need to be represented by attorneys. These boards make decisions which are then binding on housing authorities.

PHADA cannot identify the exact cost of this extra effort. Its comment to the Department, though, is that HUD has not identified that cost either. It has provided no

description of the methodology it used to determine what human resource costs are in public housing and how they differ from the FHA properties. That lack of transparency and method is simply inappropriate in determining fees that are to be paid to housing authorities to conduct the business of housing the nation's low-income population.

As with IT, PHADA requests that a study be conducted on the effect of operating in a unionized and/or public sector environment to determine more systematically how much should be provided in the form of a fee for human resource costs. Again, as property management need not be achieved until 2011, five years from now, the Department has adequate time and resources to conduct such a study.

To sum up, PHADA does not believe HUD has a reliable method of benchmarking the costs of public housing accounting on the data from FHA properties. It also does not believe using the median is an acceptable method, and it reminds the Department that this is not the method used either in developing property management fees or PELs. PHADA believes that the Department should examine what housing authorities actually spend on their accounting function and develop a bookkeeping fee on that basis.

Section Three: Asset Management Fees

A. Asset management responsibilities

One of the components of the conversion to asset management is the provision of an asset management fee. Since owners take their asset management fee out of the profit, there is no direct line item that HUD can point to and say that is what the private sector pays as an asset management fee. Nevertheless, there are several models which are identified by the Harvard cost study as possible benchmarks for the asset management fee, and they all indicate that the \$10 PUM identified in the supplement to the Financial Management Handbook is neither comparable to the amount others earn nor sufficient to cover these costs.

The first thing that needs to be done to determine how much asset management costs is to identify what its responsibilities are. There are a number of sources that can be used. For instance, the Harvard cost study, in its appendix C, described the tasks of asset management. In addition, it wrote that “the term asset management is frequently used to refer to the contract administration of project-based housing assistance contracts....” Thus, the responsibilities of the contract administrators, found in Handbook 4350.5, Subsidy Contract Administration and Monitoring, can be used as a second example of asset management duties. Another source is the operating fund rule itself, which describes asset management in section 990.270. Finally, Notice 2006-14 lists a number of factors which are associated with just one of asset management’s jobs—risk management responsibilities related to regulatory compliance.

The table shows that there are essentially three responsibilities in asset management: the performance of the property; making decisions beyond the authority of the property manager; and planning and implementing long-term strategy.

The table on the following page compares the asset management duties from these four sources. It shows that there are essentially three elements to asset management. The first is a responsibility for the performance of the property and its compliance with regulations. The second is a responsibility to take decisions beyond the authority of the property manager, such as selecting the property manager, approving budget amendments, deciding legal problems, authorizing large-scale capital improvements as well as accepting the audit. The third is a responsibility to plan and implement a long-term strategy for the property.

In regard to the first responsibility, the Harvard cost study says that the asset manager must monitor the performance of the property manager, approve the operating budget, and approve rents and operating policies. Similarly the final rule states that the asset manager is responsible for the property management performance, including the physical stock and the finances. The contract administrator has similar responsibilities, having to inspect 25 percent of the units, review monthly accounting reports and check such performance indicators as occupancy, screening and rent collection.

	Harvard cost study	Final rule	Notice 2006-14	Contract Administrators Handbook 4350.5 Change-4
1.	Approving operating budgets			Review operating budget
2.	Monitoring performance of management agent, approving budget deviations	Property management performance; review of financial information and physical stock; risk management pertaining to regulatory compliance	Responsible for being in troubled status; FHEO compliance; energy audits; IG findings; compliance with the ACOP; RIM review of rent calculations; 50058 reporting; capital fund obligations	Ensure management agent has adequate system of recordkeeping; review staffing patterns; vacancy rate; screening procedures; utility allowances; inspect 25 percent of units and all vacancies; review monthly accounting reports
3.	Selecting management agents			
4.	Deciding legal actions by or against owner			
5.	Interacting with lenders, regulatory bodies on major issues which cannot be handled by property management agent			
6.	Approving rents and leases of non-residential space	Setting of ceiling or flat rents		Ensure rent increases are submitted in a timely manner
7.	Approving operating policies			Assess operating policies; review procedures for collecting rent; pet policy
8.	Reviewing and accepting annual audit			Determine if there is known or suspected fraud
9.	Creating and revising property-specific strategic plans and capital budgets	Long term capital planning; long-term viability of stock; property repositioning; replacement strategies		
10.	Approving major contracts and capital expenditures that exceed management agent's authorized levels			Review requests for reserve for replacement
11.				Verify distributions to owner

The final rule and notice 2006-14 are even more specific that the asset manager must be responsible for the property's regulatory compliance. The final rule states that asset management includes risk management pertaining to regulatory compliance. The notice goes even further by saying that a stop-loss agency is not in compliance with asset management if has not adhered to all the program components measured by the Public Housing Assessment System (PHAS), fair housing regulations, the admissions and continued occupancy policies, rent calculations and tenant reporting. The contract administrators, too, must assess operating policies and ensure similar indicators to those in PHAS by monitoring the physical condition, occupancy rate and financial status.

Thus, appendix C of the Harvard Cost Study, the final rule and notice 2006-14 show that for the first asset management responsibility—performance of the property

and compliance with regulations—asset managers have extensive duties, which in turn correspond closely to those of the contract administrators.

The other two responsibilities, though—making decisions that are above the capacity of the property manager and developing a long-term strategy for the property—are beyond those of the contract administrators and must be considered separately.

B. Costing out asset management responsibilities

1. *The project-based Section 8 contract administrators.* Since asset management consists of reviewing and monitoring the physical condition of the property, its financial condition and its regulatory compliance, one method of determining how much these activities cost is to look at how the contract administrators, who also perform these functions, are paid. The contract administrators are remunerated in one of two ways. Housing authorities which contract directly with HUD are paid by a formula described in handbook 4350.5. Basically, the formula takes the FMR of a two-bedroom unit from 1991 and adjusts it to the present using the annual adjustment factor for each year. Then, this administering agency receives 3 percent of this amount per unit month.

Although PHADA does not have information on every contract administrator, the information it has indicates that these fees greatly exceed the amount HUD has suggested for housing authorities.

Although the FMR will differ depending on the region of the country, the range will go from a low of about \$400 to a high of about \$1,551, and so the formula will produce fees starting at a low of \$12 PUM and going to a high of close to \$47 PUM. Thus, even the low for contract administrators, which must perform only one of the three asset management responsibilities, exceeds the amount the HUD has proposed for the asset management fee for public housing.

Contract administrators serving either a state or a region of the country are paid through a competitive bidding process. HUD selects the best contract administrator from the groups which have applied for the work. The fee is part of the bid. Although PHADA does not have information on every contract administrator, the information it has indicates that these fees often exceed \$20 PUM. Thus, they are in a range similar to the fee generated by the formula and one which greatly exceeds the amount HUD has suggested for housing authorities.

2. *Methods described in the Harvard cost study.* The Harvard cost study's appendix C provides three methods of determining the asset management fee. The first is to do what these comments have done, model it after similar work, such as the responsibilities of the contract administrators. The cost study, though, does not analyze the cost of the contract administrators, despite its saying that "...the term asset management is frequently used to refer to contract administration..." but instead chooses tax

credit monitoring agencies. According to the cost study these fees range from \$1 to \$17 PUM.

The third method of determining the asset management fee is based on the profit of the FHA properties' owners. Appendix C of the Harvard cost study states that the "median profit (before depreciation) of properties in the FHA database for 2000 was \$76 PUM"—well in excess of the \$10 PUM HUD amount.

Tax credit monitoring, though, as described in 26 CFR 1.42, is very different from contract administration and asset management responsibilities, and one might add the description of its responsibilities in the cost study's appendix C. First of all, in the tax credit program, monitoring only has to be conducted once every three years, and needs simply to include a physical inspection of 20 percent of the units along with a review of the tenant files for these same units. Unlike contract administrators and other asset managers, tax credit monitoring does not include a responsibility to review the operating budget, the accounting, the staffing, the vacancy rate, screening procedures, rent increases, operating policies or determine whether there is known or suspected fraud. Therefore, unlike contract administrators, tax credit monitoring is not a good model for basing public housing's asset management fee.

The second method in appendix C is to base the asset management fee on its relation to the property management fee. The report states, "Most professionals would easily surmise that the task of ownership (beyond property management) should cost half or less than what is charged in management fee." The study reports that property management fees typically run from \$20 PUM to \$40 PUM.

As PHADA has already commented, HUD has not yet come up with a "reasonable" property management fee, as required by the rule. Therefore, it is difficult to use this method. Nevertheless, even taking the amounts in attachment A of the supplement to the Financial Management Handbook, there is a different picture. The property management fees in this schedule range from \$36.90 to \$63.07. Considering that these amounts do not reflect the property management fees for the limited dividend properties and are at least two years old, the average comes to well above \$50 PUM. Of course, this amount does not include funding for add-ons or for public housing's unique operating and regulatory environment.

Simply applying appendix C's method to these figures, though, would provide a much higher asset management fee than the \$10 allowed by HUD. If the asset management fee is to be half the property management fee, then it would be at least \$25 PUM. Alternatively, since HUD has offered \$10 PUM, which is half of the low end of its \$20–\$40 range, taking half of the low end of the range in Attachment A would mean an asset management fee of at least \$18.45 PUM. Thus, no matter how this method is applied, housing authorities are entitled to far more than the \$10 PUM HUD has allowed.

