

**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT****24 CFR Parts 901 and 902**

[Docket No. FR-4313-F-03]

RIN 2577-AB81

**Public Housing Assessment System**

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

**ACTION:** Final rule.

**SUMMARY:** This final rule implements a proposed rule published on June 30, 1998 to provide for the assessment of the physical condition, financial health, management operations and resident services in public housing. The rule also provides for a Troubled Agency Recovery Center to improve poor performers, and an Enforcement Center and possible receivership for agencies that fail to improve performance. Public housing agencies that fail to post significant improvement within a year will be automatically referred to the new HUD Enforcement Center, which will institute proceedings for judicial receivership to remove failed agency management. The purpose of the new Public Housing Assessment System is to enhance public trust by creating a comprehensive management tool that effectively and fairly measures a PHA's performance based on standards that are objective, uniform and verifiable, and provides real rewards for high performers and consequences for poor performers. The final rule takes into consideration public comment received on the June 30, 1998 proposed rule.

**EFFECTIVE DATE:** October 1, 1998.

**FOR FURTHER INFORMATION CONTACT:** For further information contact the Real Estate Assessment Center, Attention William Thorson, Director of Physical Inspection Management, Real Estate Assessment Center, Department of Housing and Urban Development, 4900 L'Enfant Plaza East, SW, Room 8204, Washington, DC 20410; telephone (202) 755-0102 (this is not a toll-free number). Persons with hearing or speech impairments may access that number via TTY by calling the Federal

Information Relay Service at (800) 877-8339.

**SUPPLEMENTARY INFORMATION:****I. The Proposed Rule**

On June 30, 1998 (63 FR 35672), HUD published a proposed rule that would establish a new system for the assessment of America's public housing. The new Public Housing Assessment System (PHAS) is designed to enhance public trust by creating a comprehensive oversight tool that effectively and fairly measures a PHA based on standards that are objective and uniform. The PHAS represents a major rethinking of public housing management.

Under the PHAS as proposed on June 30, 1998, HUD evaluates a PHA based on the following indicators: (1) the physical condition of the PHA's public housing properties; (2) the PHA's financial condition; (3) the PHA's management operations; and (4) residents' assessment (through a resident survey) of the PHA's performance. The management indicator of this new assessment system will incorporate the majority of the existing statutory management assessment indicators (the remaining statutory indicators will be part of the other PHAS indicators). Each of these major indicators is comprised of components. To assess the performance of a PHA on the basis of the first two indicators, the Assessment Center will use comprehensive and standardized protocols to conduct physical inspections of public housing properties and to assess the financial condition of PHAs. For the Management Operations Indicator and the Resident Service and Satisfaction Indicator, the Assessment Center will gather and analyze data and information provided by the PHA.

In order to determine a composite score for each PHA, the four indicators of the PHAS will be individually scored and then combined to present a composite score that reflects the overall performance of PHAs for a total of 100 possible points. The 100 points are distributed as follows:

- 30 total points for the physical condition;
- 30 total points for the financial condition;

30 total points for management operations; and

10 total points for resident service and satisfaction.

The PHAS, although applicable only to public housing, reflects HUD's new approach, under HUD 2020 Management Reform, to all properties assisted by HUD. HUD intends to assess all HUD-related properties in a manner similar to that under the PHAS, using uniform financial and physical indicators and resident feedback.

An accurate assessment of a PHA's performance is critical because the consequences of that assessment can be significant. For PHAs determined to be high performers, the consequences will be less scrutiny and additional flexibility. For PHAs determined not to be performing well, the consequences will be intensive technical assistance, deadlines for improvement and possible punitive actions for failure to improve during established periods. The approach provided by the PHAS maximizes the best use of public funds by concentrating resources on those PHAs in most need of attention and recognizing outstanding performers. The system is fundamentally designed to provide relevant and verifiable measures that directly relate to PHA performance.

The June 30, 1998 proposed rule provided for the new PHAS to become effective for PHAs with fiscal years ending September 1999 and later. Financial reports due for PHAs' fiscal years ending in September 1999 and later must be prepared on a GAAP basis. The first scores under the new PHAS will be issued not later than December, 1999 for PHAs with FYs ending in September 1999. Thus, PHAs will have at least one year before the new PHAS scores are issued. Until September 30, 1999, PHAs will continue to be scored under the current PHMAP. During this one year transition period, advisory scores for physical condition and financial management may be issued to provide guidance to PHAs. The implementation schedule for inspection of public housing properties and reporting is as described in the following table:

## REAL ESTATE ASSESSMENT CENTER (REAC)

[Assessment Periods and Reporting Dates]

REAC assessment results		Financial reporting	Physical inspection	Management operations	Resident survey
Score issued	Period covered fiscal year end (1)		Inspection dates (3)	Submission due date (4)	Survey dates (5)
12/1999 .....	9-30-99	11-30-99	7/99-9/99	11-30-99	4/99-9/99
03/2000 .....	12-31-99	2-28-2000	10/99-12/99	2-28-2000	10/99-12/99
06/2000 .....	3-31-2000	5-31-2000	1/2000-3/2000	5-31-2000	1/2000-3/2000
09/2000 .....	6-30-2000	8-31-2000	4/2000-6/2000	8-31-2000	4/2000-6/2000
12/2000 .....	9-30-2000	11-30-2000	7/2000-9/2000	11-30-2000	7/2000-9/2000

**Notes:**

1. The period covered for each indicator will be the PHA's entire fiscal year ending on dates shown above. Once the new PHAS is effective, a PHA cannot change its fiscal year for a period of 3 years.

2. PHAs with fiscal years ending 9-30-99 and later must provide GAAP financial reports. These reports must be provided by electronic submission not later than 60 days after the end of the PHA's FY. Audited GAAP reports (due 9 months after the close of the FY in accordance with the Single Audit Act and OMB Circular A-133) will be used to update and confirm unaudited financial results. If significant differences are noted between unaudited and audited results, scoring penalties will apply. For those PHAs that spend less than \$300,000 of Federal funds, HUD cannot require or pay for an audit in accordance with the Single Audit Act. HUD, however, can require and pay for an "Agreed-Upon Procedures" report that could be specifically directed at verifying calculations.

3. Physical inspections will be scheduled to approximate the new PHAS calculation dates; i.e. within the final quarter of the PHA's fiscal year.

4. The certifications and supporting documentation required for the Management Operations Indicator will be due 60 days after the end of the PHA's fiscal year.

5. Resident surveys will be required to be conducted during the course of a PHA's fiscal year and will be required to be submitted by a PHA at the time that the PHA submits the certifications required under the Management Operations Indicator.

**II. Changes Made to Proposed Rule at the Final Rule Stage**

The initial due date for the receipt of public comments on the proposed PHAS rule was July 30, 1998. In response to requests from commenters for additional time to comment on this rule, HUD published a notice on July 30, 1998 (63 FR 40682) extending the deadline for public comments until August 13, 1998. HUD received 776 comments on the proposed rule. The commenters included housing authorities, residents of public housing (whose 670 form letters represented the great majority of the comments), and organizations representing residents or housing authorities. The form letters provided by the residents addressed only the issue of the resident survey proposed in the PHAS rule.

As a result of the public comments and HUD's further consideration of certain issues, the following changes were made to the rule at the final rule stage.

1. A new part 902 is established for the PHAS rule. Since PHAS will not be implemented until October 1, 1999, PHAs will continue to comply with the requirements of the Public Housing Management Assessment Program (PHMAP), and therefore HUD needs to retain 24 CFR part 901 which contains the PHMAP regulations. After PHAS is fully implemented, HUD will issue a final rule to remove 24 CFR part 901.

2. In § 902.7 (§ 901.7 in the proposed rule), a definition of "Alternative management entity (AME)" has been added, and the definition of

"deficiency" has been clarified by including "sub-indicator" within its scope.

3. Section 902.25(a) (§ 901.25(a) in the proposed rule) is revised to clarify that the score is based on the relative importance of the individual inspectable areas and the relative severity of the deficiencies observed.

4. Section 902.25(b)(2)(ii) (§ 901.25(b)(2)(ii) in the proposed rule) is clarified to indicate that a majority of the population that resides in the census tracts or census block groups on all sides of the development will be examined to determine if the neighborhood environment adjustment applies.

5. Section 902.50(b) (§ 901.50(b) in the proposed rule) is revised to state that the survey will be "managed" rather than "administered" by the PHA.

6. Section 902.53(a) (§ 901.53(a) in the proposed rule) is revised in accordance with the preamble discussion at section III.F.7. below, to indicate only the first two components of the survey indicator are awarded points, with the third component being a threshold requirement.

7. In § 902.53(b) (§ 901.53(b) in the proposed rule), the text is modified for clarity and to remove the words "by the PHA" following the phrase "survey results are determined to be altered."

