DEPARTMENT OF AGRICULTURE

Rural Housing Service

Rural Business-Cooperative Service

Rural Utilities Service

Farm Service Agency

7 CFR Part 1944

RIN 0575–AC15

Rural Rental Housing (RRH) Assistance

AGENCIES: Rural Housing Service, Rural Business-Cooperative Service, Rural Utilities Service, and Farm Service Agency, USDA.

ACTION: Final rule.

SUMMARY: The Rural Housing Service (RHS), formerly Rural Housing and Community Development Service (RHCDS), a successor Agency to the Farmers Home Administration (FmHA), amends its regulations for the Rural Rental Housing (RRH) program. This action is taken to implement legislative reforms mandated by the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 1997, Pub. L. 104–180, enacted August 6, 1996, and to implement Pub. L. 105–86, enacted November 18, 1997, which amends the maximum loan term for Section 515 loans from 50 years to 30 years. The intended effect of these reforms is to improve the effectiveness and efficiency of the Section 515 RRH program.

DATES: The effective date of this final rule is January 22, 1998.

FOR FURTHER INFORMATION CONTACT: Linda Armour or Carl Wagner, Senior Loan Specialists, Multi-Family Housing Processing Division, RHS, U.S. Department of Agriculture, Room 5349—South Building, Stop 0781, 1400 Independence Ave., S.W., Washington, D.C. 20250–0781, telephone (202) 720–1608.

SUPPLEMENTARY INFORMATION:

Classification

This rule has been determined to be not significant for purposes of Executive Order 12886 and therefore has not been reviewed by the Office of Management and Budget.

Paperwork Reduction Act

The information collection requirements contained in this regulation have been previously approved by the Office of Management and Budget (OMB) under the provisions of 44 U.S.C. chapter 35 and have been assigned OMB control number 0575–0047, in accordance with the Paperwork Reduction Act of 1995. Under the Paperwork Reduction Act of 1995, no persons are required to respond to a collection of information unless it displays a valid OMB number. The valid OMB control number assigned to the collection of information in these final regulations is displayed at the end of the affected section of the regulation. This rule does not impose any new information collection requirements from those approved by OMB.

Civil Justice Reform

This rule has been reviewed under Executive Order 12988, Civil Justice Reform.

In accordance with this rule: (1) all state and local laws and regulations that are in conflict with this rule will be preempted; (2) no retroactive effect will be given to this rule; and (3) administrative proceedings in accordance with 7 CFR part 11 must be exhausted before bringing suit in court challenging action taken under this rule.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Pub. L. 104–4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, RHS generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with ''Federal mandates'' that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of $100 million or more in any one year. When such a statement is needed for a rule, section 205 of the UMRA generally requires RHS to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule.

This rule contains no Federal mandates (under the regulatory provisions of Title II of the UMRA) for State, local, and tribal governments or the private sector. Therefore, this rule is not subject to the requirements of sections 202 and 205 of the UMRA.

National Performance Review

This regulatory action is being taken as part of the National Performance Review program to eliminate unnecessary regulations and improve those that remain in force.

Programs Affected

The affected program is listed in the Catalog of Federal Domestic Assistance under Number 10.415, Rural Rental Housing Loans.

Intergovernmental Consultation

For the reasons set forth in the Final Rule related Notice to 7 CFR part 3015, subpart V, this program is subject to Executive Order 12372 which requires intergovernmental consultation with State and local officials. RHS has conducted intergovernmental consultation in the manner delineated in RD Instruction 1940–J.

Environmental Impact Statement

This document has been reviewed in accordance with 7 CFR part 1940, subpart G, ''Environmental Program.'' It is the determination of RHS that this action does not constitute a major Federal action significantly affecting the quality of the human environment and in accordance with the National Environmental Policy Act of 1969, Pub. L. 91–190, an Environmental Impact Statement is not required.

Background

On August 6, 1996, Congress enacted the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 1997, Pub. L. 104–180 (herein referred to as the Act). The Act included six reforms to the multifamily housing (MFH) program, which the Agency was directed to implement without delay. Four of the six reforms were directive and could be implemented as enacted without the need for public comment. However, public comment was needed for the other two reforms, which provided for substantive changes in the manner in which MFH loan requests are processed and gave the Secretary administrative discretion in their implementation. Because of the mandate to implement the reforms immediately, the rule was published as an interim final rule on May 7, 1997 (62 FR 25062), effective upon publication. The rule included a 60-day comment period, which ended on July 7, 1997.

Discussion of Comments

A total of seventeen written comments were received from developers, nonprofit groups, Rural Development staff, members of Congress, and state housing agencies. The Agency appreciates the time and effort that went into these comments, many of which offered detailed and constructive suggestions.

Several commentors expressed their support for the four directive reforms,

which have been adopted without change in this final rulemaking document:

(1) Assurance That Project Transfers Are in the Best Interest of the Tenants and the Government

Two commentors indicated support for the provisions pertaining to project transfers. One stressed the importance of maintaining the Agency's inventory in good condition to avoid health and safety problems.

(2) Elimination of the Occupancy Surcharge

Two commentors indicated their support of this legislative change. One suggested that the monies collected prior to the elimination of the surcharge be used for other program opportunities such as funding the Section 538 program or for servicing rental assistance (RA), if not returned to the properties. The Agency will consider these recommendations on this issue.