The third method is based on the profit of the owners of the FHA properties. Appendix C has stated that the “median profit (before depreciation) of properties in the FHA database for 2000 was \$76 PUM.” In a meeting on this issue, Byrne stated that this figure was a typo. He announced that it would be corrected, but to date no further information on this subject has been offered.

Given the context of the report, though, it does not appear to be a typo. The narrative of the report states, “it stands to reason that any asset management costs would be some small percentage of this profit.” Thus, the narrative of the report indicates that the profit is much larger than the \$5–\$15 asset management fee estimate listed in the report, making it appear as if the \$76 PUM is a valid amount. Therefore, considering that the report was issued three years ago in 2003, and that the \$76 PUM figure has been quoted in print many times and was also discussed during negotiated rulemaking without being challenged, PHADA will continue to consider it valid unless better information is made available. Clearly, then, the owner’s profit is substantial and sufficient to pay an asset management fee well in excess of the \$10 PUM HUD amount. Thus, the methods employed by the Harvard cost study, authored by Byrne, support the need for a revision to the asset management fee listed in the supplement to the Financial Management Handbook.

3. Limited dividend property payouts and partnership management fees. Another model would be the amount paid to owners of the limited dividend properties. These owners generally received significant tax breaks from the development of their properties, which in effect served the role of profit. As a result, the distribution itself could be considered to be the asset management fee. PHADA understands that this amount generally ranges from \$15 to \$30 PUM.

Finally, managing partners of tax-credit properties are also provided an asset management fee. This fee is separate and distinct from the property management fee. One of PHADA’s members, the Bellingham/Whatcom County Housing Authorities, has provided PHADA with a table of the asset management fees it earns as the managing partner. For its five tax credit properties, these fees average \$44.15 PUM. The asset management responsibilities of the managing partner are quite similar to those of a housing authority.

Project	Units	Asset management fee	PUM
Heather Commons	25	\$20,000	\$66.67
Prince Court	25	\$5000 + 50% cash flow (\$2500)	\$25
Oakland Block	20	\$5000 + \$10% gross cash (\$1984)	\$29.10
River House	50	\$20,000/year + 50% of cash flow (\$15,000)	\$58.33
Laurel Village	50	\$25,000	\$41.67
Mean asset management fee			\$44.15

PHADA has also been informed that a national developer and manager of affordable housing charges a “partnership management fee” using a formula for properties of all sizes based on 9 percent of projected effective gross income. PHADA understands this amount is roughly equivalent to public housing’s property expense level. Thus, the amount it charges for work similar to public housing’s asset management fee resemble a fee based on 9 percent of the PEL.

HUD has not completely addressed the issue of the cost of the long-term strategic planning for properties. According to the final rule, housing authorities are required to conduct long-term strategic planning including assessing the viability of the stock and then if appropriate developing property repositioning and replacement ideas.

Not all housing authorities will decide that a repositioning policy is in the best interests of their properties. For those that do and use the mixed finance program, the 3–6 percent administrative fee can be used to meet the agency’s asset management needs. For those that do not, however, there still is a cost associated with planning and acting on long-term decisions for the property.

HUD has not directly addressed the costs of these responsibilities in the asset management fee. It is acknowledged by those engaged in long-term planning that these costs can be considerable. PHADA believes HUD must identify the different types of long-term planning, rehabilitation and repositioning that can occur and develop a cost proposal covering these different levels of work requirements.

Another factor which needs to be considered is geographic location. It hardly seems worth mentioning that the asset management fee in areas with high costs will not be the same as the fee in areas with lower costs, but as HUD has ignored this obvious fact, it does have to be mentioned. As an example, the median income in Blaine County, NE is \$34,450, while in San Jose, CA it is more than three times as much at \$105,500. Clearly, contract administrators’ fees are distinguished by geography, since they can be based on the FMR. Therefore, it is not sensible to provide the same asset management fee for every location.

C. Requirements placed by HUD on charging properties an asset management fee

Another important issue relating to the asset management fee is the question of how an agency will actually qualify for one. HUD has proposed requiring each property to have a one-month reserve before it can provide an asset management fee to the central office. A standard this rigid will mean that many properties will not qualify for an asset management fee. The entire concept of requiring a reserve is unrealistic in an era when housing authorities face a 74 percent proration and skyrocketing utility costs. Housing authorities should not be expected to maintain a reserve at these funding levels and should not have the funding needed to carry out essential housing authority functions dependent on a reserve level that may either be unrealistic or not in the best interests of the property.

Properties should also be able to accrue a payable to the COCC, if they cannot pay the asset management fee due to a low proration caused by inadequate funding of the formula. The definition of a low proration could be any amount below the 25-year average between 1981 and 2005.

The asset management fee is an important component of the conversion to asset management and will be critical to housing authorities being able to fulfill their responsibilities. HUD has not given this fee adequate thought, and in its current configuration, it is not sufficient to fund the tasks it is supposed to pay for.

PHADA believes HUD needs to increase the \$10 PUM asset management fee. To begin, HUD should list the responsibilities it believes are encompassed under the concept of “asset management” and provide an estimate of the cost of these responsibili-

ties along with a transparent method. PHADA has demonstrated that the costs of monitoring, as performed by the contract administrators and managing partners of tax credit properties, will amount to much more than \$10 PUM. Similarly, the long-term planning component can be extremely expensive. Finally, there is the cost of taking the decisions that need to be made to run the property above the level of the property manager, such as hiring the property manager, reviewing the budget, approving capital projects, handling legal issues, reviewing the audit and interacting with HUD and state agencies. HUD also needs to prepare an estimate of these costs. These estimates and a transparent method of how they were derived should then be available for public comment.

The entire concept of requiring a reserve is unrealistic in an era when housing authorities face a 74 percent proration and skyrocketing utility costs.

The supplement states that the asset management fee was “based on an examination of cash flows in HUD’s multifamily projects...” (p. 35). This cash flow averaged \$76 PUM in 2000. Thus, HUD apparently decided that the asset management fee should be based on 13 percent of 2000’s cash flow. As this method seems so unusual, PHADA believes HUD owes its housing authority partners some further explanation of how it was developed.

Section Four: Capital Fund

A. QHWRA permits capital funds eligible for operations to be used for administrative expenses

PHADA has been very clear that it believes that HUD's prohibition of the use of the capital fund for central office costs violates the QHWRA statute. Both the notice and the supplement to the Financial Management Handbook mention this prohibition. In the Federal Register, p. 52712, Section XII, it says "Additionally, where a PHA may use Capital Funds for 'management improvements' and 'operations,' it may only use those amounts to fund 'property' expenses and not expenses of the central office cost center." The Supplement, p. 24, states "**Except for certain exceptions noted in this section, and other than through use of management fees, Capital Fund Program funds cannot be used to directly support the COCC**" (bold in original).

PHADA has been very clear that it believes that HUD's prohibition of the use of the capital fund for central office costs violates the QHWRA statute.

QHWRA describes which operating fund costs are eligible for the portion of the capital fund that can be used for operations, and administration is clearly included. HUD has introduced the idea that when capital funds are used for operations they lose their character as capital funds, but PHADA does not believe that a change of this nature occurs. PHADA has had its general counsel meet with HUD's office of general counsel to ensure that the Department has no misunderstanding concerning PHADA's position.

The Senate Appropriations Committee has also passed language which confirms PHADA's interpretation of the QHWRA statute. Senators Christopher Bond (R-MO) and Patty Murray (D-WA), chairman and ranking member respectively of the TTHUD appropriations subcommittee, have also written to HUD in support of PHADA's understanding, explaining to the Department that it must present legislation if it wishes to change QHWRA.

This issue is a critical one for housing authorities. HUD must acknowledge that its definition of a "reasonable" property management fee is not infallible. PHADA has already described in some detail its shortcomings. An additional issue to consider is the fact that HUD's schedule is based on the 80th percentile of the FHA property fees. Therefore, even in the private sector represented by the FHA properties, 20 percent of them require fees above HUD's fee schedule. These include properties which are trying to maximize their profit, so their property management fees are as low as they can be. If they are above the 80th percentile, it is because they need to be to manage the properties. These fees must be "reasonable" since they are authorized by the Department.

It stands to reason that there will also be many public housing properties which need fees beyond HUD's fee schedule. As with the 20 percent of FHA properties, it

may not have anything to do with management style or any preconceived notions HUD may have about the appropriateness of public housing's central office costs. It may simply be a necessity to manage well-run property. Housing authorities need the flexibility to be able to respond to these circumstances. Having the statutory authority provided by QHWRA to utilize capital funds for these purposes when necessary provides housing authorities with this much needed flexibility.

PHADA urges the Department to reverse its position on this critical issue and continue to implement the provisions of QHWRA which permit the use of capital funds for administrative purposes.

B. Additional Capital Fund issues

There are several other issues in regard to the Capital Fund.

1. Payment of the 10 percent management fee. After the disbursement of 50 percent of the management fee over the first year, the remaining funds will be disbursed to housing authorities proportionately to the spending of the capital fund. PHADA sees several problems with this policy and requests that the Department return to the system of paying housing authorities their management costs based on actual expenditures.

The first and most important issue is that housing authorities need a stable cash flow to carry out their capital improvement work day in day out. Capital improvements are known for being very inconsistent in rate of expenditure. Therefore, it is not wise to base housing authority management fees on capital fund expenditures, because if this method leads to a cash flow problem, housing authorities may not be able to perform their work.

Secondly, many, many problems can develop with a capital improvement project. First of all, the bids can come in over budget. Therefore, the design documents may need to be redone, once or even more than once. Secondly, a contractor's work schedule can be delayed for many reasons. Some are legitimate, such as weather, or unforeseen conditions, while others may reflect lack of competence on the contractor's part. In extreme conditions, the contractor may default.