8. Sections 902.67(b) and 902.71(d) (§§ 901.67(b) and 901.71(d) in the proposed rule), which address the HUB/Program Center's discretion to subject a PHA to any requirement that would

otherwise be omitted under the specified relief, are removed.

9. The requirement in § 902.71(a)(2) (§ 901.71(a)(2) of the proposed rule) for public recognition is made consistent with the rest of the PHAS rule by stating that at least 60 percent of the points available under each of the four PHAS Indicators and an overall PHAS score of 90 are necessary.

10. In § 902.73(g) (§ 901.73(g)), this final rule adds language to clarify that if the TARC determines that it is appropriate to refer the PHA to the Enforcement Center, it will only do so after the PHA has had one (1) year since the issuance of the PHAS score (or, in the case of an RMC, notification of its score from a PHA) to correct its deficiencies. This one-year period includes the 90 days or such other period of time (if less than one year), as described in § 902.73(c)(1).

11. In § 902.75(g) (§ 901.75(g) in the proposed rule), this final rule adds language to clarify that a PHA cannot maintain its troubled status indefinitely; the maximum period of time for remaining in troubled status before being referred to the Enforcement Center is 2 years. This final rule also clarifies in § 902.75(g) that the REAC makes the determination of whether a PHA has made substantial improvement toward a passing PHAS score.

12. Section 902.75(h) is a new subsection, added to clarify that, to the extent feasible, while a PHA is under a referral to a TARC, all services to residents will continue uninterrupted.

13. Section 902.77(b) is new subsection, added to clarify that, to the extent feasible, while a PHA is under a referral to the Enforcement Center, all services to residents will continue uninterrupted.

15. Language is added to § 902.79(b) (§ 901.79(b) of the proposed rule) to clarify the meaning of "credible source" for events or conditions constituting a substantial breach or default.

### III. Discussion of Public Comments

The public commenters on this rule overwhelmingly commended HUD for its efforts to improve PHMAP, and there was considerable support among the commenters for the new PHAS, as announced in the June 30, 1998 proposed rule. One commenter stated that the proposed PHAS is superior in approach to PHMAP. Another commenter stated that PHAS logically focuses on appropriate operational areas, with the primary emphasis on physical and financial concerns. Several commenters, however, expressed reservations about one more aspects of the new PHAS. The following provides a more detailed discussion of the commenters' concerns as well as a discussion of other issues raised by the public commenters on the June 30, 1998 proposed rule.

#### A. General Comments

*The Public Comment Period for the Rule Was Not Sufficient.* Many commenters stated that the 30-day public comment period provided by the June 30, 1998 proposed rule was insufficient. These commenters remarked that a rule of such importance and complexity merited a longer comment period. Several commenters remarked that, rather than reducing the customary 60-day comment period, the proposed rule should have provided 90 days for the submission of comments. Two of the commenters also questioned the consultative process that HUD used to justify the reduced comment period.

One of the commenters remarked that "HUD consulted with a few authorities, but this is the first time more than 3,300 housing authorities have been able to comment" on the PHAS.

Given the extensive consultative process in the development of the rule, HUD believes that a 30-day public comment period was sufficient for this rule. Nevertheless, in response to commenters' request, HUD did extend the public comment period through August 13, 1998, to allow additional time for comment. HUD recognizes that although not every PHA was involved in the extensive consultative process that preceded publication of the proposed rule, there was substantial PHA representation and participation in that process over a six month period. HUD also reminds PHAs, residents and other interested parties that although this rule takes effect 30 days after publication in the **Federal Register**, PHAS is not implemented until October 1, 1999. This first year is a transition year, which allows both HUD and PHAs the opportunity to test the new PHAS, for PHAs to continue to offer input and suggestions, and for HUD to consider and make any changes that may be needed before PHAS becomes fully implemented.

In addition, HUD has provided, and will continue to provide, documents and assistance by direct request and over the Internet, such as the 24-hour on-line assistance on the GAAP Conversion Guide at HUD's website (<http://www.hud.gov/reac/reafin.html>). As the discussion below of the public comments on the individual indicators will demonstrate, HUD will continue to make available all of the information and assistance necessary for PHA compliance with the rule.

Rule is Vague; Lacks Necessary Details. A number of commenters remarked that the proposed rule is too vague and uninformative. These commenters wrote that the lack of specificity of the proposed rule made

the submission of meaningful comments almost impossible.

With respect to the details of all of the components of the PHAS, specifically the physical and financial components, HUD notes that traditionally HUD regulations, and indeed other agency regulations, do not contain all the details and processes that are part of these components. A great majority of these are technical or examples of implementation processes. The regulation enunciates the policy, provides the broader requirements (in this case, uniform, enforceable baseline standards), and the details are left to supplemental documents, such as handbooks and guidebooks. These documents allow for a more detailed (and therefore more helpful) description and discussion of the components to be addressed, and the procedures to be followed and the information to be submitted, which include examples and model reports, and which can be corrected and updated easily.

This is the practice that HUD has followed to date, and HUD will continue to follow this practice with the PHAS. HUD already has developed certain guidance in connection with implementation of the PHAS, and has made this guidance available to PHAs for review and any comments they may have. For example, HUD has developed the HUD-GAAP Conversion Guide, which is available at HUD's internet web site at <http://www.hud.gov/reac/reafin.html>, or by calling the HUD Real Estate Assessment Center's Customer Service Center on 1-(888)-245-4860.

Several commenters requested additional information on the relative weights/points of the four PHAS indicators. Although this information will be contained in the supplementary guidance to be provided, HUD has listed below the *approximate* relative weights/points of the four PHAS indicators, sub-indicators, and components within the sub-indicators:

#### APPROXIMATE RELATIVE WEIGHTS/POINTS

Indicator/Sub-Indicator/Component	Indc. Pts.	Approx. Pts.
#1, Physical Condition .....	30	.....
Site (plus 1 pt. for physical condition and neighborhood environment) .....	.....	4.5
Building Exterior (plus 1 pt. for physical condition and neighborhood environment) .....	.....	4.5
Building Systems .....	.....	6.0
Dwelling Units .....	.....	10.5
Common Areas (plus 1 pt. for physical condition and neighborhood environment) .....	.....	4.5
In addition, Health and Safety deficiencies will result in reductions to the total physical inspection score which takes into account the five areas, above, with their approximate relative weights/points.		
#2, Financial Condition .....	30	.....
Liquidity .....	.....	9.0
Net Asset Adequacy .....	.....	9.0
Days Receivable Outstanding .....	.....	4.5

## APPROXIMATE RELATIVE WEIGHTS/POINTS—Continued

Indicator/Sub-Indicator/Component	Indc. Pts.	Approx. Pts.
Vacancy Loss .....		4.5
Net Income/Loss .....		1.5
Expense Management .....		1.5
Flags:		
No audit opinion (minus 30 pts.) .....		
Going concern opinion (*) .....		
Disclaimer of opinion (minus 30 pts.) .....		
Material weakness/internal control (*) .....		
Adverse opinion (minus 30 pts.) .....		
Qualified opinion (*) .....		
Reportable conditions (*) .....		
Findings of non-compliance and questioned costs (*) .....		
Indicator outlier analyses (*) .....		
(*) Points will be deducted to the extent points remain after initial scoring for the sub-indicator affected by the flag.		
#3, Management Operations .....	30	
Vacancy Rate/Progress to Reduce .....		8.0
Vacancy Rate .....		(4.0)
Unit Turnaround Time .....		(4.0)
Modernization .....		6.0
Unexpended Funds .....		(1.0)
Timeliness of Fund Obligation .....		(1.5)
Contract Administration .....		(1.0)
Quality of the Physical Work .....		(2.0)
Budget Controls .....		(0.5)
Rents Uncollected .....		4.0
Work Orders .....		4.0
Emergency Work Orders .....		(2.0)
Non-Emergency Work Orders .....		(2.0)
Inspection of Units and Systems .....		4.0
Inspection of Units .....		(2.0)
Inspection of Systems .....		(2.0)
Security .....		4.0
Tracking/Reporting Crime-Related Problems .....		(1.0)
Screening of Applicants .....		(1.0)
Lease Enforcement .....		(1.0)
Grant Program Goals .....		(1.0)
#4, Resident Service and Satisfaction .....	10	
Survey Results .....		(5.0)
Level of Implementation/Follow-Up Action Process .....		(5.0)

**Modification of PHAS Indicators Requires Rulemaking.** Several commenters objected to the statement in the preamble of the proposed rule that "HUD reserves the right to add new indicators or components of indicators, or remove indicators or modify indicators of the new PHAS." The commenters noted that the preamble to the proposed rule also advised that "PHAs and the public will be notified of any change in indicators or components through issuance of the appropriate type of notice." (See 63 FR 35680.) These commenters wrote that any modifications to the indicators would involve substantive issues and require the use of notice and comment rulemaking procedures.