(3) Changes to the Equity Loan Program

Two comments were received on the equity loan program. One indicated support for the legislative changes and noted that the Agency has not yet established an office of rental housing preservation which would make decisions relative to prepayment and incentives, as authorized by section 537 of the Housing Act of 1949. The second commentor expressed the opinion that the preservation of low income housing stock could not be accomplished without significant financial incentives for borrowers and predicted that new approaches to the prepayment issue would be forthcoming from the courts or Congress in the near future.

(4) Implementation of Penalties for Equity Skimming by Project Owners and Managers

Two commentors indicated their support for this legislation. One urged the Agency to act quickly in pursuing parties who abuse the program to the detriment of residents and other borrowers.

The majority of the comments on the interim final rule addressed the two reforms that included administrative discretion in their implementation: (1) Prioritization of assistance and (2) assurances that the amount of assistance provided is no more than necessary. Based on comments received, several minor changes have been made in the final rule.

(1) Prioritization of Assistance

Sections 1944.228, ''Ranking of rural places based on greatest need for Section 515 housing,'' and 1944.229, ''Establishing the list of designated places for which Section 515 applications will be invited,'' were added to 7 CFR part 1944 to implement the statutory requirements pertaining to prioritization of Section 515 assistance. The statute directs the Secretary to identify and designate rural areas with the greatest need for Section 515 housing, taking into consideration the incidence of poverty, the lack of affordable housing and existence of substandard housing, the lack of mortgage credit, the rural characteristics of the location, and other factors determined by the Secretary that demonstrate the need for affordable housing.

Section 1944.228 of the interim rule provides that places will be ranked as follows: Places must qualify as rural areas in accordance with 7 CFR 3550.10, lack mortgage credit for borrowers in accordance with § 1944.211(a)(2), and demonstrate a need for multifamily housing based on the following factors, with equal weight given to each: the incidence of poverty, measured by determining households below 60 percent of the county rural median income; the incidence of substandard housing, measured by determining the number of occupied housing units lacking complete plumbing or having more than one occupant per room; and the lack of affordable housing, measured by determining households below 60 percent of rural median income who are paying more than 30 percent of income in rent.

Twelve commentors addressed the provisions of § 1944.228 and offered thoughtful suggestions for modifying the ranking system. Specific areas addressed were:

Ranking Factors

Several commentors felt the ranking factors should be expanded. One commentor suggested using additional factors such as the availability of existing subsidized housing, the number of vacancies in existing subsidized housing, demand, the availability of services, the anticipated growth of the area, and the availability of adequate utilities. We agree that these factors need to be considered and, in fact, they are taken into consideration, either in the selection of ranked places for the designated place list or in the market feasibility determination. For example, after places have been ranked using the Census data, the list is reviewed to determine if any of the ''build and fill'' conditions exist, one of which is a high vacancy rate in existing RHS or similar assisted rental units. Places with any ''build and fill'' condition may not be included on the designated place list; they are deferred until the condition no longer exists. The other recommended factors (demand, anticipated growth, availability of housing, services, and utilities) are part of the market feasibility determination. The Agency believes this is the most effective way to take these factors into consideration. It would not be feasible to obtain and maintain current market data on all rural communities for inclusion in the initial ranking process.

Weights of the Ranking Factors

Three commentors felt the formula provided an advantage to larger rural communities and two of these expressed the opinion that the Agency should consider percentages instead of raw numbers to give smaller rural communities a better opportunity to compete. In fact, the formula used by the Agency, which was not published in the **Federal Register**, considered both raw numbers and percentages. A ranking score was assigned to each place for the three factors (income, rent overburden, and substandard housing) based on the percentage of its total households and on the actual number of households or substandard units. Each score for these six rankings was totaled to reach a final ranking score. This method targets communities that demonstrate a high potential need for housing assistance both by raw numbers and high percentages of their total households. This has resulted in a good mix of small to mid-size rural communities, and we plan to continue with this methodology.

One commentor suggested giving less weight to substandard housing; another suggested giving more weight to rent overburden. We considered these suggestions and ran data for several States with the adjusted factors. The results were inconclusive and we feel that, in the absence of supporting data or documentation, it would be premature to make changes in the formula. We intend to leave the weights unchanged for the remainder of the 3-year designated place cycle but will continue to evaluate the benefits of modifying the formula for future cycles.

Use of 60 Percent of County Rural Median Income

Two commentors disagreed with the Agency's use of 60 percent of county rural median income to determine households in poverty. One commentor suggested using 80 percent; the other felt strongly that 30 percent more closely represented households in poverty, and thus areas of greatest need,

as required by the statute. The Agency has compared the various percentages of county rural median income in several states to the National poverty figure. Based on our review, we agree that 30 percent more closely approximates the National poverty figure. As a result, ranking will be based on households at or below 30 percent of county rural median income. The ranking data has been calculated for all States based on this figure and will be used to select any additional designated places. Places that are currently on the designated place list will remain on the list for the remainder of their 3-year designation period, or until removed or deferred in accordance with § 1944.229(d). The revised ranking data and list of designated places are discussed further in the ''Implementation Proposal''.

Adding Counties to the Ranking List

Two commentors suggested the Agency rank counties as well as communities. This is an issue that was considered at length in the development of the interim final rule. Because the statute mandates the Secretary to identify and target areas of greatest need, we felt that a county-wide designation was too broad, since the needs of the communities within a county can vary widely. If an entire county were designated, an applicant might well choose areas that have higher incomes and less substandard housing, even though the true need for housing may be greater in another community. We believe it is necessary to identify and designate specific communities to ensure that funds are directed to areas of greatest need and, therefore, we have not revised this provision.