The relationship between the housing authority and the contractor is often filled with tension. The housing authority has to enforce the design documents, insist on quality work and negotiate a fair price for any change orders. In carrying out these responsibilities, the housing authority may often be called upon to withhold or delay payments to the contractor.

Placing the housing authority's own payment at the mercy of the payment to the contractor creates an unnecessary conflict of interest for the housing authority. The housing authority needs to hold the line to ensure quality work, but it either may not be able to or may be tempted not to when its own payment depends on paying the contractor. Will housing authorities be as ready to throw out bids, demand work be redone and insist on a fair change order price when they know that delay will mean that they will not get paid either?

HUD should encourage PHAs to carry out their fiduciary responsibilities, but this policy provides an incentive to approve inferior work, excessive costs and unsatisfactory bids just to get some work accomplished in order to be able to process a payment. HUD must rethink this shortsighted policy and return to the existing system. Housing authorities are accomplishing their capital fund responsibilities and meeting the statu-

tory time frames for obligated and expending money. Since there is no real problem in this area, HUD does not need to take an action which appears to be designed as an incentive to get work accomplished more quickly.

Placing the housing authority's own payment at the mercy of the payment to the contractor creates an unnecessary conflict of interest for the housing authority.

2. Capital Fund Financing Program (CFFP). Guidance states on page 27 of the supplement that “Capital Fund Program management fees will be considered earned annually and calculated from the total amount of the Capital Fund Program award.” This decision appears to hamper the administration of the capital fund under the financing program.

Under CFFP, an authority may receive significantly more money one year than its annual award. Apparently, however, its management fee will be based solely on its annual award. Thus, it appears questionable that an authority could manage a significantly larger amount of work, based on the significantly larger amount of funding it has available, while only receiving a management fee based on the smaller, annual amount.

PHADA urges the Department to rethink this provision. The management fee should be based on the amount of money available. It would appear logical, then, that an authority should be able to draw down 10 percent of the amount of capital fund it has available through the CFFP program.

3. Front-line costs vs. management fees. The guidance in the supplement states that “documented costs incurred during the **construction** phase of the project” are considered front-line costs of the asset management project (AMP), and as such can be considered an expense above and beyond the 10 percent management fee.

HUD’s description of what constitutes a “cost during the construction phase” seems confusing. On the one hand, the guidance states that “only actual, documented costs pertaining to the construction supervision activities, such as inspections, incurred during the construction phase, can be charged directly to the AMP.” This sentence seems to be consistent with HUD’s bolding out of the word “construction” cited above.

However, immediately following this description, the guidance has another description and an example that appear to establish a different standard. This further guidance states that “such costs... include architect and engineering fees related directly to a specific construction project...” The example then specifically states that an architect’s work planning an improvement to an AMP “is considered a front-line cost...”

As stated, PHADA is confused by these descriptions. Is capital improvement work related only to the **construction** supervision phase considered to be a front-line expense? Or is the work done by architects and engineers designing an improvement

also considered to be a front-line expense? PHADA would appreciate clarification of this issue.

4. *Non-dwelling equipment.* The guidance in the supplement (p. 26) states that the “Capital Fund grant may not be used to support front-line service needs that continue to be centralized” such as a vehicle. PHADA believes this prohibition runs counter to the rule and is an example of unnecessary micromanagement, and it asks the Department to remove this prohibition.

For instance, a 360-unit PHA with a central maintenance department could not buy a vehicle for its maintenance workers under this provision. On the other hand, a 360-unit project could buy one, and a shared resource totaling 360 units also appears eligible for a vehicle purchased by the capital funds. It does not make sense to have different regulations for such similar circumstances. Each of these configurations is a legitimate management decision, in conformity with the rule, made in the best interests of the property, and it is unwise for the Department to prohibit actions for one configuration while permitting it for another which is essentially the same.

5. *Management improvements.* HUD has forbidden the use of management improvements for the COCC (p. 26, supplement, Financial Management). Certainly, HUD cannot deny that there are legitimate COCC uses for management improvement funds. Housing authorities note that they often use them for computer upgrades, for instance. A housing authority might also need assistance in its labor relations, especially as organizational changes connected to the conversion to asset management might require extensive union negotiations. This help could be an eligible and important management improvement use. As there are legitimate and necessary uses for management improvements for the COCC, therefore, which have been permitted by HUD throughout the existence of the capital fund program, PHADA asks that the Department reinstate the eligibility of the COCC for management improvements.

Section Five: Assignment of Costs

A. The language in the rule itself

With the establishment of property management fees, the issue of what costs are assigned to the central office and what are assigned to the front line becomes important. Essentially, PHADA believes the rule allows front-line costs to be done centrally and still be assigned to the project as front-line costs. Unfortunately, this guidance contradicts this basic axiom.

Section 990.275 of the rule states “Property management services may be arranged or provided centrally; however, in those cases in which property management services are arranged or provided centrally, the arrangement or provision of these services must be done in the best interests of the property, considering such factors as cost and responsiveness.”

Here are the relevant sections of the rule. Section 990.275 states “Property management services may be arranged or provided centrally; however, in those cases in which property management services are arranged or provided centrally, the arrangement or provision of these services must be done in the best interests of the property, considering such factors as cost and responsiveness.” Thus, the section states clearly that property management services (without any qualification) can be arranged centrally, with the only restriction being that they must be done “in the best interests of the property, considering... cost and responsiveness.” It seems quite clear that if a property management service is done cost-effectively and responsively, it can be provided centrally.

If it is done centrally, where are the costs placed? This question is answered in section 990.280 (d) which says, “In the case where a PHA chooses to centralize functions that directly support a project..., it must charge each project using a fee-for-service approach.” Thus, the rule specifically addresses the issue of how a centralized function is to be expensed. According to this section of the rule, it is to be expensed to the project using a fee-for-service approach.

PHADA believes the rule is quite straightforward in stating that property management functions can be done centrally, and if so can be expensed to the projects. The only restriction is that they must be cost effective and responsive.

HUD, however, has not followed this straightforward language and has promulgated guidance which requires several functions provided centrally to be expensed centrally. Therefore, PHADA does not believe this guidance complies with the rule and it asks that it be changed.

The reasoning PHADA has heard from the Department is that the rule also says asset management is supposed to follow the multifamily model and that in the multifamily world, some centralized functions, such as procurement, are not done cen-

tally. Section 990.255 states “PHAs shall manage their properties according to an asset management model consistent with the management norms in the broader multi-family management industry.” This section goes on to state that one of the goals of asset management is to “improve the operational efficiency and effectiveness of managing public housing assets.”

PHADA believes that there is no conflict between the section in 990.255 calling for asset management to follow management norms in the multifamily industry in an operationally efficient and effective manner and section 990.275 which permits functions to be done centrally if they are done in the best interests of the property, considering cost and responsiveness.

If the purpose of asset management as defined in section 990.255 is to improve operational efficiency and effectiveness, and if providing a service centrally as permitted in 990.275 is cost efficient and effective, then it has met the management norms of the multifamily industry. In effect, the management norm of this industry is that operations be efficient and effective, and that norm is met under 990.275 because the central provision of the service is efficient and effective. Thus, PHADA does not believe HUD should pick and choose which services provided centrally can or cannot be expensed at the front line. If they are efficient and effective according to 990.275 they meet multifamily norms and can be expensed at the front line as provided in 990.280. The rule certainly does not want housing authorities to adopt a “multifamily norm” that would not be cost efficient and effective.

Furthermore, PHADA does not believe the rule would have, on the one hand, stated that actions be consistent with multifamily norms (990.255) while on the other hand stating that services could be done centrally if they were cost-efficient and effective (990.275) unless providing cost-efficient and effective services centrally was consistent with multifamily norms. The key is whether they are efficient and effective, because that is the most important multifamily norm.

It simply does not make sense to say that a certain function must be done at the front line because it is done that way most often in multifamily if it can be done more cost-efficiently and equally effectively centrally in public housing.

In conversations with multifamily providers, they have confirmed to PHADA that indeed their most important norm is that a service be efficient and effective. They do not care whether it is provided centrally or at the front-line. What they care about is whether or not it is cost-effective and accomplishes the required task. If given the choice between accomplishing a task equally effectively for more cost at the site or for less cost centrally, a multifamily manager will choose providing the service for less cost centrally. Providing a service efficiently and effectively is the overriding multifamily norm, and that should be the same for public housing, as described in 990.275 of the rule.

It simply does not make sense to say that a certain function must be done at the front line because it is done that way most often in multifamily if it can be done more cost-efficiently and equally effectively centrally in public housing. That would contradict 990.255 which states that a goal of asset management is operational efficiency. If it can be done more cost-efficiently and equally effectively centrally then it should still be expensed at the front line as described in 990.280.

B. Explanations provided during negotiated rulemaking

PHADA also believes that explanations of whether property management services would be central or front-line during the negotiated rulemaking sessions support its understanding of the rule. This topic was discussed on May 12, 2004. Here is the statement of Byrne, HUD's Director of Public Housing's Financial Management Division.

“And essentially my view of the reading of this is, the property's running well; you actually have true costs. Over and done with. I don't ask questions about whether you've got—whether the manager is sitting in the central office or sitting in the property. What's most important is, the property is performing well. And so that way, if there's not language in here that says, Property management means, you have to have this function done at the property or not. There's a bias towards it, because you know, in Jeff's survey and others, is that predominantly people tend to do that stuff—more at the property level; but some people do it a little bit differently.