As noted in the preamble to the proposed rule, HUD will provide appropriate notice of any change or notification. Where notice and comment rulemaking is determined necessary, HUD will undertake such rulemaking.

**Section 3 Requirements Should Be Part of PHAS.** A few commenters suggested that the requirements of section 3 of the Housing and Urban Development Act of 1968 be incorporated in the PHAS. Section 3 requires that economic opportunities generated by certain Federal financial assistance, including public housing, shall be given, to the greatest extent feasible, to low and very low income persons. Since public housing is subject to the section 3 requirements, the commenters suggest that PHA compliance with section 3 be included in the new assessment system.

A PHA's responsibilities with respect to the Section 3 program are specifically addressed in the extensive regulations at 24 CFR part 135. The PHAS assessments are not focused on specific programmatic requirements, but on the overall quality of a PHA's physical, financial, and managerial well-being, and the residents' perception of that

quality. At this time, HUD will not include this additional element in its assessment.

**PHAS Would Not Represent the First-Ever Assessment of Public Housing.** A few commenters took exception to the statement in the preamble to the June 30, 1998 proposed rule that PHAS would provide for the "first-ever assessment of the physical condition, financial health and resident services in public housing" (63 FR 35672). The commenters wrote that PHAs regularly inspect the condition of their public housing stock.

HUD agrees that while certain components of the new PHAS are not new, the consolidation of these previously disparate elements into a single assessment undertaken by HUD is new. HUD intends for this new consolidation to result in the overall improvement of PHAs, which will lead to the greater satisfaction of both PHA administrators and residents.

*Proposed Rule Would Establish Unfunded Financial Burdens.* Two commenters objected to the proposed rule due to the unavailability of the additional funding they believe is necessary for the successful implementation of the new assessment system.

Although the initial implementation of the new assessment system may result in some increased costs, these are not expected to be significant. Under PHAS Indicator # 1 (Physical Condition), HUD will conduct the physical inspection. Therefore, this is neither an administrative or financial burden on PHAs. With respect to reporting in GAAP, HUD is allowing a full year for PHAs to convert to GAAP. Many PHAs already have converted to GAAP, and for those that have not yet converted, HUD already has provided guidance through the HUD-GAAP Conversion Guide and will provide additional training and assistance during the year of transition. HUD also is developing electronic submission software, which will provide an easy to use submission template at no cost to PHAs and other housing entities. HUD also will consider alternative means of submission if electronic reporting is determined to be excessively burdensome or costly. The management components of the PHAS are familiar to PHAs, and will not be a new burden. Additionally, HUD provides a full year of transition before PHAS is implemented. For these reasons, and others discussed later in this preamble, HUD believes that new PHAS will not present an undue financial burden.

*Proposed Rule May Exceed HUD's Statutory Authority under PHMAP.* Two commenters questioned whether the proposed rule is in violation of the public housing assessment requirements of section 6(j)(1) of the United States Housing Act of 1937 (the 1937 Act). These commenters noted that all seven of the indicators listed in section 6(j)(1) are combined within a single PHAS indicator that is weighted at "only 30% of the total maximum score allowable under PHAS." One commenter noted that the Secretary's general rulemaking authority under section 7(d) of the Department of HUD Act (42 U.S.C. 3535(d)) cannot be exercised in a manner that is inconsistent with statutory law, and that the proposed treatment of the statutory indicators may violate the statutory assessment requirements established by the 1937 Act.

The PHMAP statutory indicators, which are intended to assess the management performance of PHAs, comprise the entirety of the PHAS

Management Indicator. As such, they continue to serve the statutory purpose for which they were established. A good score on the statutory PHMAP management indicators, in which assessment is based on PHA self-certification, is expected to carry over and be reflected in the scores for the physical and financial examinations, which are based on HUD-reviewed data, and in the resident survey, in which the residents' perception of the PHA is manifested. The new PHAS indicators thus serve as a check on the self-certified PHMAP indicators, and amplify, through consistency, the accuracy of the certifications, or, through discrepancy, the certifications' shortcomings, thereby establishing a more solid basis for confidence or intervention. The Department has determined that, rather than undercut the statutory scheme, PHAS will serve to reinforce the accuracy and reliability of (what formerly was called) PHMAP.

*Proposed Rule Should Provide for Greater Resident Participation.* Three commenters wrote that all major components of the PHAS should reflect the principle and practice of resident participation. One of the commenters suggested that the rule be amended to enforce and protect the right of residents to voluntarily participate in the overall assessment process, and that residents be afforded the opportunity to participate in the assessment process through employment and training created in connection with the assessment work. Other commenters suggested that residents should be permitted to participate in the physical inspection process.

Residents are an integral part of the PHAS assessments. An entire PHAS indicator is devoted to a survey of the residents' level of PHA satisfaction. This survey serves as a valuable check on the other PHAS indicators. Residents will also participate in the physical inspection process, which requires the HUD inspectors to visit and inspect individual PHA units.

*HUD State Offices Should be Included in Assessment Process.* A few commenters wrote that local HUD offices should be provided a role in the PHAS. According to the commenters, such a policy would help to ensure that the HUD officials most knowledgeable about local housing conditions participate in the assessment process.

Local HUD Offices, through the participation of program staff and Community Builders, will work closely with the REAC, TARC, and Enforcement Center in ensuring the reliability and accuracy of the PHAS effort.

*The Same Standards Should Not Be Applied To Public Housing and FHA Insured Properties.* A few commenters noted a PHA does not have the ability to increase rents and generate more income from its property, and an FHA property has higher total development cost limits, typically resulting in better construction quality. One commenter stated that it is unfair to hold public housing to a standard that it was not designed nor funded to compete with.

The PHAS is not intended to measure competing housing amenities, but to measure and promote a basic level of housing that is decent, safe, sanitary, and in good repair; financially sound; well managed; and which thereby manifests a general level of resident satisfaction. The Department knows that many PHAs, even given their modest resources, can meet and, in fact, exceed this basic level. The unfairness lies in falling below this basic level.

*Role of the Assistant Secretary for Public and Indian Housing.* Two commenters raised the issue of the involvement of the Assistant Secretary for Public and Indian Housing (PIH) in the PHAS. One commenter stated the PHAS marginalizes the role of the Assistant Secretary, and that it appears that the Assistant Secretary will have no authority with respect to the activities of the REAC or the TARC. Another commenter noted that although the REAC will have the most significant role of the various HUD components in PHAS, the REAC will not be under the jurisdiction of the Assistant Secretary for PIH, or any other Presidential-appointee level official, other than the Secretary, and questioned the accountability of REAC. The commenter also expressed concerns that such arrangement may create internal wars and standoffs over PHA operations within the Department.

First, as with all HUD offices and officials, REAC and the Director of REAC are under the jurisdiction of the Secretary of HUD. Second, HUD expects that its new approach of consolidating discrete, cross-cutting functions such as assessment and enforcement into separate centers will permit HUD's program offices to concentrate on providing better program service. No longer will program staff wear the multiple hats of assistance provider, monitor, and enforcer. The wearing of multiple hats has been one of the major deficiencies of the HUD workforce addressed by the HUD 2020 Management Reform Plan (issued June 26, 1997). For too many years, the HUD workforce has been given schizophrenic mandates. On the one hand, HUD employees were asked to provide

assistance to communities and HUD's housing partners to help them meet their needs. On the other hand, these same employees were asked to police the actions of those same communities and housing partners. The PHAS allows REAC and the Enforcement Center to handle the enforcement obligations of program monitoring, and allows the Office of Public and Indian Housing to target its energies and resources on providing services to the 3,400 housing authorities and 1.4 million families they house. Having said this, HUD is nevertheless aware of the need to keep lines of communication and cooperation open among all of its functions and responsibilities, and expects to do so.

#### *B. Comments on Subpart A—General Provisions*

*PHAS Components Should Reflect PHA Differences.* Several commenters objected to the uniformity of the components that would be established under the PHAS. The commenters stated that the PHAS should factor the geographic, cultural, and other differences between housing authorities. One of the commenters wrote that while a uniform set of standards may be desirable, components should be developed to reflect local variances. Another commenter remarked that there may be great difficulty in comparing the management of PHAs that manage only housing for the elderly or persons with disabilities, to those that manage family developments or both.

As stated earlier in this preamble, the PHAS is intended to measure and promote a basic level of housing. HUD believes the PHAS achieves a basic level on a national basis that will be satisfactory to tenants without making unrealistic demands upon PHAs.

#### *C. Comments on Subpart B—PHAS Indicator #1: Physical Condition*

*Relationship Between PHAS and HQS is Unclear.* Several commenters expressed uncertainty regarding the relationship between the PHAS Physical Condition Indicator and the Housing Quality Standards (HQS). Other commenters asked how differences between the HQS inspection and the REAC inspection would be resolved. One of the commenters wrote that the proposed rule does not clearly define a connection between the new uniform physical condition standards, HQS, and the newly developed HUD computerized inspection protocol software that will assign physical condition scores.