Flexibility in the Ranking Factors

Eight commentors felt the ranking factors should allow more flexibility for state and local conditions. This is another issue that was discussed at length in the development of the interim final rule. We recognize that conditions and goals vary from state to state; however, we believe it is critical to maintain National standards for program consistency. In addition, it would be difficult for States to obtain objective data that could be added to the ranking formula. Instead of providing flexibility in the ranking factors, we provided flexibility in the selection of designated places. This was accomplished in the regulation by allowing States to select places from further down the ranking list, but still within the top ranked, that have been identified as high need areas in the state Consolidated Plan or state needs assessment. To provide further flexibility, we have included provisions in the final rule for States with an active state leveraging program. Details are given below under the heading ''Designated places for States with an active state leveraging program''.

As published in the interim final rule, § 1944.229, ''Establishing the list of designated places for which Section 515 applications will be invited'', provides that the number of designated places may equal up to 5 percent of the State's total eligible rural places but must equal, in all cases, at least 10 places. To be included on the list of designated places, a place must have 250 or more households as a minimum feasibility threshold for multifamily housing and may not have any of the ''build and fill'' conditions specified in § 1944.213(f)(2). Places that meet the minimum size threshold and do not have any ''build and fill'' conditions are then selected in rank order to form the list of designated places. This section provides the flexibility for States, with National Office concurrence, to select up to 10 percent of their designated places to provide geographic diversity or to reach high need areas, provided such places are within the top-ranked 10 percent of the state's total rural places.

Nine commentors addressed the provisions of § 1944.229 in the following areas:

Establishing the Number of Designated Places

Five commentors felt that the limit of 5 percent of the state's total eligible rural places was too restrictive and did not provide sufficient diversity. Recommended percentages ranged from 10 to 20 percent. One commentor recommended a percentage of places equal to 25 percent of the state's total rural households. An analysis of several states showed that the latter suggestion was equivalent to approximately 10 percent of the states' total rural places. We reviewed the ranking data for several States and found that there was little difference in the ranking scores between places that rank in the top 5 percent compared to those within the top 10 to 20 percent, simply because of the volume of places being ranked. Therefore, a small increase in the percentage of designated places will still target the neediest communities. Accordingly, the 5 percent limit has been modified in the final rule to allow States to designate up to 10 percent of their total eligible rural places. In addition, based on comments that expressed concern that Indian reservations, colonias, Empowerment Zone and Enterprise Communities (EZ/ECs), and Rural Economic Area Partnership (REAP) communities were frequently not included on the list of designated places, the final rule provides that States may designate these special high-need areas in addition to their 10 percent or minimum 10 places.

Build and Fill Conditions

Three commentors mentioned their support for ''build and fill'', which is widely understood to mean that no additional Section 515 housing will be approved if other Section 515 or similar assisted units have been approved, are under construction, or not yet filled. However, the ''build and fill'' provisions include other conditions which indicate that the market does not currently need additional rental housing: existing Section 515 or similar assisted housing units are experiencing high vacancies; a request for a Servicing Market Rate Rent (SMR) is pending or in effect and still needed; or the need in the market area is for additional rental subsidies and not for additional housing units. Places with any of these conditions may not be included on the designated place list. States are responsible for reviewing their ranking list, consulting with HUD and other housing agencies, and deferring places with ''build and fill'' conditions. In response to the comments we received recommending that the Agency consider these or similar market factors in the ranking data, we believe the provision which defers places with ''build and fill'' conditions accomplishes just that. One commentor noted that places were listed on the designated place list with high vacancies in assisted housing complexes. Any such instances should be brought to the attention of the RHS State office staff for their review. The Agency will continue to stress the importance of reviewing the designated place list annually for ''build and fill'' conditions. Another commentor recommended including low income housing tax credit (LIHTC) units in the definition of assisted housing complexes for purposes of ''build and fill''. We agree and have added a specific reference to LIHTC units in the ''build and fill'' provisions in § 1944.213(f)(2).

Minimum Number of Households for Designated Places

Four commentors objected to the requirement that designated places have a minimum of 250 households and noted that market demand should be the determining factor, not an arbitrary size requirement. We agree that market demand should determine project feasibility; however, we feel that places

with fewer than 250 households rarely have sufficient demand or the support services necessary for multifamily complexes. We believe it is prudent to maintain a National feasibility standard and, therefore, have retained this provision. We have also retained the ability for States that have been successful in developing and operating multifamily units in very small communities to request an exception from the National Office to establish a lower state-wide feasibility threshold. In addition, based on concerns that Indian reservations are sometimes excluded because households are frequently split between two or more communities within the same reservation, we have modified this provision to specify that, for Indian reservations, there must be 250 or more households on the reservation.