“So not for HUD to get into that game, but more or less to say, Are you performing and are those costs reasonable? Can you show me that those, in fact, are those the costs? And there are costs that you're doing that are centrally provided that aren't normally part of the management fee, then I want to make sure that those are the actual costs and those are reasonable. And I think that is the overall approach.”

PHADA believes this statement by Byrne is very important as it was provided in the context of negotiated rulemaking to explain what was intended by the language in the rule. Here are the points that were made.

1. The performance of the property is what is important. Exactly how the performance is achieved is not important. He specifically says, “I don't ask questions about whether... the manager's sitting in the central office or the property.” Thus, there should be no requirements forcing housing authorities to perform functions at the property, and he says the rule does not say that “you have to have this function done at the property...”
2. Although, functions may be done generally more often one way than another, there is still variety. “Some people do it differently.” The rule does not have a problem with performing a function differently than it is normally done.

3. It is important to know the actual cost of the function, no matter how it is done. That is why the rule calls for centrally provided functions to be expensed to the front line.
4. There can be centrally provided functions in public housing “that aren’t normally part of the management fee.” Just because it is not normally part of the management fee in multifamily does not mean that it will not be allowed to be done centrally and expensed to the front line in the public housing operating fund rule. Again, he reiterates that what is important is knowing the actual costs and that they be reasonable.

Byrne explained the issue of centrally provided front-line services in this manner to the negotiated rulemaking committee. The committee, in turn, developed a rule which embodied these concepts—property management services could be done centrally or at the site, and if they were done centrally they would be expensed to the front-line.

Unfortunately, however, this guidance contradicts the rule and Byrne’s explanation in several important ways, which PHADA asks be changed so that the guidance conforms to the rule.

PHADA has the following specific concerns.

C. Procurement

This guidance does not appear to permit central procurement to be expensed to the front line (supplement, p. 43). As PHADA has commented, this guidance does not comply with the rule. The rule is clear that property management services may be performed centrally and if done so may be expensed to the front line. There is no justification for HUD’s decision in this regard, even if it is the common method in the multifamily program. HUD has not stated that other services commonly done at the project level in multifamily, such as rent collection, work order management and maintaining the waiting list cannot be expensed to the front line. Therefore, HUD is acting inconsistently in singling out this one service and stating that it must be expensed centrally.

In essence, the IG is requiring housing authorities to utilize centralized procurement, but HUD is not allowing any compensation for performing the function centrally.

This decision is especially unfortunate, because the Inspector General’s office has specifically stated that it encourages centralized procurement as a means of combating waste, fraud and corruption. PHADA has provided this information to the Office of Public and Indian Housing.

The Inspector General has also required housing authorities to use centralized procurement following an audit. The recent audit of the Omaha, Nebraska Housing Authority, 2006-KC-1010, is an example of this action. It found “Authority Management Not Effectively Involved in the Procurement Process,” because it did not “appoint a procurement manager” (p. 7). In essence, the IG is requiring housing authorities to

utilize centralized procurement, but HUD is not allowing any compensation for performing the function centrally.

This audit is troubling in another regard as well. According to the IG, the Omaha Housing Authority had numerous similar small purchase contracts whose total exceeded their local policy of \$10,000, as well as HUD's \$100,000 limit. Since the total of these small purchase contracts exceeded this threshold, the IG stated that they should have been bid out as a single contract, allowing the housing authority potentially to receive a lower price. "One vendor billed the Authority for \$309,693 or 86 percent of the total amount. The Authority should have consolidated these purchases to obtain the best price" (p. 6).

If procurement is conducted separately at each project as this guidance envisions, housing authorities will not be able to comply with the IG's requirement. The IG is requiring that housing authorities conduct their procurement centrally, but this guidance is not allowing them to get paid for performing it in this manner. The IG considers the housing authority as an entity, combining all of its procurement, while this guidance appears to assume that procurement will be evaluated project by project.

Since centralized procurement expensed at the front line complies with the rule, is consistent with HUD's treatment of other services, such as rent collection, and allows housing authorities to meet the requirements of HUD's Inspector General, PHADA believes that HUD should change this guidance to permit authorities to conduct procurement activities centrally, yet expense them to the project level.

Many front-line functions require supervision. If a worker has to be sent out to repair a leak, someone needs to organize the job, be available for consultation and ensure that it was done properly. In multifamily, a supervisor at a project performing this work is expensed to the project.

D. Maintenance supervisors

This guidance is extremely inconsistent and confusing in its treatment of how to expense supervisors of personnel performing front-line functions. PHADA believes that in many cases the Department is not following multifamily practice or allowing personnel performing front-line functions centrally to be expensed to the project as required by the rule. This confusing guidance is a vivid example of HUD's micromanagement and top-down decision making when local boards are far better positioned to evaluate costs and assign staff.

Many front-line functions require supervision. This observation does not refer to supervisors who oversee project management such as a regional manager. It refers to the fact that if a worker has to be sent out to repair a leak, someone needs to organize the job, be available for consultation and ensure that it was done properly. In multifamily, a supervisor at a project performing this work is expensed to the project. This practice is confirmed in the staffing plan presented by the Harvard cost study for Washington Carver in New York City. The staffing plan for this project had a full-

time maintenance superintendent as well as a full-time assistant maintenance superintendent. Thus, practice in multifamily pays for a supervisor assigning and overseeing the work of maintenance employees at a project to the project itself.

In other public housing staffing plans in the Harvard cost study, as well as in the staffing plans of public housing projects managed privately, there was a cost associated for routine maintenance supervision. If it was not a full-time supervisor, as in the case of Washington Carver, it was the extra cost associated with a lead worker such as at Boston's Whittier Street or Detroit's Sojourner Truth. The principle is clear, though, that in the multifamily world supervisory work for all maintenance, routine as well as specialized, is a project expense.

Rather than following multifamily practice and the rule, however, this guidance has taken a random approach allowing some centralized supervisors to be expensed at the project and prohibiting others.

Most notably, in maintenance, a housing authority may charge a fee-for-service for specialized maintenance tasks, such as electrical work, which would cover overhead, including supervision, but it may not charge such a fee for routine maintenance work. Using direct costs, the agency cannot expense a central supervisor at the front line for either routine or specialized maintenance. These inconsistent decisions do not follow the multifamily pattern demonstrated by the Harvard cost study. All maintenance supervision was paid for at the project level, not simply that for specialized trades. PHADA asks that HUD simply follow the rule, which permits property management services to be done centrally and expensed at the project level. Supervision of maintenance is clearly one of these eligible property management services.

HUD's distinction between specialized and routine maintenance does not make common sense. As demonstrated, the supervision of front-line maintenance work is clearly a front-line expense. If, in order to be more cost-effective, a housing authority chooses to combine several projects and supervise this work centrally, in order to take advantage of economies of scale, it should be encouraged in this decision, because it will improve the cost-efficiency of its operation, not discouraged by prohibiting assigning supervision costs to the project. Housing authorities may only be funded at a 74 percent proration level in 2007, so they have to look for economies of scale which might not be necessary in multifamily.

Similarly, it does not make sense to allow supervision for specialized trades to be paid using a fee-for-service approach, but not allow it to be paid by using actual, documented costs, which can be used for the maintenance personnel themselves. Either supervision is an eligible project-level cost when it is done centrally or it is not. Since HUD has determined that specialized supervision is, supervisors' direct costs should be eligible to be expensed at the project level similarly to those of the maintenance mechanics and groundskeepers.

HUD's guidance on the issue of maintenance supervisors is ambiguous in the area of shared resources. Is it permissible to have a maintenance supervisor, or a maintenance lead man, for routine maintenance for several projects at an authority, but not for all projects as in a completely centralized system? It appears so on page 39 of the supplement, which says "Where it is not economical to have full-time personnel dedicated to a specific AMP, the PHA may establish a reasonable method to spread these personnel to the AMPs receiving the service." Since maintenance supervisors are not

excluded, one assumes that spreading their costs is also permitted. By maintenance supervisor, PHADA also includes a lead maintenance man, who gets paid more than the regular mechanics. The salary differential for supervision appears to be eligible to be spread among the projects in question rather than having it placed in the central office cost center.

This interpretation is supported by the Management Agent Handbook, p. 6-31, which states, “If front-line management functions for several properties are performed by staff of the agent operating out of a single office, the following conditions apply. The agent must prorate the total associated costs among the projects served in proportion to the actual use of services. Allowable total associated costs include: Salaries and fringe benefits of personnel performing front-line duties....” PHADA has demonstrated in this section that maintenance supervisors are performing front-line duties.

PHADA’s position—which is supported by the rule, multifamily guidance and practice, and cost-efficiency—is that direct supervision of maintenance work should be a front-line cost.

One can imagine, then, an agency that decides that it should provide one maintenance supervisor, or lead man, for three 120-unit projects under the shared resources rubric. Apparently, such a decision would permit these costs to be expensed at the project level. Imagine a second agency with three similar projects and a total of 360 units, which makes the same decision. In its case, its supervisor, or maintenance lead man, is a “centralized” one rather than a “shared resource.” Therefore, under this guidance it appears this second authority is not permitted to expense these costs to the project level. It seems very far-fetched, though, to make a distinction between these two almost identical situations and say that the centralized authority cannot expense its supervisory costs to the projects while the shared resource one can.

If PHADA has misinterpreted this guidance and it were permitted, since these two cases are essentially the same, at what point would it become improper to attribute a centralized supervisor’s cost to the front line? If there are more than 400 units? 500 units? 750 units? 1,000 units? Washington Carver with 1,246 units had a maintenance supervisor and an assistant supervisor charged to the front-line. Would a housing authority with 1,246 units not be able to charge the centralized costs of a maintenance supervisor and an assistant supervisor to the front line?