Under PHAS, a new uniform physical condition standard is established in subpart B. This is the standard that HUD

will use in assessing the physical condition of a PHA's housing stock.

The previous requirement in PHMAP that PHAs inspect to local codes or the HQS, whichever is more stringent, has been eliminated. Instead, Indicator 3 (§ 902.43(a)(5) of this final rule) requires PHAs to inspect to the same standard as does HUD in Indicator #1. As a result, HQS will no longer be used as the standard for PHAs to inspect public housing units under PHAS. Therefore, there will be no differences between the two standards to reconcile. The new software developed by HUD will reflect all of the inspectable areas and inspectable items reflected in the new standard and capture deficiencies associated with those items.

*PHAS Indicators #1 and #3 Should be Consolidated.* Two commenters suggested that, since both PHAS Indicators #1 and #3 (Management Operations) require inspection of PHA units, the two indicators should be consolidated. According to one commenter this consolidation would permit the PHA to submit one less certification under the Management Operations indicator. The other commenter remarked that since HUD will conduct its own independent inspection to determine the quality of a PHA's maintenance effort, it appears duplicative to have another score relating to the PHA's own inspection which presumably also is intended to determine the quality of the maintenance effort.

HUD does not agree that Indicators #1 and #3 should be combined or that they are duplicative. While Indicators #1 and #3 both require physical inspections, they do not serve the same purpose. The HUD inspection under Indicator #1 is to determine the basic physical condition of the PHA's portfolio. This will be determined by inspecting a statistically valid sample of the units in the PHA's stock. The PHA will be notified of the deficiencies found in this limited assessment. Alternatively, the PHA inspection under Indicator #3 is a measure of PHA management performance. The inspection is intended to be more comprehensive and will assess each unit to determine the immediate maintenance and modernization and correct identified deficiencies. There is no intent in this rule for HUD to replace the PHA's inherent responsibility as the property owner to maintain decent, safe and sanitary housing, through the inspection of each of its units and the timely correction of deficiencies found.

*Notice of Defects.* Several commenters remarked that PHAs cannot be expected to cure problems caused by willful

resident damage or neglect of which the PHA does not have notice. As one of the commenters wrote: "A PHA cannot control a resident's housekeeping habits or abilities to correct 'other observable deficiencies'."

PHAs are required by law and contract to maintain decent, safe and sanitary housing. Nothing in the law or contract exempts the PHA from this responsibility due to resident caused damage. If a PHA is properly managing its properties, including regular annual unit and house keeping inspections, and enforcing lease provisions, the effect of resident caused damage on the overall assessment of the condition of the properties will be minimal.

*More Time Required for Implementation.* A few commenters requested that PHAs be provided with additional time before implementation of the PHAS Physical Condition Indicator. One commenter wrote that PHAs need the additional time to ensure that they comply with the new standards. This commenter also wrote that a one year test "of the proposed sampling methodology and survey design will provide needed estimates of the adequacy of the PHAS inspection system."

Section 902.60(b) of the final rule provides that "Information necessary to conduct the physical condition assessment under subpart B of this part will be obtained from HUD inspectors during the fiscal year being scored through electronic transmission of the data." In accordance with the implementation timetable published in the preamble of the June 30, 1998 proposed rule (63 FR 35679), physical inspections for PHAS scores to be issued by December 1999 will be conducted during the period July 1999 through September 1999. Before implementation of PHAS, HUD may conduct inspections and issue advisory scores to PHAs. This would enable PHAs to see how they will be assessed under the new rule and make necessary adjustments before HUD conducts inspections which will be reflected in the new PHAS score.

*Questions Regarding Statistically Valid Sampling.* Several commenters asked what constitutes a "statistically valid sample" for purposes of the PHAS physical condition inspection; what methods would be used to select PHA units; and whether HUD would also use samples of areas other than units, or would instead inspect all such areas. One commenter wrote that the inspected sample should reflect the differences in a PHA's housing stock, which may contain both high rise and garden style developments. One of the

commenters supported the random selection of samples from all developments within each PHA jurisdiction. This commenter wrote that physical condition and resident attitudes vary between developments; and that sampling a subset of a PHA's development would not be truly representative of housing conditions and resident attitudes.

The statistically valid sample will be based on inspecting the number of units necessary for estimating the physical inspection score for a property within two percentage points at a 95% confidence level. Units that will actually be inspected will be selected at the time an inspector arrives on site. The new software will contain a "random unit generator" that will be used to select units. The inspector will inspect the randomly selected units along with all other components in their associated buildings (e.g., building exterior, building systems, common areas, etc). The inspector will inspect the entire site of the project being inspected.

The sampling methodology does differentiate between those buildings with four or more floors and all other buildings. While it is true that there are differences among developments in physical condition of the units and attitude of the residents, HUD believes that use of the statistically valid sample will result in an accurate assessment of the units in a PHA's stock.

*Questions Regarding the Timing of Inspections.* Several commenters raised questions regarding the timing of PHAS physical condition inspections. Two commenters wrote that the timing of inspections will have an impact on the outcomes in many climates, and inspections should be adjusted to take into account climate impact on outcomes. Two other commenters noted that under most leases, a PHA must provide notice to its tenants of any inspections, and recommended that HUD take tenant notification into account in scheduling inspections. One commenter asked whether HUD would provide a PHA with ample time to reschedule any postponed inspections or simply use a smaller sample size.

HUD acknowledges that the timing of the inspection could impact the inspection results of certain items (e.g., inspecting heating systems in the summer). It is HUD's intent to schedule inspections to coincide with the end of the PHA's fiscal year so as to provide consistency between the timing of the various components of the assessment. Seasonal problems as described by the commenters are unavoidable. In these cases, HUD would not, for example,

expect the PHAs to start the heating plant in the middle of the summer. The inspector would only make visual observations for deficiencies and examine any certificates that the PHA may have obtained under a maintenance contract or city inspection.

HUD anticipates that PHAs will have at least five calendar days advance notice prior to the time of inspection to provide notification to residents. If there are scheduling conflicts, the PHAs and contractors are expected to work together to arrange a mutually agreeable date within the general time frame of the originally scheduled date. HUD does not expect that extended delays in rescheduling (e.g., weeks or months) will be permitted.

*Questions Regarding the Cost of Inspections.* Several commenters raised questions regarding the cost of the physical condition inspections. Three commenters wrote that if PHAs incur significant new expenses connected with the inspection process, they should be reimbursed in operating expenses. Another commenter wrote in opposition to the requirement that all PHA properties be inspected by an independent HUD inspector. The commenter stated the cost of paying for these private inspections could be better utilized by local housing authorities.

Under PHMAP, PHAs are required to conduct inspections of 100% of the units in their inventory, and no additional operating subsidies are provided as a result of the PHMAP rule. The PHAS rule requires PHAs to use the new physical inspection standard as the minimum physical quality standard in lieu of HQS. PHAs are not required to use the new HUD software. PHAs may continue to inspect using whatever means they are currently using (e.g., their own staff contract inspectors, etc.). As a result, PHAs should not incur significant new costs as a result of the new rule.

With respect to HUD's independent inspection of public housing, HUD has an obligation to ensure that all PHAs are complying with the law and contracts in the provision of decent, safe and sanitary housing. The methodology used by HUD in the past, where only a limited number of PHAs were visited by HUD, was the subject of considerable criticism from Congress, the General Accounting Office, and the HUD Inspector General. The new methodology is intended to address those criticisms and provide credibility to HUD's method of assessing PHA performance.

*Questions Regarding Inspector Qualifications.* Several commenters raised questions regarding the

qualifications of the independent inspectors contracted to perform the physical condition inspections. One commenter noted that PHAs must comply with State and local laws, and asked whether the inspectors will be trained in building and maintenance codes for each State and locality. Another commenter asked how HUD would exercise quality control over the contracted private inspection firms. The commenter also questioned whether PHAs would be provided an opportunity to review and comment on the quality control standards. One of the commenters wrote that the inspectors will need to be able to distinguish between day-to-day maintenance items and deferred maintenance items.

Contractor qualifications include, at minimum, the following: high school education or equivalent; specific technical knowledge in major building trades used in residential construction, including foundations, structures, framing, roofing, plumbing, heating, air conditioning, interiors, insulation and ventilation; general personal computer (laptop) skills including familiarity using Windows 95 (or later versions) software or equivalent environment; and experience, within the past three years, demonstrating sufficient knowledge of multifamily housing and public housing properties. The qualifications also may include experience as a construction inspector of multifamily real estate properties for determining compliance with construction requirements and/or a superintendent of construction for a builder of multifamily properties, or a record of performing acceptable multifamily property inspections.