Designated Places for States With an Active State Leveraging Program

Eight comments were received from Rural Development State staff, state housing agencies, members of Congress, and applicants, urging the Agency to provide more flexibility for States with an active state leveraging program. It was noted that, in many cases, the areas targeted by the state agencies did not correspond to the RHS designated places. As a result, funds that had been set aside by state agencies for leveraging with RHS funds were not able to be fully used. The Agency is committed to partnering with other providers of resources; however, at the same time, we have a legislative mandate to designate rural areas of greatest need and to direct RHS funds to those areas. To accomplish both priorities, we have added provisions in the final rule to allow States with a formal state leveraging program and agreement with their state agency to develop a partnership designated place list with the state agency, which must be approved by the National Office. Places selected for the list must be high-need areas based on criteria consistent with the Agency's statutory requirements as well as the state's authorizing requirements. All loan requests (including those for places on the partnership designated place list) will be scored together as one group. In order of point score or, where there are point score ties, in order of point score and number assigned in accordance with § 1944.231(b)(3), two ranking lists will be formed: the RHS ranking list will include loan requests for places on the RHS place list, and the partnership ranking list will include loan requests for places on the partnership place list. Selection for further processing will be as follows: Loan requests must first be selected from the RHS ranking list that, based on total development cost (TDC), are proportionate to the State's RHS allocation. Loan requests will then be selected in order of highest point score (or point score and tie-breaker number), regardless of whether the loan requests are on the RHS ranking list or the partnership ranking list. For example, a State with a Section 515 allocation of $2 million has three loan requests on the RHS ranking list with point scores of 20, 9, and 5 respectively; and two loan requests on the partnership ranking list with point scores of 18 and 15. The first loan request that will be processed is the highest ranked proposal on the RHS list, with a point score of 20. This request has a TDC of $1.2 million, of which the RHS loan request is $500,000. The next request that will be processed is the second ranked proposal on the RHS list, with a point score of 9. This loan request has a TDC of $1 million, of which the RHS loan request is $750,000. The total amount of RHS funds requested for these two proposals ($1,250,000) is less than the RHS allocation of $2 million; however, the total TDC for the two requests equals $2.2 million, which exceeds the State's allocation. This satisfies the provision that loans must be funded in places on the RHS designated place list proportionate to the RHS allocation. Having satisfied this provision, the next loan requests will be selected in order of highest point score, regardless of whether they are on the RHS list or the partnership list. In this example, assuming there are sufficient funds remaining, the next loan request to be processed would be the 18-point request on the partnership list, followed by the 15-point request on the partnership list, and then by the 5-point request on the RHS list.

Section 1944.230 was added in the interim final rule to establish provisions on loan application submission deadlines and the availability of funds. This section specifies that the Agency will publish annually in the **Federal Register** a Notice of Funds Availability (NOFA), any limits on the amount of individual loan requests, the dates for the funding cycles, and the deadline for submission of loan applications.

Five commentors addressed this section. Two commentors expressed their support for the NOFA system; one commentor was opposed; the other two offered suggestions but did not indicate strong feelings one way or the other. One of the supporters felt the NOFA system was a very cost effective way for developers to participate in the program without having development money tied up for several years waiting for funds to become available. We agree, and would like to add that the decision to move to a NOFA system was reached with extensive input from the Section 515 stakeholders who participated in the development of the reform regulations.

The commentor who opposed the NOFA system felt that it: (1) Encouraged applicants to expend funds for proposals that might not materialize; (2) eliminated nonprofit applicants because they lack the time and money to put together an application; and (3) nearly eliminated leveraging because of the problems coordinating with partners. On the first issue, we believe the NOFA system will be more cost effective, not less, since applicants do not have to incur costs over a period of time waiting for funds to become available. The submission requirements for applicants are the same under the NOFA system as under the previous regulations, so the cost of submitting a loan request has not changed; the difference is that, under the previous system, applicants were required to maintain the site option and update the market and financial information annually and still were not guaranteed of funding because of the backlog of requests and limited availability of funds. Under the NOFA system, applicants know within a short timeframe whether their loan request has been selected. No further costs are incurred unless or until the applicant reapplies in the next funding cycle. As a point of interest, the Agency is reviewing the Section 515 submission requirements to determine if the initial cost to applicants can be reduced, for example, by modifying the initial market analysis requirements. These changes are being considered as part of the Agency's ''reinvention'' regulation, which is scheduled to be published for comment early in 1998. On the second issue, we do not believe the NOFA system precludes nonprofits from applying. In fiscal year 1997, the period of time for submitting applications was shortened because of the time involved in writing and publishing the regulations. However, in future years, the Agency will publish NOFA as early as possible in the fiscal year and provide a longer application period. In addition, places are designated for 3 years, so applicants can continue to develop applications prior to publication of NOFA. On the third issue of coordinating NOFA with other funding cycles, we believe this issue will also be alleviated by the publication of NOFA early in the fiscal year. The earlier publication of NOFA

will enable States to coordinate the RHS funding cycle with the state agency's funding cycle. Three other commentors on this section also mentioned the importance of coordinating with other funding cycles and publishing the NOFA as early as possible.

One commentor suggested adding a provision that a project must have full funding committed by the end of the fiscal year and must start construction within a specified number of days (270 was suggested) or lose its obligation. We agree that it is necessary to establish and enforce processing deadlines or timeframes and we are addressing this issue in the reinvention of the multifamily regulations.