If the answer is no, would the same 1,246-unit authority be able to charge the costs of two separate maintenance supervisors to the front line if they each operated under the shared resources guidelines and supervised 623 units apiece? Apparently they would, based on the language on page 39 and the description in the Management Agent Handbook. If they could, is that decision cost-effective? Based on salary levels, a staffing plan with a supervisor and an assistant supervisor would probably be less expensive and therefore more cost-effective for the authority than two separate supervi-

sors under the shared resource provision. As a result, the centralized supervisors conform more to asset management's goal of operational efficiency stated in 990.255.

Another possibility is that HUD might say that it would not be proper to expense a supervisor of 643 units under the shared resource language. If so, where would the line be drawn as to the number of units that could be supervised? Or does the shared resource language mean that no maintenance supervision costs can be shared across projects? If that is the case, it clearly contradicts the Management Agent Handbook and 990.255 of the rule.

PHADA hopes that this discussion illustrates how arbitrary and essentially counter-productive HUD's parsing of maintenance supervision costs is. Housing authorities need to make their own decisions to establish their optimal staffing patterns based on their budgets. PHADA's position, therefore, which is supported by the rule, multifamily guidance and practice, and cost-efficiency, is that direct supervision of maintenance work should be a front-line cost.

E. Administrative supervisors

In addition to contradicting the rule, HUD is also extremely inconsistent when it comes to supervisors of administrative front-line functions. Page 38 of the supplement states, "With the exception of a central waiting list, a project may not pay for the cost of a supervisor overseeing a front-line task that is performed centrally." On the very next page, though, it states in regard to resident services that "where PHAs cannot reasonably track personnel costs for resident services, including supervisory personnel costs to an AMP, PHAs are permitted to prorate these costs to AMPs."

Thus, it appears that at least two administrative front-line supervisors can be expensed to the front line. Other front-line supervisors, such as those overseeing rent collection and work orders, cannot have their expenses paid for at the project level. This distinction appears arbitrary.

As PHADA has pointed out, the rule clearly states that housing authorities can perform property management services centrally, and if so can expense them to the front line. Thus, by prohibiting this practice for some administrative supervisors, HUD is in violation of the rule and it should reverse its decision.

F. Inspections and other issues

HUD has only permitted expensing centralized inspections to the front line for the first year of project-based accounting. Since HUD has also stated that housing authorities need not comply with its property management fee schedules during the first year of project-based accounting, this decision has no practical meaning.

Inspections are a property management service, and as such, housing authorities are permitted by the rule to perform them either centrally or front-line. If they choose to perform them centrally, the rule clearly states they may expense them to the front line.

PHADA would also like to point out that this issue was directly addressed by Byrne during negotiated rulemaking. Again on May 12, 2004, he discussed the management fee. Here is how he explained it. "And so the other costs that the agency would choose to do centrally like a central maintenance or a central inspection does not get funded out of that (the management fee); but that separately, centrally provided property

management service would have to be done on some fee-for-service basis for which you are charging the property based on the service received and whatever the reasonable cost of that service is. Does that help you?”

The rule itself reflects Byrne’s statement almost verbatim. It is extremely puzzling to PHADA, therefore, that the guidance that HUD has issued on inspections and central maintenance contradicts both Byrne’s explanation and the rule. PHADA’s point in these comments is simply to ask that HUD honor the explanations that were made to participants in the negotiated rulemaking prior to their voting on the rule and honor the rule itself.

Below are two additional issues.

Other maintenance expenses. HUD has stated, for instance, that for centrally provided routine maintenance, housing authorities may only charge for direct personnel costs. In addition to the supervisory costs, it means that all other maintenance costs, such as the costs of a vehicle, vehicle insurance, gas, and tools, among other costs, must be charged to the central office.

Clearly, the cost of tools is not a central office cost and expensing it as such violates the rule. PHADA asks whether a vehicle, insurance and gas are eligible front-line expenses under the shared resources concept. If so, PHADA reminds the Department that similar staffing arrangements for similar circumstances could be treated differently. A group of AMPs totaling 360 units could have a vehicle paid for at the project level, while a 360-unit PHA performing its routine maintenance centrally could not.

PHADA believes all maintenance costs should be expensed at the project level as permitted in the rule and confirmed in Byrne’s statement to the negotiated rulemaking committee.

Separating costs for personnel working for both the COCC and the AMPs. HUD understands that some personnel, such as an executive director in a small housing authority, provide services that are both front-line and central office. In this guidance (p. 39) HUD has stated that when performing front-line work, personnel, such as an executive director, cannot charge their salary to the project, if it exceeds the cost of a property manager.

PHADA believes this decision is unnecessary micromanagement which will add to the difficulty of administering small housing authorities. If the difference between the salary of an executive director and that of a property manager is sufficient to make the housing authority unable to live within the management fee schedules, the agency will in effect be required to hire a part-time executive director and a part-time property manager.

It may not be possible for the agency to find as qualified employees if it is required to look for part-time ones rather than a full-time person. This guidance jeopardizes a housing authority’s effectiveness, one of the goals of asset management. The amount of money involved for these agencies is going to be relatively small, and no matter how it is expensed does not cost the Department any additional funds.

HUD should give agencies the flexibility they need to manage their properties. HUD’s guidance will only cause difficulties not only without sufficient added value but with a potential downside. Housing authorities should be allowed to assign costs based on actual salaries in cases such as these.

G. Board training, stipends and travel

HUD's guidance states that these costs are fee expenses (p. 43). Many of the properties in the FHA database upon which HUD's fee schedules are set do not have an institution comparable to public housing's boards of commissioners. Board members are private citizens appointed by their communities to oversee housing authority management. Frequently, they do not have extensive experience in managing property or administering government programs.

Since property management companies do not pay for training for a board of commissioners, this cost is not represented in their fees.

There can be no question that training for these members is vital and in HUD's best interests. Nevertheless, under HUD's arrangement, there is insufficient money for these important activities. Since property management companies do not pay for training for a board of commissioners, this cost is not represented in their fees.

It is critical that funding be available for commissioner travel and training in order to maintain high-performing public housing. Placing these expenses in the central office without a corresponding add-on is not satisfactory. Therefore, PHADA believes HUD must provide additional funding for this unique public housing function, if it is to maintain this decision.

Another possible solution is found in chapter 6 of the Management Agent Handbook (p. 6-32) which treats a somewhat similar situation when it discusses training for board members of resident-owned/co-op housing. In this situation, "Project funds may be used to provide project related training for the Board of Directors of a housing cooperative." As public housing board training will often be project-related, HUD could use this example as a precedent and allow training for public housing boards to be expensed to the projects.

Section Six: Excess Cash

A. Excess cash should not depend on a specific reserve level for every property

PHADA has two concerns in regard to HUD's guidance on excess cash. The first is the requirement that properties have one month's worth of reserve in order to determine that the property has excess cash. PHADA does not believe any reserve amount should be required. The second is the prohibition on placing excess cash into the central office cost center. PHADA believes this prohibition contradicts the rule and should be removed.

In the multifamily program, there is no operating reserve requirement in calculating a property's excess cash.

There are several reasons why HUD should not require agencies to have one month's reserve to be considered to have excess cash. First of all, the language in the rule reads, "If the property has excess cash flow available after meeting all reasonable operating needs of the property..." (990.280 (b)(5)). Thus the rule defines excess cash as solely having to meet operating needs of the property. The operating needs do not include a reserve of whatever size. They refer to the costs of operating the property. Thus, once the costs of the property have been met, any remaining revenue is excess cash.

Secondly, in the multifamily program, there is no operating reserve requirement in calculating a property's excess cash. HUD should not selectively choose the multifamily norms it believes apply to public housing.

Thirdly, HUD is not providing the full funding called for by the rule. The formula in the rule provides the amount "needed by a well-run PHA to sustain the project" (990.160 (a)). HUD is not funding housing authorities anywhere near the amount it itself declares needed to manage well-run property. Therefore, as housing authorities attempt to manage their property as well as they can without adequate funding, it is not realistic to believe that they can maintain one month's reserve for every property. Since housing authorities are not provided the funding to maintain a reserve, HUD should not require a housing authority to have a reserve before it can be considered to have excess cash.

Fourthly, it is critical that properties be able to transfer funding from one to another. The Harvard cost study had an error rate of plus or minus 42 percent. Therefore, it is extremely likely that a housing authority will have some properties whose formula expense level is inadequate, while having others whose formula expense level is more than sufficient. In order to be able to manage all of these properties optimally, housing authorities need to have the unconstrained ability to move funds from one to another. Therefore, there should be no unnecessary obstacle, such as the requirement for one month's reserve, in determining whether or not a property has excess cash.

Fifthly, properties are not really stand-alone properties. Funding can be transferred from one to another when there is excess cash. In addition, 20 percent of the capital fund is available for operations. Therefore, since the authority is still managed as an entity, it is not essential that each property have its own one-month reserve.

For all of these reasons—the language in the rule, the multifamily norm, HUD’s inadequate funding, and the cost study’s error rate—PHADA believes that there should be no requirement to have an operating reserve in the calculation of excess cash.

B. The rule allows excess cash to be used for central office costs

PHADA also believes that HUD’s guidance violates the rule by prohibiting the use of excess cash for central office costs. The rule (990.280 (b)(5)) states that “excess cash flow may be used for the following purposes:… (iii) Other eligible purposes.” It certainly does not say “other HUD-approved eligible purposes” as does the supplement to the Financial Management Handbook (p. 29). The supplement goes on to say “The COCC may not be loaned or transferred excess cash except through asset management fees.”