The new physical inspection standard, as was the case with the HQS, is not intended to be a local code inspection. Instead, the inspection is only intended to determine compliance with the Federal physical standards. It would be impractical to expect the inspector to determine compliance with local codes.

HUD will use its own staff in the REAC to perform Quality Assurance (QA) inspections of work performed by private contractors. The HUD QA inspectors will follow behind contract inspectors within a period of approximately 48 hours and inspect the same properties and units inspected by the contract inspector. HUD will then compare the results of the QA inspector and the contract inspector to determine if the contractor is inspecting using the HUD inspection protocol and software properly. HUD will take appropriate action where it finds problems with the quality of the contract inspector's work.

There will not be a need to distinguish between day-to-day maintenance and deferred maintenance. The condition of the property at the time of the inspection will be recorded regardless of why the condition exists or any plans for correction.

**Rating Criteria are Vague.** Several commenters wrote that the proposed rule was unclear regarding how the physical condition component would be scored and weighted. These commenters asked that HUD provide a definition of the term "good repair."

PHAs will be judged on how well they maintain their properties in the context of the specific inspectable areas and inspectable items identified in the new physical inspection standard. It will be the responsibility of the PHA to maintain all components of each property. HUD does not intend to provide the details of the scoring algorithms at this time. HUD is providing the approximate relative weights/points of the five inspectable areas to give PHAs a general indication of importance of those areas and the direction of how the scores will be derived. HUD plans to constantly analyze the scores and make adjustments to ensure validity. In addition, the relative weights/points may change with some properties because, for example, they do not have common areas. In these cases, the available points will be redistributed among the remaining inspectable areas. PHAs that maintain their properties in decent, safe and sanitary condition will not be significantly adversely affected by HUD's approach.

#### APPROXIMATE RELATIVE WEIGHTS/ POINTS

Inspectable area	Approx. points
• Site (plus 1 pt. for physical condition and neighborhood environment) .....	4.5
• Building Exterior (plus 1 pt. for physical condition and neighborhood environment) .....	4.5
• Building Systems .....	6.0
• Dwelling Units .....	10.5
• Common Areas (plus 1 pt. for physical condition and neighborhood environment) .....	4.5

In addition, health and safety deficiencies will result in reductions to the total physical inspection score which takes into account the five areas, above, with their approximate relative weights.

**Negative Effect on Resident Surveys.** A few commenters expressed concern about the potential negative impact of

the physical condition inspections on resident satisfaction surveys. One commenter wrote that the PHAS inspection would cause resident disruption that could be reflected in the resident survey. Another commenter asked whether HUD had considered the effect multiple inspections will have on some residents of public housing.

HUD's independent physical inspection of public housing will not have a direct effect on the resident survey score. The physical inspection score will be derived based on the results of the observations recorded during the physical inspection. The comments obtained by the PHA during its survey of the residents are intended to be used by the PHA management to assist it in assessing its operations and determine where improvements are needed.

HUD considered the effect of multiple inspections on residents, but concluded, as advised by PHAs, that residents are already subject to multiple inspections (e.g., annual unit inspections, housekeeping, preventative maintenance, etc.). Since the purpose of the HUD inspection is to ensure that the resident is living in decent, safe and sanitary housing, it should not pose a major problem for the residents.

**Inspection "Snapshot" Might be Inaccurate.** Two commenters wrote that HUD's inspection would only provide a "snapshot" of the property's physical condition. The commenters expressed concern that this one-time snapshot might be misleading. One of the commenters recommended that PHAS allow for any deficiency to be abated or corrected and for the unit to then be reinspected. According to the commenter, this is the current practice under HQS. The commenter also wrote that if uniform physical condition inspections do not allow for such corrections, they might have a significant negative impact on a PHA's score.

All inspections are "snapshots" in time. That is the nature of inspections and is no different than any other inspection previously performed by HUD, the PHA or the residential inspection industry at large. As a result, HUD does not agree that the HUD inspection would be misleading. HUD's independent inspection should accurately represent the condition of the property at the time of the inspection. Conversely, HUD believes that it would be misleading to conduct the inspection, allow correction of deficiencies, and then conduct a reinspection of the unit with a resulting higher score as suggested in the comment. PHAs will be provided with the results of the

inspection, and it will be the responsibility of PHAs to take any necessary corrective actions at that time. HUD Field Offices will work with PHAs to ensure that corrections are made in a timely manner.

**Need for Exit Conferences.** A few commenters recommended that HUD conduct post-inspection conferences with PHAs. One commenter stated that these exit conferences would eliminate unnecessary appeals by allowing local authorities to review the results with the inspecting group/auditor.

HUD appreciates the recommendation, but notes that PHAs are required to designate a representative to accompany the inspector during the entire inspection. As a result, the PHA representative will be aware of the inspection and be able to provide any clarifications that may be required during the inspection. The PHA representative will be provided with a notice of life-threatening health and safety deficiencies observed during the inspection. Shortly after the inspection, the PHA should be able to obtain the detailed results of the inspection directly from the HUD web page. The PHAS provides for no appeals of the inspection results. Instead, a PHA may, as provided in the statute, appeal its overall score if the score results in a troubled designation. As a result, HUD does not plan to require formal "exit conferences."

**Accounting for Lack of Modernization Funding.** Several commenters asked HUD to specify how the lack of modernization funding would be taken into account by PHAS. The commenters were particularly concerned about smaller agencies that, according to the commenters, often only succeed in getting emergency items funded.

The purpose of the physical inspection is to determine the condition of the PHA's housing stock. HUD provides an adjustment, as required by statute, for physical condition and neighborhood environment. HUD did not adjust for the lack of past or present funding under PHMAP and does not intend to do so under PHAS as it would misrepresent the assessment of the condition of the PHA's portfolio.

**HUD Should Rely on Certain Professional Inspection Certifications.** Two commenters wrote that some mechanical and electrical systems could not be satisfactorily inspected visually. The commenters suggested that HUD's contract inspectors should rely on the PHA's records of inspections by appropriate professionals or other qualified inspectors not employed by the PHA. Another commenter wrote that local inspections and certifications



should be sufficient for many of the health and safety systems.

HUD agrees with the commenters, and the inspection software permits the acceptance of certifications from appropriate professionals for such items as elevators, boilers, fire extinguishing equipment, etc.

*Need for Comp Grant Waiver.* One commenter recommended that HUD grant a waiver of conditions observed in a unit or project element scheduled to be corrected pursuant to an approved Comprehensive Grant (Comp Grant) 5-year plan or otherwise identified in the needs assessment.

HUD believes that adopting this comment would result in a misleading score with respect to the current condition of the property. If the PHA has identified an item(s) for correction in its Comp Grant 5-year plan or a needs assessment, there will be little or no corrective action to be taken by the PHA until such time as the deficiencies are corrected. Once the deficiencies have been corrected and the property is inspected, the resulting score should properly reflect the then current condition of the property.

*Comments Regarding Adjustment for Older Housing.* Several commenters raised concerns regarding the PHAS adjustment for physical condition and neighborhood environment. These comments included: statements that the three point physical condition adjustment for older housing stock was vague; questions about the kind of documentation that will be necessary to demonstrate eligibility for the three points; concerns that the three-point adjustment that would be provided under the PHAS rule might violate the statutory PHMAP requirements; concerns that giving bonus points for authorities with older units in a state of ill repair penalizes authorities that strive to keep their property in good repair; recommendations that the adjustment should not be limited to three points under the physical condition indicator, but should continue to apply as under PHMAP; and recommendations that HUD should limit the adjustment to those PHAs that have a financially feasible plan for the renovation of the project.

The comments on this adjustment factor reflect that the industry has differing views regarding the statutorily mandated adjustment. HUD believes that it has taken a reasonable approach to implementing this requirement. HUD disagrees that this provision is vague. This PHAS provision is similar in nature to that which was required under PHMAP and will require similar documentation. Since the requirement

is statutory, HUD is obligated to permit the adjustment and, therefore, cannot accede to those who object to the adjustment.

HUD has determined that this provision does not violate the statutory requirement. In addition, HUD has limited the adjustment to the physical condition of the property because that is the most appropriate place where the PHA has limited control over "physical condition and neighborhood environment." PHAs have direct control over other areas of the PHAS assessment and the scores in those areas should not be adjusted for "physical condition and neighborhood environment."

#### *D. Comments on Subpart C—PHAS Indicator #2: Financial Condition*

*This Indicator Lacks Necessary Details About the Requirements and the Change to GAAP Will Be Significant for the Vast Majority of PHAS In Terms of Time and Cost, and the Implementation Date Is Not Realistic.* A number of commenters raised various concerns about this indicator. Comments on this indicator included statements that: this PHAS indicator provides little more than a conceptual framework with little attention to details; no information has been provided to explain what electronic transmission of financial data means or how this is to be done; the change to GAAP would be significant, burdensome, costly, time-consuming and the implementation date in the rule is not realistic; GAAP will require the education of PHA staff and fee accountants, and the conversion of most PHA accounting software applications; even though the rule states PHAs will not be scored under PHAS until September 30, 1999, giving the appearance of a one year period, the actual implementation for some PHAs will be October 1, 1998, the beginning of the period to be assessed, and this is not a realistic and logical date for implementation; conversion to GAAP should not be required until January 1, 2000, or later.