Section 1944.231, processing loan requests, was revised in the interim final rule to incorporate processing procedures for the NOFA system and to add provisions for scoring and ranking loan requests under the new system. Six commentors addressed this section in the following areas:

Application Requirements

Two commentors discussed the application process and requirements. One suggested that the Agency develop a uniform application package and checklist to ensure that all applications are received in the same format and judged by compliance to that format. We think this is an excellent idea and are developing a checklist and administrative guidance on determining a complete application that will be provided to States concurrently with the publication of this rule. The other commentor objected to the elimination of the term ''preapplication'', believing this served no useful purpose and was changed merely for the sake of change. We adopted the term ''initial loan request'' (or ''initial application'') because we believe it to be more appropriate for the NOFA process, which is a one-step annual selection process instead of the two-step process previously used, in which preapplications were kept on hand until funds became available. We also feel the terms are more consistent with those used by other lenders.

Scoring Loan Requests

The interim regulation provides that loan requests will be scored based on five factors:

(1) The presence and extent of leveraged assistance (including services, abatement of taxes, etc.) for the units that will serve RHS income-eligible tenants, not including tax credits or donated land. (0 to 20 points)

Five commentors addressed this loan scoring factor. One commentor felt the Agency needed to quantify amounts for services and tax abatements; another felt the 0–20 point range was too subjective. The same commentor recommended that the Agency reexamine its decision to give points for leveraged assistance because the benefits of the leveraged funds might be offset by an increase in demand for rental assistance. Another commentor felt that leveraging should not dominate the scoring and suggested that the Agency consider several additional factors, which are discussed below in ''Other scoring factors''. One commentor said it was unclear whether tax credit funds were eligible to receive points for leveraging, and three commentors recommended that tax credit funds that are dedicated back to the project's development or operation or to tenant subsidies be eligible to receive points.

In response to the comment that the range of 0 to 20 points is too subjective, the Agency provided separate administrative guidance to RHS staff at the time the regulation was published to ensure that all loan requests were scored consistently. We also provided guidance on establishing a value for services and tax abatements. On the issue of whether tax credit funds may be considered leveraged assistance for purposes of awarding points, we agree that any funds the applicant contributes to the proposal in excess of his or her required contribution, including tax credit proceeds, should be eligible for consideration for points as long as there is an equal or positive impact on basic rents. We have modified this provision accordingly in the final rule. Regarding the demand for rental assistance (RA), we do not foresee a major impact on RA usage, especially with the increased interest in developing mixed-income complexes that require only partial RA.

(2) The loan request is for units to be developed in a colonia, tribal land, or EZ/EC community, or in a place identified in the state Consolidated Plan or state needs assessment as a high need community for multifamily housing. (20 points)

No comments were received on this loan selection factor; however, the Agency inadvertently omitted REAP (Rural Economic Area Partnership) communities in the list of high need areas in the interim final rule. This omission has been corrected in the final rule.

(3) The loan request is in support of a National Office initiative announced in NOFA. (20 points)

One commentor addressed this factor, expressing a concern that, without specific parameters, the factor could be used for politically motivated initiatives.

This factor was developed to ensure there is flexibility in the regulation for initiatives that are consistent with the statute that would enable the Secretary to direct funds to specific areas or for specific purposes in the event of unforeseen circumstances or events. We feel it is important to maintain this flexibility and, in the absence of other opposing comments, we have retained this provision.

(4) The loan request is in support of an optional factor developed by the State that promotes compatibility with special housing initiatives in conjunction with state-administered housing programs such as HOME funds or low income housing tax credits (LIHTC). A factor thus developed cannot duplicate factors already included in this paragraph and must be provided to the National Office prior to the funding cycle for concurrence and inclusion in the NOFA. (20 points)

One comment was received on this provision. The commentor felt that the factor needed further description and expressed a concern that it could be used to give preference to LIHTC loan requests, effectively excluding other loan requests.

This provision was included to give Rural Development State Directors more flexibility in working with their states to accomplish common housing goals, which we believe is critical to the Agency's partnership efforts. Factors developed under this provision require National Office concurrence, and we have retained this provision in the final rule.

(5) The loan request includes donated land meeting the provisions of § 1944.215(r)(4). (5 points)

One commentor felt that the Agency needed to redefine its provisions pertaining to preference for donated land in § 1944.215(r)(4), stating that the 1-year ownership requirement was too restrictive. The same commentor expressed the opinion that the value of land provided at no cost to the project should be included as leveraging or factored into the evaluation of costs.

On the first issue, the provisions for donated land preference are based on statute, and pertain to land donated by States, units of local government, public bodies, and nonprofit organizations. The 1-year ownership restriction was added to prevent abuse of this preference and may be waived by the State Director if it is clearly documented that there was no intent to circumvent the provisions.

On the issue of including donated land as leveraged assistance or factoring the value into the evaluation of costs,

the regulations do provide for this. Section 1944.211(a)(4) provides that the borrower's contribution may be in the form of cash, land, or a combination thereof. Any land value (as determined by the appraisal) that exceeds the borrower's required contribution may be considered leveraged assistance up to the amount which, when added to the loan and grant amounts from all sources, does not exceed the security value of the project. This applies to all donated land; therefore, donated land meeting the provisions of § 1944.211(a)(4) may receive 5 points under the donated land scoring factor and may also be eligible for points for leveraged assistance under the leveraged assistance factor. We have revised the point score factor for leveraged assistance to remove the exclusion of donated land.