This guidance clearly contradicts the rule. The rule allows excess cash to be used for “other eligible purposes,” and the central office cost center is an eligible use of operating funds. Therefore, transferring money for its use meets the language of the rule.

When the issue of excess cash was raised during negotiated rulemaking, there was no indication that the language “eligible purposes” referred only to “HUD-approved eligible purposes.” Michael Liu, HUD’s Assistant Secretary for Public and Indian Housing, addressed how excess cash could be used on May 12, 2004. He stated, “if you have excess cash flow, you may use it for these other purposes. Okay? It doesn’t say you shall use it for these outlined purposes. So, if you have excess cash flow and you want to use the dollars for other purposes relative to, say, other eligible purposes, you could continue.”

PHADA believes HUD has violated the rule by having the guidance in the supplement change the language in 990.280(b)(5) from “other eligible purposes” to “other HUD-approved eligible purposes.”

Liu, thus, told the committee that a property did not have to spend excess cash flow on the other two allowed purposes—the asset management fee or fungibility to other projects; instead it could use “the dollars for other purposes relative to… other eligible purposes…” The word “eligible” has a clear meaning in the context of what housing authorities are “eligible” to spend operating funds on. It contrasts with “ineligible costs,” which refer to non-program purposes. Liu did not say “other HUD-approved eligible purposes,” which would have had a very different meaning, and PHADA does not believe the committee would have approved language saying “other HUD-approved eligible purposes.”

Thus, PHADA believes HUD has violated the rule by having the guidance in the supplement change the language in 990.280(b)(5) from “other eligible purposes” to “other HUD-approved eligible purposes.” This language was not in the rule and it does not conform to the rule. Therefore, it should be changed to reflect the rule. In addition, HUD should remove the prohibition on using excess cash for central office costs, because they are clearly an eligible operating fund expense. A housing authority which has excess cash should have the flexibility permitted in the rule to determine how to spend it.

HUD has also not been entirely consistent in its prohibition of non-management fee funds going to the central office. For instance, examine the manner in which the Department has treated cost savings from an energy service contract. “Fifty (50) percent... may be used to fund the COCC” (p. 23). Thus, in a similar situation, when a property has reduced its expenses below its revenue stream, HUD has permitted 50 percent of the savings to go the central office cost center. Allowing excess cash that exists after “all reasonable operating needs of the property” have been met to flow to the central office cost center is essentially the same principle.

PHADA, therefore, not only believes the rule specifically authorizes excess cash to be used for the central office, it believes HUD has allowed a similar outcome in a similar situation.

PHADA is somewhat unclear on the timing for the implementation of excess cash fungibility. The guidance states that there will be complete fungibility for a PHA with a June 30 fiscal year end until June 30, 2008. It then states in the supplement that “the final amount of excess cash available is based on the approved audited submission” (p. 31). Since the approved audited submission will not be available until the beginning of 2009, will an agency with this fiscal year end be able to transfer excess cash between July 1, 2008 and the date of its approved audit?

Section Seven: Small PHAs

A. Additional work is needed to establish thresholds for administrative costs

HUD has provided some confusing instructions for small housing authorities. First of all, it appears that a small PHA with fewer than 250 units, but with more than one AMP, is considered to be converting to asset management. This determination, if correct, was not clear to small PHAs when they were developing their AMPs. First of all, is PHADA's assumption correct? If so, PHADA believes that a very easy solution to the problem of small PHAs with more than one AMP which do not want to convert to asset management is to provide them with another window of opportunity to redeclare their AMPs before the implementation of project-based budgeting and accounting.

HUD has provided an additional method for small PHAs to base their central office cost in addition to the options available to other housing authorities. Small PHAs may use a table on page 49 of the Financial Management Handbook supplement, which establishes a PUM threshold for administrative costs, defined more broadly than those in the central office cost center.

PHADA has argued for additional options for "reasonable" management fees. It does, however, have the same questions concerning how these fees were calculated as it has for the property management fees in Attachment A on page 52. In other words, exactly what properties in the FHA database were used for this comparison and how do they compare with public housing properties? Are the add-ons available in multifamily available for these small public housing authorities? Is it fair to use 2004 data applicable for 2007 and beyond without inflating it? Do these administrative fee amounts reflect the cost of the 24 regulatory and operating environment differences between public housing and the FHA properties?

Exactly what properties in the FHA database were used for this comparison and how do they compare with public housing properties? Are the add-ons available in multifamily available for these small public housing authorities? Is it fair to use 2004 data applicable for 2007 and beyond without inflating it?

PHADA believes that when HUD answers these questions, it must make the requisite adjustments between the FHA database and public housing that will provide validity to administrative fee thresholds such as these. Without these adjustments, these fees are not a "reasonable" benchmark for housing authorities.

As with the property management fees, PHADA would suggest that HUD explore the option of determining the percentage of operating cost that the administrative fee in the FHA properties represents and offer that percentage as an option for a "reasonable" fee to small housing authorities.

B. Small PHAs with single AMPs should not have to differentiate between central and other costs

PHADA questions the utility of having a small PHA which is converting to asset management with a single AMP establish a COCC or use the alternate method. By definition, the housing authority central office and the project management are one and the same, because there is only one project. It appears irrelevant whether the costs of the central office exceed some threshold since those costs are for personnel and functions at the project itself. The COCC is an artificial concept. All of the money is being spent on the project, in other words.

By definition, the housing authority central office and the project management are one and the same, because there is only one project.

HUD itself recognizes this fact in the Federal Register notice, p. 52713, when it writes, “In the case of a small PHA operating as a single property, the establishment of a separate cost center would be contradictory to the streamlining and cost-efficiency goals of the... final rule. The establishment of a separate cost center would impose financial and administrative burden on the PHA...”

In regard to the alternate method, housing authorities should be allowed to spend their money at the project level as they choose. There is no limit placed on administrative costs at the project level for any other housing authority. A recently built elderly property with few maintenance needs may not need to spend a specific amount on maintenance costs, as the alternate method requires. It may need more administrative personnel to help the elderly deal with their paperwork and issues that might arise if there are young disabled included. HUD should not make this decision from Washington as it has done. PHADA does not believe small PHAs with one AMP should be required to meet a HUD-imposed administrative threshold.

The guidance states that small housing authorities that convert to asset management using the alternate asset management model are not eligible for the \$2 PUM asset management fee. For agencies with one AMP, since all of the money is being spent on the project, it appears irrelevant whether the agency has adopted a COCC or the uses the alternate asset management system. For agencies with more than one AMP, HUD’s adoption of the alternative asset management system indicates that this method satisfies an authority’s conversion to asset management. Since the authority using this method has converted to asset management, it does not appear to PHADA that there should be a distinction between these two methods of such importance that one earns the \$2 PUM asset management fee and the other does not. PHADA asks HUD to provide all small housing authorities which convert to asset management with the \$2 PUM asset management fee.

Section Eight: Need for flexibility to cope with funding shortfalls

A. Effect of a 74 percent proration in 2007

Based on HUD's 2007 budget request, PHADA is projecting that the 2007 proration will be 74 percent. It has shared this estimate with Department and OMB officials. In addition, if utility costs in 2007 equal the eligibility amount for utilities, the proration for all other housing authority expenses would be 57 percent.

There are two conclusions to draw from this scenario. The first is that since the rule states that "formula expenses represent the costs of services and materials needed by a well-run PHA to sustain the project" (990.160(a)) the inadequate provision of formula expenses by the Department and Congress calls into question the ability of authorities across the country to sustain well-run projects.

The second conclusion is that housing authorities cannot necessarily do everything "like it is done in multifamily" with only 74 or 57 percent of the funding. The multifamily programs will continue to receive full funding as they manage their properties in 2007. Public housing will receive an amount dramatically lower than full funding levels. Therefore, HUD should not automatically reject a public housing decision because "it is not done like it is done in multifamily."

The inadequate funding level argues that housing authorities need flexibility in managing their operations. This flexibility should be applied to both the deadlines applied to the conversion of asset management and the operational standards set by the Departments, such as the fee schedules.

In terms of time, no one questions that converting to asset management costs a considerable amount of money. With a 74 or 57 percent proration, it is obvious that money is a problem for housing authorities. They are not even being provided the same amount of money as multifamily to carry out operations, much less the additional money needed to convert to asset management. Without adequate money, it may be hard for housing authorities to meet the deadlines in the rule.

Housing authorities cannot necessarily do everything "like it is done in multifamily" with only 74 or 57 percent of the funding. The inadequate funding level argues that housing authorities need flexibility in managing their operations.

As previously argued, housing authorities should not have to adhere to the property management fee schedules until 2011, and the lack of funding is even another reason why this date, rather than the 2008–2009 one, should be used. Housing authorities simply will not be provided the money to undertake the planning, training and reorganization necessary to comply with property management fee schedules based on multifamily prior to 2011.

With funding at these levels, housing authorities are also going to have to take close looks at their organizations. Take a housing authority with 1,000 units and 10 properties of 100 units each. This housing authority might wish to develop a staffing pattern modeled on multifamily by placing a property manager at each of the 10 properties, who would handle maintenance supervision, with one regional manager for a total of 11 employees.

At these projected funding levels, though, the housing authority may simply not be able to afford this multifamily-based staffing pattern. Instead, to retrench, it might decide to adopt a different organizational structure. Based on its funding, it might choose to have four property managers, two managing two of the properties and two managing three. The authority would add an additional regional manager to assist them. Since this authority has gone down from 10 property managers to 4, it decides to remove the maintenance function from the property managers' responsibilities and creates a central maintenance department with a supervisor.