The GAAP conversion process entails only year-end adjustments to convert the PHA's record-keeping so information may be reported under GAAP. It does not require the wholesale conversion of PHA accounting software in order to meet the mandated schedule. The reporting under GAAP is being required for all PHAs with fiscal years beginning October 1, 1998 and thereafter. Therefore, the first unaudited financial statement information that must be submitted to HUD under a GAAP basis is not due until November 30, 1999. HUD strongly believes that the time frame is sufficient and realistic for

all PHAs to be able to convert to GAAP and accordingly report their results. PHAs are not required to change their current accounting and record keeping systems. They are only required to do so to report their information using GAAP as the accounting basis.

As stated in the proposed rule, PHA and industry representatives preferred GAAP accounting as more meaningful and widely accepted. Reporting results under GAAP offers the following benefits: allows for financial consistency among PHAs; provides a common mechanism for HUD to fairly and accurately assess the financial condition of each PHA as compared to its peers; and presents a more accurate picture of PHA financial condition by accounting and accruing for all liabilities that may exist. With respect to costs, additional GAAP-related audit costs will be covered by the PFS.

To facilitate and help each PHA in its conversion, HUD has developed a detailed GAAP Conversion Guidebook that is available on the Internet. It can be accessed at: (<http://www.hud.gov/reac/reafin.html>). In addition, a help desk (The REAC Service Center) is available to answer any GAAP related questions. A toll free number is provided (1-(888) 245-4860).

*The Benefits of GAAP Are Not Clear for PHAs.* Other commenters stated that the benefits of converting to GAAP for PHAs are not clear. Comments and questions included the following: allowance for depreciation schedules, required under GAAP accounting, have no value to PHAs and should not be required; guidance relative to the depreciation of assets (including those purchased in prior years) is needed; GAAP may create liabilities against reserves that were not previously considered under HUD's chart of accounts; how will bad debts be uniformly quantified; what will be the impact of conversion on first year expenses for depreciation, vacation and sick leave accruals; must PHAs quantify the present value of a guaranteed ACC; and how will first year paper conversion costs affect PHAs. Commenters also stated that neither PHAs nor HUD can know the effect of conversion to GAAP; that the effect will vary depending on the policies of each authority in the areas of sick leave, annual leave, collection of bad debts, etc. Other commenters asked HUD to explain how it will maintain consistency among PHAs in accounting and financial reporting under governmental accounting.

With respect to depreciation, GASB-GAAP requires depreciation under the Enterprise Method and permits the

recording of depreciation under the Governmental Method. HUD strongly prefers that under both the Governmental and Enterprise methods, each PHA depreciate its fixed assets over their useful lives. HUD prefers that each PHA record depreciation because of the benefits associated with recognizing depreciation. Recording of depreciation provides each PHA with a systematic allocation method of showing the cost of an asset over its useful life. The recording of depreciation permits each PHA to show the directly related consumption of the asset over the periods in which the asset is used. Financial indicators are designed so as not to be impacted by the PHAs decision whether to record depreciation or not to record depreciation. Examples of depreciation of assets is as follows:

National Council on Governmental Accounting Statement (NCGAS) 1, *Governmental Accounting and Financial Reporting Principles*, states that while depreciation expense cannot be recorded in a governmental fund, accumulated depreciation may be reported in the General Fixed Assets Account Group. Reporting accumulated depreciation in the account group is not mandatory. If the governmental unit decides to report accumulated depreciation, follow the conventional accounting standards with respect to acceptable depreciation methods, economic life, and estimated salvage value.

Under NCGAS 1, all depreciable property of an enterprise fund must be depreciated in accordance with GAAP as applied by a commercial enterprise. Depreciation on fixed assets of a proprietary fund must be shown as an expense on its operating statements, with appropriate disclosures in the financial statements.

Depreciation including suggested entries and conversion guidance is explained in depth in the HUD-GAAP Conversion Guide. The GAAP conversion guide also discusses composite depreciation. For practical purposes, property items frequently are grouped and an average life applied to determine depreciation. Groupings may be by year of acquisition, by type (all cars), by classification (all equipment), by location, or by a combination of these ways. Depreciation based on groups that include items with varying lives is referred to as composite depreciation. No gains/losses should be recognized on normal dispositions when this technique is used.

With respect to the chart of accounts, the Chart of Accounts has been revised to reflect additional accounts that may

be needed by each PHA. The use of the revised accounts permits each PHA to present a more accurate picture of its financial condition using GAAP.

On the question of bad debts, both the Governmental Method and the Enterprise Method required the development of an allowance for uncollectible accounts receivable. For the Governmental Method, NCGA Statement No. 1, *Governmental Accounting and Financial Reporting Principles*, requires that an allowance for uncollectible accounts be established for potentially uncollectible amounts. For the Enterprise Method, SFAS No. 5, *Accounting for Contingencies*, guides the establishment of the allowance for uncollectible accounts for potentially uncollectible amounts.

To provide for all reasonably anticipated losses inherent in the receivable balances that will not be collected, a PHA must "establish an allowance for uncollectible (or doubtful) accounts." When calculating the size of the reserve, each PHA should consider such factors as the current accounts receivable aging and the historical collection experience. The following provides an example of a calculation methodology:

1. Group the receivables into these categories:

Current receivables

Receivables less than 90 days

outstanding, but not current.

Receivables 90—180 days outstanding.

Receivables over 180 days outstanding.

2. Identify all receivables that are known to be uncollectible or that the probability of collection is very low.

3. For those receivables identified in item 2, establish a reserve for the estimated amount that will not be collected.

4. Based on the receivables in the groups shown above in item 1 that were not specifically identified in item 2, establish an overall additional reserve for each category.

Again, this is just an example. The method used by each PHA could change based on its specific circumstances.

With respect to vacation and sick leave accruals, GAAP provides as follows:

*Vacation Leave and Other Compensated Absences with Similar Characteristics.* Accrue these types of compensated absences as a liability because employees earn these benefits by meeting both of these conditions: (1) The employees' rights to receive compensation are attributable to services already rendered; and (2) it is probable that the employer will compensate employees for the benefits

through paid time off OR some other means, such as cash payments at termination or retirements.

*Sick Leave and Other Compensated Absences with Similar Characteristics.* If paid time off is contingent on a specific event outside the control of the employer and employee (jury duty, for example), other compensated absences have characteristics similar to sick leave. If it is probable that the employer will compensate employees for the benefits through cash payments conditioned on the employees' termination or retirement, accrue a liability as the benefits are earned by the employees

First year experience regarding the impact of converting to GAAP reporting will vary. The recording of GAAP accounts will have an impact on the financial indicator results under GAAP versus PHMAP. This recording of new liabilities and contra assets amounts will be reflected in the first year financial indicator results and the overall score given to each PHA.

With respect to the PHA's ACC, the conversion to GAAP will have an impact on the ACC when the PHA converts to accrual accounting since you accrue receivables and defer revenue in anticipation of the actual receipt of the revenue.

On the matters of the effect of the conversion to GAAP and maintaining consistency in reporting under GAAP, HUD points out that GAAP permits choices among acceptable options for certain accounting transactions. Because the purpose of converting to GAAP is to achieve uniform and consistent financial data from all PHAs, HUD has selected preferred options for those transactions where GAAP allows a PHA to choose from more than one method. For these transactions, HUD strongly encourages PHAs to choose the HUD-preferred option.

PHAs can project in large measure how their financial position will be affected by the major GAAP provisions. HUD has taken into consideration the anticipated effects of converting to GAAP and the reporting of results using GAAP. The scoring mechanism will reflect the adjustment to GAAP.

*Clarification of Certain Aspects of GAAP Are Necessary.* Other commenters asked specific questions about certain aspects of GAAP or asked for clarification of certain points. The commenters stated that HUD should clarify its position as to what constitutes GAAP because in the proposed rule for Uniform Financial Reporting Standards, HUD refers to GAAP as being prescribed by GASB and FASB but these are two different standard setting bodies with

differing jurisdictions. Another commenter requested that HUD permit the use of Enterprise GAAP. Other commenters stated that GAAP will require PHAs to keep two sets of books.

HUD's rule on Uniform Financial Reporting Standards covered private entities as well as PHAs, and under GAAP, the accounting principles and financial reporting standards are established by the Governmental Accounting Standards Board (GASB) for governmental entities, and by the Financial Accounting Standards Board (FASB) for nongovernmental entities. Since the PHAS rule is only applicable to PHAs, HUD uses the term "GASB/GAAP" in this final rule. GASB permits two types of reporting mechanisms, the Governmental Method and the Enterprise Method. The use of either method is acceptable to HUD. In fact, HUD is not requiring one method over the other. Each PHA has the discretion to determine its own method. The guiding criteria should be the type of activities performed by the PHA. That determination will drive which method most accurately provides the reader of the financial statements with a clear understanding of the PHA's operations and financial results.