Other Scoring Factors

Several commentors suggested additional factors for scoring loan requests. One commentor recommended awarding points for proposals in communities with RUS financed water or sewer systems to encourage total rural development. We agree there is merit in encouraging total rural development; however, awarding points for RUS financed facilities would penalize other communities with adequate systems that were not developed through RUS, or communities whose residents are unable to support the cost of these systems. In developing the interim final rule, we considered a similar provision whereby communities would be required to have water and sewer systems to qualify as a designated place; however, for the same reason, i.e., that communities that could not support the cost would be penalized, we did not adopt this provision. Another commentor noted that leveraged assistance should not dominate the scoring, and suggested other factors to consider such as design, construction quality, experience of the development team, resident services, ease of maintenance, and compatibility with the community. We agree these factors are critical to a successful proposal and, in developing the interim final rule, we considered awarding points for many of these same factors. However, we felt it would not be possible to develop standards for factors that require subjective judgments, such as an assessment of quality or experience, that could be equally applied to all proposals. With our competitive selection process, we believe it is essential to maintain an objective scoring process and, therefore, we have not adopted these factors.

Nonprofit Preference

One commentor supported the preference for nonprofit applicants but asked for clarification on how the preference was given; another commentor stated that loan requests from nonprofit applicants should be selected by merit and not by lottery. In response to the first comment, preference is given to loan requests from nonprofit or public body applicants meeting the provisions of § 1944.231(e) by giving preference in the event of point score ties. If there are point score ties for loan requests from two or more applicants meeting the provisions of § 1944.231(e), selection is made by lottery. In response to the suggestion that applicants be selected by merit and not by lottery, we feel it would not be possible to develop objective standards for judging the quality or experience of applicants that could be uniformly applied; therefore, we have retained the lottery provisions for point score ties.

Conditional Commitments

Two commentors recommended that the Agency issue a conditional or ''soft'' commitment when funding from other sources is contingent upon RHS funding. We recognize that this has been a problem in many instances, with both parties wanting the other to make the first commitment. The following policy will be followed: The Agency will publish NOFA as early in the year as possible to coordinate with other funding cycles. Loan proposals that include secondary funds from other sources that have been requested but have not yet been committed will be scored and ranked based on the requested funds: *Provided,* That (1) the applicant includes evidence of a filed application for funds, and (2) the funding date of the requested funds will permit processing of the loan request in the current year, or, in the event the applicant does not receive the requested funds, will permit processing of the next highest ranked proposal in the current year. States will issue a conditional commitment letter to the applicant with a specific deadline for providing a commitment of funds from the other lender. If the deadline is not met, the application will be returned as incomplete. The next highest ranked proposal will then be selected for further processing.

(2) Assurances That the Amount of Assistance Provided is No More Than Necessary

Section 1944.213 was revised in the interim final rule to implement the statutory reforms pertaining to necessary assistance. Four commentors expressed their support for these provisions and recommended minor revisions as follows:

Developer's Fees

One commentor noted that the section on developer's fees was included twice, once in § 1944.213(a)(1)(iv) and again in § 1944.213(a)(2). This error has been corrected in the final rule.

Fee Norms

One commentor expressed support for the fee norms in § 1944.213(a)(1) but suggested that the rule clarify that the fee norms are to be used only in cases where an executed Memorandum of Understanding (MOU) with the state agency is not in effect.

The regulation pages provided to RHS staff included a provision to this effect, as well as other administrative guidance, that was not published in the **Federal Register**. Interested parties may obtain a copy of the regulation pages from any Rural Development office.

Loan Request Analysis

The same commentor expressed support for the requirement that RHS consult with the applicant and the state allocating agency in cases of potential excess assistance to strive to reach an agreement for reducing any excess, and asked that the phrase ''and state agency'' be added after the words, ''In the event that excess assistance is not reduced through an agreement with the applicant,'' in § 1944.213(a)(3)(iii). This revision has been made in the final rule.

Excess Assistance

Two commentors suggested that if excess assistance is determined, the funds be put into project reserves or otherwise used to benefit the project, instead of reducing the amount of assistance. One of the commentors noted that current mandated reserve levels are minimal and it would make good sense to increase the reserve level.

We agree that additional funds could be used to benefit the project; however, we do not believe this would be consistent with our statutory mandate to provide only the amount of assistance necessary for the development of the project. As a point of interest, the project reserve requirements are being revised as part of the reinvention effort, which should alleviate the problems we

have experienced because of underfunded reserves.

In addition to the reforms discussed above, this rule includes a change in the maximum loan term for Section 515 loans from 50 years to 30 years. This change is mandated by Pub. L. 105–86, enacted November 18, 1997.

Implementation Proposal

The provisions of this rule become effective 30 days from the date of publication and all loans will be processed in accordance with the revised regulations. The final rule changes the income basis for the ranking data from 60 percent of county rural median income to 30 percent and increases the number of designated places that may be selected. This, in turn, may affect loan requests on hand that were issued an AD–622, ''Notice of Preapplication Review Action,'' inviting a formal application prior to November 7, 1996 (the date Agency staff were advised not to issue additional AD–622s pending the implementation of the new statutory requirements). For purposes of this discussion, these loan requests will be referred to as ''AD–622s''.

The interim final rule announced the Agency's intent to fund AD–622s on hand, in date order received, provided they met the new statutory requirements and were in designated places. Agency staff were directed to return AD–622s that were not in designated places. This was later amended by a Notice published in the **Federal Register** (62 FR 32752) on June 17, 1997, which directed Agency staff to hold the AD–622s until after the publication of the final rule because of anticipated changes in the designated place requirements.