Under this organization, the authority has reduced its employees from 11 to 7, allowing it to function under the reduced proration. On the other hand, though, it has increased the staff that must be paid out of the management fee from 1 to 3. Since the management fee is based on the multifamily structure, fully funded, it is not adequate to support the three central office employees this authority has to adopt in order to manage its properties under HUD's funding level. Therefore, because of the inadequate funding level, this authority needs flexibility in its management fees to manage its resources as best it can.

PHADA does not believe that at these funding levels, HUD can adhere strictly to a standard of managing property "as it is done in multifamily." It needs to be flexible both in the time frames in which it expects asset management goals to be met and in determining what a "reasonable" management fee is. PHADA specifically asks HUD not to apply its property management fee schedules until 2011 and consider waiving them after this date if funding levels continue to fall below those provided multifamily properties.

PHADA reminds the Department that 990.280 (b)(2) states "Provided that the PHA complies with GAAP and other associated laws and regulations pertaining to financial management (e.g. OMB Circulars), it shall have the maximum amount of responsibility and flexibility in implementing project-based accounting."

The Department itself has cited the fact that the introduction of the "reasonable" property management fee falls under 990.280 in the rule, "Project-based budgeting and accounting." PHADA reminds the Department that 990.280 (b)(2) states "Provided that the PHA complies with GAAP and other associated laws and regulations pertaining to financial management (e.g. OMB Circulars), it shall have the maximum

amount of responsibility and flexibility in implementing project-based accounting.” Thus, PHADA believes the rule supports the request for “the maximum amount” of flexibility in determining “reasonable” property management fees that PHADA is making.

B. Extend the exemption from asset management to housing authorities with 500 units or fewer

Asset management should not be mandatory for agencies managing between 250 and 500 units. Conversion to asset management should be based on local discretion for housing authorities with 500 or fewer units because requiring conversion risks reducing efficiency and effectiveness for small agencies without compelling benefits. Every such agency would retain the option to convert to asset management where it is in the best interests of the properties.

Conversion to asset management should be based on local discretion for housing authorities with 500 or fewer units because requiring conversion risks reducing efficiency and effectiveness for small agencies without compelling benefits.

The Operating Fund Final Rule (Federal Register Sept. 19, 2005) exempts housing authorities with fewer than 250 units from an asset management model (24 CFR 990.260).

This threshold should be expanded to agencies with 500 or fewer units. This change would affect 441 agencies, or about 14 percent of the housing authorities. Subpart H of the Final Rule, section 990.275, states that “the arrangement or provision of services must be done in the best interests of the property, considering such factors as cost and responsiveness.”

Based on these criteria, project-based management may not be in the best interests of the properties for agencies with 500 units or fewer.

- A. These small agencies have few properties, few staff and few financial resources.
- B. They are already well run as a rule.
- C. Since each of these agencies generally manages only a handful of properties, individual property performance is well understood.
- D. It is generally more economical to manage them *as a single entity* rather than breaking them up into *multiple components*.
 1. The Harvard cost study found it was less expensive to manage larger properties than smaller ones.
 - a. Staffing, purchasing and management can be done more efficiently centrally in agencies with few properties that cannot support site staff.
 - b. Decentralizing these agencies may create costly and inefficient duplication of work, services and staffing.
 - c. HUD essentially recognizes the need to consolidate groups of properties

- of this size in its shared resources concept.
2. These agencies are often in small communities so they are easily managed as a single entity geographically.
- E. If the exemption is expanded to 500 units, these 441 agencies would not have to comply with burdensome new HUD regulations whose micromanagement will cost them money and reduce their efficiency. HUD has already acknowledged that conversion to asset management is a burden to smaller PHAs (Federal Register, p. 52713).
 - F. HUD's efficiency would be improved as well as it would not have to monitor conversion for 441 agencies.

C. Reserves for the central office cost center

HUD has placed a restriction of six months on the amount of reserves which can be placed in the central office cost center. This decision is made with no explanation. No restriction has been placed on the amount of reserves which can be placed at a property.

Reserves reflect the management of a housing authority since its inception. There is no way to tell at this point which property or cost center at a housing authority produced these reserves. Thus, there is no way to divide them up based on how they were actually created.

HUD has therefore taken a very arbitrary step in restricting the amount of reserves which can go into the COCC. There is no actual basis for this decision, and it removes the discretion of the housing authority in making this decision.

HUD has made a conscious decision to restrict the amount of money which can go to the COCC. This decision reflects its notion that money spent at the COCC is not money well spent, and it has substituted its judgment for that of the local officials who are in the best decision to determine the division of the reserves.

HUD has never explained the basis for its idea that money at the COCC is not wasteful. It should provide this explanation before implementing a restriction on COCC reserves. PHADA has gone to some length to explain the differences between the properties in the FHA database and public housing properties that HUD has not recognized in its determination of property management fee schedules. Since HUD's fee schedules do not provide a "reasonable" property management fee for public housing properties, it is even more important that the central office have an adequate reserve level. Therefore, PHADA asks the Department to remove the restriction on the amount of reserves which can be placed in the COCC and allow this decision to be made where it can best be done—by each individual housing authority.

PHADA also points out that since, at a 74 percent proration, many properties may not be able to fund an asset management fee, housing authorities may need to pay these fees out of the COCC reserve. Simply because funding may not be available for these asset management fees does not mean that the work of asset management will not have to be done. Since it has to still be done, the COCC reserves may be one of the few sources available to cover these costs. Given HUD's funding inadequacy, then, it should not place a restriction on the amount of reserves which can be placed in the COCC.

Section Nine: Rulemaking through notices

A. Formal notice and comment required

Although PIH Notice 2006-33 invites comments, PHADA is concerned that HUD has been instituting rulemaking through notices without opportunity to comment. In particular HUD has issued guidance on property groupings (PIH Notice 2006-10) and stop-loss criteria (PIH Notice 2006-14) without adequate opportunity for housing authorities and other interested parties to provide their input.

Notice 2006-14 institutes many new criteria on the characteristics that define whether or not a property is performing that may impact a housing authority's funding. These include criteria on energy use and security as well as new thresholds for physical condition. HUD has then further changed these criteria in its frequently asked questions.

HUD has implemented other portions of the rule, such as the utility inflation factor, without comment and contrary to instructions from the Bureau of Labor Statistics.

As PHADA believes the implementation of asset management is a question of considerable importance for housing authorities, and as it is not satisfied that HUD has been following the rule or taking valid industry input into consideration, PHADA urges the Department to follow the example it has used in regard to PIH Notice 2006-33 and offer housing authorities a chance to review and comment on decisions which will be vital to their ability to manage the nation's low-income public housing program.

B. Defederalization

While PHADA believes defederalization could be beneficial to housing authorities, it believes HUD should provide HAs with a stronger authorization than provided in this notice. PHADA would like to see the written approval OMB has provided to exempt these funds from 24 CFR Part 85 and OMB Circular A-87. It also believes that a determination of this magnitude should be part of a rule, and not just a notice. Housing authorities need to be protected from the risk of being criticized and sanctioned at some later date for having taken actions based on a simple notice that regulators, such as the Inspector General, might construe as conflicting with other requirements, such as OMB Circular A-87. The rule itself (990.280 (b)(2)) specifically calls for housing authorities to comply with OMB circulars.

PHADA would also like some assurance that Congress approves of defederalization. History has shown, with the Section 8 administrative fees, that Congress can lay claim to the amount remaining between a fee and the actual expenses of performing the service paid for by the fee. As a result, housing authorities need to know whether Congress is prepared to let housing authorities retain and use this amount, before running the risk that legislators may reclaim it at a later date.

The issue of defederalization also relates to HUD's intention to peg public housing funding on "actual costs" at some date in the future. If housing authorities operate their properties for several years at a lower cost than provided in their fee structure, taking advantage of the concept of defederalization to provide money for other af-

fordable housing purposes, will their fee structure be reduced commensurately when funding is set at an “actual cost” level? If that action is a possibility, housing authorities would have little incentive to try to take advantage of defederalization for a few short years only to see their funding reduced permanently. HUD should clearly state that fees will not be affected by defederalization if HUD moves to an “actual cost” basis of funding public housing in the future.

Housing authorities need to be protected from the risk of being criticized and sanctioned at some later date for having taken actions based on a simple notice that regulators, such as the Inspector General, might construe as conflicting with other requirements, such as OMB Circular A-87.

Having expressed its concerns, though, PHADA, as mentioned, believes that defederalization can be beneficial and as a result questions why it only applies to the management fees and not to the property expense level. HUD’s rationale for defederalization is that the property management fees pay for a specific service and are based on the private sector’s market rate. Since the fees are market costs, if a housing authority can perform the service less expensively than the market, it should be able to retain the difference.

Similarly, HUD is providing housing authority a set amount of money for administering a public housing property. This amount is “reasonable” based on the operating cost of similar properties in the private sector, represented by the FHA database. In this sense, the property expense level (PEL) represents a fee for service based on the private sector for administering public housing property, in the same way that HUD has said that the property management fee represents a “reasonable” fee for managing the property based on the private sector.

Since the concept is the same—HUD providing a fee for performing a task—and since the method for developing the fee is the same—based on the FHA database—PHADA believes that the concept of defederalization could be extended to include the property expense level. If a housing authority can administer its public housing property for less than the fee HUD provides, based on the private sector’s market rate, the remaining money should be exempt from 24 CFR Part 85.