With respect to bookkeeping, PHAs will not be required to keep two sets of books to comply with GAAP. HUD does not require a change to recordkeeping as part of the GAAP provision. In addition, HUD is revising financial reporting requirements to eliminate obsolete forms and requirements.

*HUD Must Clarify the Compensation of the Costs of the Conversion.* There were several comments on whether HUD would pay for the software and upgrading of PHA computers for the electronic submission, and the costs of converting their accounting systems to GAAP, or if additional operating subsidy to cover these costs would be provided through PFS "add-ons."

Additional GAAP-related audit costs will be covered by the PFS.

*The New Financial Reporting Requirements Constitute an Unfunded Mandate.* Related to the issue of compensation costs are comments that stated the conversion to GAAP or the requirement to submit financial reports electronically constitute an unfunded mandate.

Additional audit costs, if any, associated with GAAP related audits, will be covered by HUD as a PFS add-on. These additional audit costs, if any, are anticipated to be minimal.

*Significant Training, Assistance and Guidance Will Be Necessary to Make the Conversion Work.* Commenters asked HUD to clarify what training and

assistance HUD would make available to assist with the conversion to GAAP and electronic submission, and when such technical assistance would be available.

The HUD-GAAP Conversion Guide for PHAs, now on the Internet, provides an in depth discussion of GAAP conversion including suggested accounting entries. The Guide includes sample journal entries and suggested GAAP conversion procedures. PHAs that have specific questions not addressed in this Guide, contact the REAC Service Center Help Desk (1-(888)-245-4860) and answers will be provided. HUD is providing 24-hour on-line assistance on the GAAP Conversion Guide at our Web site (<http://www.hud.gov/reac/reafin.html>). Additionally, industry specialists have developed and prepared a schedule of a comprehensive training program designed to explain how a PHA should convert its records and reporting to GAAP. HUD will supplement this training with its own training program.

*Small PHAs Are Largely Not Automated and Will Have Difficulties Complying with the New Reporting Requirements.* A few commenters expressed the concern about the impact of this Indicator on small PHAs that may have difficulty complying with the electronic reporting. The commenters asked who will supply and pay for software necessary for electronic submission.

HUD disagrees with the commenters that small PHAs will be adversely affected by PHAs Indicator #2. First, PHAs have a year before reporting in GAAP is required. Second, HUD notes that the Single Audit Act Amendments of 1996 raised significantly the monetary threshold for when an entity that receives Federal assistance is required to have an audit. The threshold was raised from \$25,000 to \$300,000. This change significantly reduces reporting costs for small entities. Therefore, although small entities must continue to submit an annual financial report to HUD, an audited report is not required. Third, although HUD has clearly expressed a preference for internet submission of financial reports, the rule provides that HUD will approve transmission of financial data by tape or diskette if HUD determined that the cost of electronic internet transmission would be excessive. Additionally, to further ease any administrative burden on small PHAs, and all PHAs, HUD will provide submission software, supplemental guidance, training and other technical assistance.

*What Protections Will Be in Place to Protect the Standardized Electronic Format from Viruses, Corruption.* Some

commenters expressed concern with the use of any standardized electronic format due to the potential of viruses or corruption.

To ensure security against computer viruses, HUD systems scan incoming data for viruses. Similarly, PHAs should ensure that data being transmitted is free of viruses.

*Final Rule Should Provide for HUD Confirmation of Receipt of Electronic Report.* Other commenters requested that HUD confirm that it has received the electronically transmitted data, and that the data are readable, correct, and accurate. The commenters stated that confirmation should be done quickly so that any transmission problems can be corrected without consequence.

HUD will give PHAs read-only systems access to view their submitted data via the Internet. It is planned that PHAs will receive a written report on HUD's financial assessment within a reasonable period of time.

*The Final Rule Should Address PHA Access to the Electronic Report.* A few commenters suggested that once a PHA has input adjustments, it should be provided read-only access to the HUD system in order to make the data most useful to it. Access to system data is not addressed in the proposed rule.

A PHA will have read-only access once the data is accepted in the system.

*The 60-Day Turnaround Time to Submit Unaudited Statements Is Inadequate.* Some commenters stated that the 60-day turnaround time to submit unaudited financial statements after the PHA's fiscal year may not be enough time to prepare a thorough submittal, especially for those PHAs that are converting to GAAP. They stated that PHAs should be given 100 days to submit their unaudited financial statements.

HUD strongly believes that 60 days following the fiscal year-end is sufficient for the preparation and submission of unaudited financial statements. Audited results need not be submitted until 9 months following the close of the PHA's fiscal year-end. HUD encourages each PHA to work with its IPA to develop procedures designed to calculate GAAP entries which will facilitate closing procedures. In addition, HUD suggests that each PHA work with its respective IPA firms developing the specific closing procedures each must use so the required information will be available 60 days following the fiscal year-end close. HUD recommends that this planning process occur early during the fiscal year to facilitate the data gathering and financial reporting methods.

*The Financial Standards Should Be Applied to all Programs Administered by PHAs.* A few commenters stated that the financial standards should be applied to the public housing entity as a whole, not just certain federal programs. The financial standards should be applied to all programs managed by the PHA, including public housing.

HUD agrees that financial assessment and the resulting financial indicators will be applied to the entity as a whole and not just to each respective Public Housing program. The Supplemental Financial Data Schedule provides a summary of each HUD program and other Federal, State, local or private funding sources.

*Final Rule Should Make Clear That a PHA's Financial Reporting Is Limited to Public Housing Programs.* Other commenters stated that the final rule should make clear that a housing authority's financial reporting on liquidity and viability will be limited to public housing program operations and will not include the housing authority's non-public housing operations or the Authority's capital programs.

HUD believes that the financial health of the PHA can only be accurately determined by assessing all aspects of the PHA, including non-public housing and capital programs.

*How Will the Six Major Components of This Indicator Be Scored?* Several commenters asked how each of the six major components of this indicator will be scored, and what weights will each of them have.

To evaluate the financial health of the nation's PHAs, REAC will assess and analyze the GAAP-based financial statements submitted each year. REAC will analyze this information using a specific set of financial indicators that focus on: (1) *Liquidity measurement*—evidence of the PHA's ability to cover its near term obligations; (2) *Viability measurement*—evidence of the PHA's ability to operate using its fund balance without relying on additional funding; (3) *Days receivable outstanding*—measures the PHA's ability to collect its tenant receivables in a timely fashion; (4) *Vacancy loss analysis*—measures the extent to which the PHA is maximizing its revenue from operations; (5) *Expense management per unit*—provides a measure of the PHA's ability to maintain its expense ratios at a reasonable level relative to its peers (adjusted for size and region); and (6) *Net income (loss)*—provides a measure of how the year's operations have affected the PHA's viability.

Financial scores will be determined as follows: (1) *Liquidity measurement*—

Adjusted Current Ratio with a maximum score of 9; (2) *Viability measurement*—Number of months operating expenditures in Expendable Fund Balance with a maximum score of 9; (3) *Days receivable outstanding*—Days Receivables Outstanding with a maximum score of 4.5; (4) *Vacancy loss analysis*—Total vacant potential revenue to gross available revenue with a maximum score of 4.5; (5) *Expense management per unit*—Expenses by category divided by total number of units with a maximum score of 1.5; and (6) *Net income (loss)*—Net income (loss) for the year compared to Expendable Fund Balance with a maximum score of 1.5.

Therefore, the maximum score a PHA may receive for its Financial Condition is 30 points. In order to receive a passing score, on the Financial Condition Indicator, a PHA must receive a score of at least 60 percent (60%), or 18 points of the 30 points available.

*Why Did HUD Not Adopt a Risk Management Approach Using Two Threshold Indicators on Cash Reserves and Assets Plus an Audit?* Two commenters asked why HUD did not rely on a risk management approach using two threshold indicators on cash reserves and assets plus an audit.

HUD believes that additional indicators were needed to ensure a full and fair assessment of PHAs' financial condition and provide a basis to compare each PHA to its peer group. While the two-tiered approach will not be used, point availability is weighted toward the first two indicators since Liquidity and Viability are significant predictors of the overall financial health of a PHA. The remaining four financial indicators provide additional assessment capability when determining the total financial health of a PHA. If a PHA receives high scores on the first two indicators, it is likely that it will receive high marks on the remaining four.

*What Additional Components Will Be Used To Identify Waste, Fraud or Abuse.* Commenters asked what "flags" HUD will use to determine when the "possibility" of waste, fraud, or abuse exists, and what types of additional components may be used.