Based on the large number of comments supporting an increase in the number of designated places, the final rule has been modified to allow States to select designated places up to 10 percent of their total rural places. Places currently on the designated place list will remain on the list for the duration of their 3-year designation period or until removed or deferred in accordance with § 1944.229(d). States may add places from the new ranking list up to the maximum 10 percent.

Using the revised place list, States may process AD–622s in designated places, in date order the complete application was received, up to the amount of the State's allocation. Existing AD–622s may be processed in this manner until the beginning of FY 2000. As in FY 1997, NOFA for FY 1998 will list those States that have AD–622s on hand that will use their direct allocation.

List of Subjects in 7 CFR Part 1944

Administrative practice and procedure, Aged, Handicapped, Loan programs—housing and community development, Low and moderate income housing—Rental, Mortgages, Nonprofit organizations, Rent subsidies, Rural areas.

Therefore, chapter XVIII, title 7, Code of Federal Regulations is amended as follows:

PART 1944—HOUSING

1. The authority citation for part 1944 continues to read as follows:

Authority: 5 U.S.C. 301; 42 U.S.C. 1480.

Subpart E—Rural Rental and Rural Cooperative Housing Loan Policies, Procedures, and Authorizations

2. Section 1944.205 is amended in the definition of ''Eligible tenants or cooperative members'' by revising the words ''exhibit C of subpart A of this part 1944 (available in any FmHA or its successor agency under Pub. L. 103–354 office)'' to read ''7 CFR 3550.53'', and by adding in alphabetical order definitions to read as follows:

§ 1944.205 Definitions.

* * * * *

EZ/EC. Empowerment Zone or Enterprise Community.

* * * * *

REAP. Rural Economic Area Partnership.

* * * * *

3. Section 1944.213 is amended by removing paragraph (a)(1)(iv), in paragraph (a)(3)(iii) by adding the words ''and state agency'' following the words ''In the event that excess assistance is not reduced through an agreement with the applicant''; and by adding the word '', LIHTC'' following the word ''HUD'' in the introductory text of paragraph (f)(2) and in the first sentence of paragraphs (f)(2)(ii) and (f)(2)(iii).

4. Section 1944.214 is amended by revising paragraph (b) to read as follows:

§ 1944.214 Rates and terms.

* * * * *

(b) *Amortization period*. Each loan will be scheduled for payment within a period that is necessary to assure that the loan will be adequately secured, taking into account the probable depreciation of the security. The payment period will not exceed 30 years; however, if necessary to ensure affordability, the loan may be amortized for a period not to exceed 50 years.

5. Section 1944.228 is amended in paragraphs (c)(1) and (c)(3) by revising the words ''60 percent'' to read ''30 percent''.

6. Section 1944.229 is amended by revising paragraphs (a), (b)(1), (c), and (d), and by adding a new paragraph (f) to read as follows:

§ 1944.229 Establishing the list of designated places for which Section 515 applications will be invited.

* * * * *

(a) *Establishing the number of designated places*. Initially, the number of designated places may equal up to 10 percent of the state's total eligible rural places ranked in accordance with § 1944.228, but must equal, in all cases, at least 10 places. For example, in a state with 1,000 total rural places, the State may designate up to 10 percent, or 100 places. However, in a state with 60 total rural places, the State would use the minimum number of 10 places, since 10 percent of 60 equals 6. In states where 10 percent equals more than the minimum number of 10, consideration in determining the number of places to include on the list should be given to the size and population of the state, funding levels, and the potential for leveraging. If warranted by funding levels, the Administrator may authorize in NOFA the selection of designated places up to 20 percent of the States' total rural places.

(1) States may designate a higher number of places than 10 percent or the minimum 10 places to reach high-need areas in accordance with paragraph (c)(3) of this section.

(2) States that anticipate high loan activity because of leveraging may designate a number of places higher than 10 percent or the minimum 10 places with the concurrence of the National Office.

(b) * * *

(1) Must have 250 or more households as a minimum feasibility threshold for multi-family housing, or, for Indian reservations, must have 250 or more households within the boundaries of the reservation; and

* * * * *

(c) *Selection of designated places*. Places meeting the requirements of paragraph (b) of this section will be selected from the ranking list as follows:

(1) At least 80 percent of the State's total designated places must be selected in rank order from the list.

(2) With concurrence from the National Office, up to 20 percent of the State's designated places may be selected for geographic diversity. For example, in a state with 1,000 total rural places, the State has elected to select designated places equal to the maximum 10 percent, or 100 places. Of

the 100 places, at least 80 percent, or 80 places, must be selected from the places that meet the requirements of paragraph (b) of this section in order of their ranking; up to 20 percent, or 20 places, may be selected for geographic diversity. Places selected for geographic diversity must be the highest ranked place in each geographic division designated by the State, which must correspond with established State divisions, such as districts, regions, or servicing areas.

(3) In addition to the designated places selected in accordance with paragraphs (c)(1) and (c)(2) of this section, States may designate the following high need areas for multi-family housing:

(i) Places identified in the state Consolidated Plan or similar state plan or needs assessment report.

(ii) EZ/ECs, Indian reservations or communities located within the boundaries of tribal allotted or trust land, colonias, or REAP communities.