A similar concept is already in use in the Moving to Work program. These agencies are given a certain amount of funding to house a set number of families. If they spend less funding than HUD provides housing these families, they can use the remaining amount in a variety of creative ways, depending on their contracts with HUD and their annual and five-year plans.

Section Ten: PHAS

HUD has announced that it plans to revise PHAS. PHADA believes there are many important questions that need to be addressed in such a revision. It believes first and foremost that housing authorities and the industry groups which represent them must be a part of such a revision. Therefore, it asks the Department to include them from the beginning in any discussions taking place on a revision to PHAS. HUD has informed PHADA that plans for this revision are already being drafted, but no attempt has been made as of yet to bring housing authorities into this process. It is not too early to include them and it may be too late if the Department brings them in only when it has completed its deliberations.

One of the important issues is whether agencies will continue to receive a score. Equally important is the relationship between the agency and the property. If an individual property fails an evaluation, but the agency as a whole is well-run, would the same sanctions be applied to a property as they would if the agency as a whole were troubled? If there is no agency score, will the property's relative importance to the agency be considered? If an agency manages 100 properties and only one is found to be a non-performer, will that relatively insignificant proportion affect the Department's position in regards to the property? Clearly, the agency knows how to manage public housing property since 99 out of its 100 properties are performing well. Would it make sense to sanction this agency, by removing its management responsibilities for example, as quickly as the Department might sanction an agency in which one out of three of its properties was non-performing?

If HUD applies sanctions on the property level, it will be providing stricter sanctions than currently exist. A property can now score a 55 on the physical assessment without causing the agency to face sanctions, if its overall score is above 60. Initiating sanctions on the basis of a score of 55 at one property is imposing a new standard above and beyond the current one.

PHADA is not offering suggestions to answer these questions at this time. It cannot comment on HUD's revisions to PHAS without knowing what those revisions will be. It does believe, though, that HUD needs to take into account the relationship between the property and the agency as it proceeds.

PHADA does not see why housing authorities should be evaluated by a different standard than the one applied in the multifamily program.

Similarly, HUD needs to consider the indicators it will include. As asset management is based on multifamily norms, it appears logical that the evaluation should be similar to HUD's evaluation of multifamily properties. In some cases, applying these norms may require statutory changes, since some indicators used for public housing but not for multifamily are included in QHWRA. PHADA does not see why, though, housing authorities should be evaluated by a different standard than the one applied

in the multifamily program. To the best of PHADA's understanding, these properties do not receive a formal evaluation on their financial status or management performance nor do they have a resident survey. PHADA believes HUD should also take this approach in its public housing assessment system.

If HUD continues to use a financial and management indicator, despite the fact that they are not used in the multifamily program, it will need to take several factors into account. First of all, the Harvard cost study had a 42 percent plus or minus error rate when establishing the PEL at individual properties. Therefore, many properties will not receive the funding needed to manage well-run public housing. This fact must be included in any discussions. Similarly, the question of peer groups will also need to be reevaluated. Is a 100-unit property in a 30,000-unit PHA a peer of a 100-unit property in a 300-unit PHA? Is a property-level reserve as critical when funding is fungible from all other properties with excess cash? What will happen to the entity-wide portion of the financial indicator?

Similarly, would each housing property be evaluated on its commitment to resident economic self-sufficiency? Would there be some indicators that were agency-wide and some that were property-wide?

A final issue that PHADA believes needs to be addressed is the relationship between the evaluation and HUD's funding level. Housing authorities are going into 2007 facing a possible proration around 75 percent. Public housing's funding is based on the properties in the multifamily program. With a proration at this level, housing authority properties will be receiving far less funding than their multifamily counterparts.

A very important question, then, is what are the expectations of a property which receives inadequate funding? Should HUD expect a public housing property with a 75 percent proration to meet the same physical standard of a multifamily property that receives its full funding? PHADA would like the Department to explain how this feat can be accomplished if the answer is yes.

Standards of performance, such as unit turnaround time, work order completion rates, and inspection percentages, will also be directly affected by a lack of funding. The rule states that the formula is the amount needed to manage well-run housing. It follows, then, that when the formula is not met, the standard of well-run housing is put in doubt. Something has to give at a 75 percent proration. PHADA believes that the Department must make an adjustment in PHAS to compensate for its inability to provide housing authorities with the same amount of money it provides properties in the multifamily program.

Conclusion

These comments have been lengthy because the conversion of asset management is an extremely important subject to housing authorities which will affect them for years to come.

Perhaps the most important fact for the Department to remember is that there is time to develop the best possible guidance, as the conversion to asset management is not scheduled until 2011, five years from now.

In the course of developing this guidance, PHADA has worked closely with the Department. To its credit, HUD has adopted many industry suggestions and modified its original proposals. In virtually every area raised in these comments HUD's guidance has changed over time in response to feedback it has received. Major changes have been made in the areas of property management and bookkeeping fees, assignment of costs, distribution of capital funds, calculation of excess cash, evaluation of small housing authorities, and even rulemaking through notices, as the Department has now officially requested comments.

There is still time to develop the best possible guidance. The conversion to asset management is not scheduled until 2011, five years from now.

With this history, there should be no reluctance on the Department's part to continue to review and absorb input just as PHADA continues to assume that even though all of its suggestions have not been accepted, its ideas are still weighed carefully. PHADA has taken the time to submit comments at this level of detail because it takes the Department at face value when it says the dialogue is still open and because the Department has shown over the past year it is prepared to listen. In these comments, PHADA has made a special effort to go beyond criticism and provide constructive suggestions on many of the issues it believes still need further work.

Although PHADA has made some of the observations here either in meetings or in written communications, it has not had the opportunity to present its positions as completely or as officially. It hopes the Department, too, will now take the time to review these ideas more deliberately and more formally.

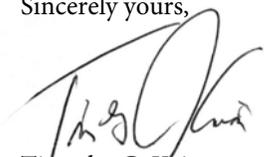
To conclude, PHADA believes each of the three fees fails to reflect fully multifamily practice and in so doing they fall short of treating housing authorities comparably and meeting the rule's standard of "reasonable." It believes restrictions on the capital fund violate the law. It objects to HUD's micromanagement in its assignment of costs and thinks many of the requirements contradict the rule. It insists on emphasizing that the rule calls for "maximum flexibility," especially important in the light of the chronic operating fund shortfalls housing authorities are experiencing.

Finally, it urges the Department to remember that there is sufficient time to continue deliberating these matters and to carry out the research necessary to arrive at a

system that will be fair, accurate and helpful to housing authorities, the residents they serve and the taxpayers who provide the funding for this vital national resource.

Thank you for your consideration of these comments.

Sincerely yours,

A handwritten signature in black ink, appearing to read 'Timothy G. Kaiser', written in a cursive style.

Timothy G. Kaiser
Executive Director

Index

Page numbers in italics refer to tables.

- add-ons, 4–9, 15, 17, 32, 53
- asset management fee, 29–35, 51, 54, 58
- asset management project, 38, 45, 47, 53, 54
- Board of Commissioners, 49
- bookkeeping fee, 3, 20–28, 63
- Capital Fund, 30, 36–39, 51, 63
- Capital Fund Financing Program, 38
- central office cost center, 34, 36, 39, 46, 48, 51–52, 53–54, 58
- contract administrators, 29–35, 30
- defederalization, 59–60
- eligible purposes, 51–52
- energy service contract, 52
- excess cash, 3, 50–52, 62, 63
- Federal Register, 1, 36, 54, 57, 58
- FHA database, 3–5, 9, 15–19, 20–23, 26–28, 33, 49, 53, 58, 60
- field office fee schedules, 3, 5
- Financial Management Handbook, 3, 16, 20, 29, 32, 33, 36, 51, 53
- front line, 20, 22, 26, 38–39, 40–49
- fungibility, 51, 52
- GAAP, 56
- Harvard cost study, 3, 5, 6, 9, 17–18, 23, 26, 27, 29–31, 30, 33, 44, 45, 50, 57, 62
- human resources, 20, 27
- inflation, 12, 13, 59
- information technology, 7, 20, 26–27
- inspection, 32, 47, 62
- Inspector General, 30, 43–44, 59
- limited dividend properties, 3–4, 32, 33
- maintenance supervisors, 44–47
- Management Agent Handbook, 4, 5, 12–13, 16, 17, 20, 26, 46, 47, 49
- management improvements, 36, 39
- micromanagement, 39, 44, 48, 58, 63
- mixed finance, 10, 15–16, 34
- non-profit properties, 17, 22, 24
- Notice 2006-14, 29, 30, 59
- Notice 2006-33, 1, 59
- Office of Public and Indian Housing, 43
- OMB, 7, 15, 18, 55, 56, 59
- OMB Circular A-87, 7, 18, 59
- operating fund rule, 1, 3, 10–12, 14, 15, 22, 29–30, 30, 32, 34, 39, 40–48, 50–52, 54, 55–57, 57, 59, 62
- procurement, 7, 27, 40, 43, 44
- project-based accounting, 10, 47, 57
- project-based management, 10–12, 57
- property expense levels, 3, 13, 23, 28
- property management fee, 3–19, 22–25, 28, 32–33, 36, 40, 47, 53, 55–56, 58, 60
- proration, 34, 45, 55–57, 58, 62
- Public Housing Assessment System, 6, 30, 61–62
- QHWRA, 36–37, 61
- regulatory and operating differences, 6–7, 17–18
- reserves, 58
- rulemaking, 33, 42, 47, 48, 51, 59, 63
- small housing authorities, 48, 53–54, 63
- stop-loss, 12, 18, 30, 59
- tax-credit, 16, 33
- unlimited dividend properties, 3, 21, 22–23