(d) *Length of designation*. Places will remain on the list of designated places for 3 years or until a loan request is selected for funding or the community is otherwise deferred for other ''build and fill'' conditions, whichever occurs first. Places that are deferred before the end of the 3-year designation period will be reviewed annually for potential inclusion on the next year's list of designated places. A place may be removed from the list prior to the end of the 3-year designation period because of a substantial loss of income-eligible population or an increase in the affordable rental housing supply, for example, a place that experiences the closing of a military base or other major employer.

* * * * *

(f) *Partnership designated place list*. States with an active leveraging program and formal partnership agreement with the state agency may establish a partnership designated place list consisting of places identified by the partnership as high need areas based on criteria consistent with the Agency's and the state's authorizing statutes. The partnership agreement and partnership designated place list must have the concurrence of the Administrator. Ranking and selection of loan requests for places on the partnership designated place list will be in accordance with § 1944.231(b)(3)(iii) and § 1944.231 (b)(6) of this subpart.

7. Section 1944.231 is amended by revising paragraphs (b)(2)(iii)(A) and (b)(2)(iii)(B), and by adding paragraphs (b)(3)(iii) and (b)(6) to read as follows:

§ 1944.231 Processing loan requests.

* * * * *

(b) * * *

(2) * * *

(iii) * * *

(A) The presence and extent of leveraged assistance for the units that will serve RHS income-eligible tenants at basic rents comparable to those if RHS provided full financing. Eligible types of leveraged assistance include loans and grants from other sources, contributions from the borrower above the required contribution indicated by the Sources and Uses Comprehensive Evaluation, and tax abatements or other savings in operating costs provided that, at the end of the abatement period when the benefit is no longer available, the basic rents are comparable to or lower than the basic rents if RHS provided full financing. Scoring will be based on the presence and extent of leveraged assistance for each loan request compared to the other loan requests being reviewed, computed as a percentage of the total development cost of the units that will serve RHS income-eligible tenants. A total monetary value will be determined for leveraged assistance such as tax abatements or services in order to compare such items equitably with leveraged funds. As part of the loan application, the applicant must include specific information on the source and value of the services for this purpose. Proposals will then be ranked in order of the percent of leveraged funds and assigned a point score accordingly. Loan proposals that include secondary funds from other sources that have been requested but have not yet been committed will be processed as follows: the proposal will be scored based on the requested funds: *Provided,* that the applicant includes evidence of a filed application for the funds; *and* the funding date of the requested funds will permit processing of the loan request in the current funding cycle, or, if the applicant does not receive the requested funds, will permit processing of the next highest ranked proposal in the current year. The Agency will issue a conditional commitment to the applicant with a specific deadline for providing a commitment of funds from the other source. If the deadline is not met, the application will be returned as incomplete and the next ranked proposal will be processed. (0 to 20 points)

(B) The loan request is for units to be developed in a colonia, tribal land, EZ/EC, or REAP community, or in a place identified in the state Consolidate Plan or state needs assessment as a high need community for multi-family housing. (20 points)

* * * * *

(3) * * *

(iii) States with a partnership designated place list developed in accordance with § 1944.229(f) of this subpart, will score and rank loan requests as follows:

(A) All loan requests (including those for places on the partnership designated place list) will be reviewed and scored together as one group, following the process described in paragraph (b)(2) of this section.

(B) Using the point score and rank order established in accordance with paragraphs (b)(3)(i) and (b)(3)(ii) of this section, two separate ranking lists will be formed: the RHS ranking list will consist of loan requests for places on the State's designated place list; the partnership ranking list will consist of loan requests for places on the partnership designated place list. Selection of loan requests for further processing will be in accordance with paragraph (b)(6) of this section.

* * * * *

(6) *Selection of loan requests for further processing for States with a partnership ranking list*. States with a partnership ranking list developed in accordance with paragraph (b)(3)(iii) of this section, will use the following process:

(i) Loan requests must first be selected in rank order from the RHS ranking list that, based on total development cost (TDC), are proportionate to the State's RHS allocation amount.

(ii) After loan requests have been selected in accordance with paragraph (b)(6)(i) of this section, remaining RHS funds must be used for the next highest scoring loan requests (or point score and tie-breaker number assigned in accordance with paragraph (b)(3) of this section), regardless of whether they are on the RHS ranking list or the partnership ranking list.

* * * * *

8. Section 1944.233 is amended in paragraph (a)(3) by revising both occurrences of the words ''debt service'' to read ''basic rent'', and in paragraph (b)(5) by revising the words ''a debt service'' to read ''basic rents''.

9. Exhibit A of subpart E is amended in section IV.B.2.c. in the second sentence by revising the words ''50 years'' to read ''30 years, with an amortization period not to exceed 50 years.''

10. Exhibit A–7 of subpart E is amended by removing paragraph VII and by redesignating paragraphs VIII and IX as paragraphs VII and VIII respectively.

11. Exhibit A–9 off subpart E is amended by adding a new paragraph 17 to read as follows:

Exhibit A–9—Additional Information To be Submitted for Rural Rental Housing (RRH) and Rural Cooperative Housing (RCH) Loan Requests

* * * * *

17 Comments must be submitted in accordance with 7 CFR, part 3015, subpart V, ''Intergovernmental Review of Department of Agriculture Programs and Activities.'' See RD Instruction 1940–J (available in any Rural Development office).

12. Exhibit H of subpart E is amended in the fourth sentence by revising the words ''50-year maximum life of the loan'' to read ''30-year maximum life of the loan''.

Dated: December 18, 1997.

Jill Long Thompson,

Under Secretary, Rural Development.

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