As part of the analysis of the financial health of a PHA including an assessment of the potential or actual waste, fraud or abuse at a PHA, HUD will look to the Audit Opinion to provide an additional basis for accepting or adjusting financial indicator scores. The following is a summary of the types of audit opinions and the number of total financial points

that will be deducted if a PHA receives such an audit opinion from its IPA:

Type of flag	Score <sup>1</sup>
Clean opinion .....	0
No audit opinion .....	30
Adverse opinion .....	30
Disclaimer of opinion .....	30
Qualified opinion .....	(2)
Going concern opinion .....	(2)
Material weakness in internal control .....	(2)
Reportable condition .....	(2)
Findings of non-compliance and/or questioned costs .....	(2)
Indicator outlier analyses .....	(2)

<sup>1</sup> Financial Condition points that will be deducted from the PHA's overall financial score.

<sup>2</sup> If points remain, further deductions can be made dependent upon the specific nature of the information reported under this flag.

*Final Rule Should Clarify That if PHA Scores Very High on Liquidity Measure, It Will Not Be Assessed on Remaining Components.* A few commenters suggested that if a PHA scores very high on the liquidity measure [Current Ratio and Number of Months Expendable Fund Balance], the PHA should not have to be assessed on the remaining [components of PHAS Indicator #2].

HUD, the industry and those PHAs who participated in the development of this proposed rule strongly preferred the use of all six financial indicators. HUD strongly believes each PHA must be scored on all financial indicators to ensure a full and fair assessment of PHAs' financial condition and provide a basis to compare each PHA to its peer group.

*To Calculate Current Ratio, HUD Needs to Better Define Current Assets and Liabilities.* Other commenters stated that to calculate the current ratio, HUD will need to better define current assets and current liabilities. They noted that the current HUD chart of accounts does not define these terms nor does it provide the framework to categorize assets or liabilities as current or long term.

The adjusted current ratio is designed to show available unrestricted and unreserved current assets divided by the unrestricted current liabilities. The HUD Chart of Accounts has been revised to reflect new accounts that will help PHA to account for the information needed to perform this calculation. The Financial Data Schedule has also been revised so this information will be reported to HUD through electronic submission.

*It Is Not Clear What HUD Means by Expendable Fund Balance; and How Does HUD Propose to Calculate "Expendable" Fund Balance in an Enterprise Fund.* A few commenters stated that it is not clear if this fund

balance would be equivalent to cash reserve (just cash and liquid investments) or Operating reserve (i.e., working capital). Other commenter noted that the terminology "expendable" fund balance generally refers to the undesignated portion of unreserved fund balance in governmental funds such as the general fund or special revenue funds. They stated that under GAAP, most PHAs would likely classify their public housing programs as enterprise funds where fund balance or fund equity is generally comprised of retained earnings and contributed capital. They asked how HUD proposes to calculate the "expendable" fund balance in an enterprise fund.

The expendable fund balance is the unreserved and undesignated portion of fund balance (or retained earnings) representing expendable available financial resources. Under both the Governmental Method and the Enterprise Method of reporting, the expendable fund balance (expendable retained earnings for the Enterprise Method) simplistically refers to funds that are unrestricted and unreserved. Expendable fund balance is what is left after subtracting all other fund balances that are either reserved or restricted.

The expendable fund balance is the unreserved and undesignated portion of the fund balance (or retained earnings) representing expendable available financial resources. Under both the Governmental Method and the Enterprise Method of reporting, the expendable fund balance (expendable retained earnings for the Enterprise Method) simplistically refers to funds that are undesignated and unreserved. Expendable fund balance is what is left after subtracting all other fund balances that are either reserved or restricted.

*What Does HUD Mean by Liquidity Measurement and Range of Liquidity.* A few commenters asked what is meant by the liquidity measurement and noted that there was no mention of a range in regard to liquidity in the proposed rule.

Liquidity measurement refers to a PHAs ability to cover its near term obligations. It will be measured by using the adjusted current ratio that is designed to show available unrestricted and unreserved current assets divided by the unrestricted current liabilities. The HUD Chart of Accounts has been revised to reflect new accounts that will help PHAs to account for the information needed to perform this calculation. The Financial Data Schedule has also been revised so this information will be reported to HUD through electronic submission. The range is not a single amount or score,

but a tolerance between acceptable scores as grouped among peers (i.e., PHAs located within the same geographical region having similar characteristics).

*The Days Receivable Outstanding Component Is Not a Good Indicator of Financial Health—Does It Take Into Account Notice and Grievance Rights.* Some commenters stated that this component [Days Receivable Outstanding] will require extensive tracking and is not a good indicator of financial health. They stated that outstanding receivables are a result of various factors, some of which an agency cannot control, and that adding this factor creates another area where justification for bad results can affect the score. The commenter stated that if an organization is in good financial health, other indicators will clearly and easily point this out, and therefore this indicator should not be included. Another commenter asked whether this component takes into account the regulatory requirements for notice provisions, grievance rights of residents, and the judicial process?

HUD left "rents uncollected" due to statutory requirements. However, the old measure is not objectively measurable. It was left to allow PHAs to be measured on a basis each was familiar with. The "days receivable outstanding" ratio measures the PHA's ability to collect its tenant receivables in a timely fashion. It is HUD's strong belief that this information is already available to each PHA (or at the minimum, should be available). Since the calculation is done "Gross" each PHA should have the ability to control the days receivable outstanding. Any tenant receivable that ages beyond a certain number of days past its due date has to be questioned as to its collectibility.

*Discard Tenants Receivable Component; What Is Wrong With Existing Receivables Measures.* Some commenters suggested that HUD discard the "tenants receivables" component because it would reinstate the objectionable "Tenant Account Receivables (TARS)" indicator from the original PHMAP rule. They said that in order to comply with the current PHMAP requirements, PHAs had to rewrite computer software that would distinguish between the different types of receivables (rents, maintenance charges, other charges, etc.). The commenters asked what was wrong with the existing measure?

Under GAAP, the collectible portion of each component within A/R must be determined. Each PHA should develop an allowance that will permit that entity

to reflect only the collectible portion of A/R. Tracking days under GAAP is an important measurement tool to estimate the collectible portion of the A/R that should be reported.

*Certain State Laws Concerning Tenant Rents May Penalize PHAs under Financial Indicators.* One commenter stated that housing authorities in North Carolina are required by State law to apply tenant payments to any rent balance before applying them to other charges that may be older; this leaves old balances on the tenant's accounts; and would penalize such a PHA when other authorities do not have the same legal requirements. The commenter stated that it is likely other States have other restrictions that would affect the PHAs in those areas.

If PHAs in North Carolina are required by State law to apply tenant payments to any rent balance before applying them to other charges that may be older thereby leaving old balances on the tenant's accounts, those PHAs may not be accounting for the tenant payments in conformity with GAAP. HUD suggests that those PHAs check with their IPA for additional guidance.

*There Are Several Problems With Vacancy Loss Component.* Several commenters stated there were problems with the vacancy loss component. Their comments included the following: it is impossible to define potential rent or compute vacancy loss; vacancy loss has questionable usefulness in public housing—given PHAs' reliance on operating subsidies which continue through normal vacant unit turnover, "lost rental income" or "vacancy loss" are not useful measures of an agency's financial health; how is potential rent calculated in a system where rent payable is a function of income and not based on unit size, location, condition or other typical market factors; vacancy loss should be eliminated, because rent is unknown until calculated for a specific unit with a specific tenant; PHAs that encourage families to become self-sufficient and move up to private housing may suffer multiple deductions to their PHAS score under two indicators [vacancy loss at § 902.35 (formerly § 901.35) and vacancy rate and turnaround time at § 902.43 (formerly § 901.43)]; the inclusion of the vacancy loss component under financial condition appears redundant—vacancy statistics are already measured under "management operations," and should remain there; and the vacancy loss indicator represents the loss of potential rent due to vacancy, but the proposed rule does not indicate how potential rent loss will be calculated. With respect to this last comment, the

commenter stated that vacancy losses are commonly used in rental projects using contract rents where the amount of loss revenue can be easily calculated. Public housing projects do not use contract rents because rents are based on tenant incomes.

With respect to these comments, HUD points out that the vacancy statistics measured under "Management Operations" will look at a formula to assess the reduction in the number of units that are vacant. The unit turnaround time measures the annual average of the total number of turnaround days between the move-out date and the date a new lease takes effect. Vacancy loss measures the loss of potential rental income due to vacancy. The calculation for this indicator is potential rent divided by gross potential rent. The gross potential rent is estimated using the projected average rent contribution that is currently used to calculate operating subsidy through the Performance Funding System. HUD believes that is important to measure whether the PHA is both meeting its mission to house low income families while maximizing revenue obtained from rent.

*Comments on Expense Management Component.* There were also several comments and questions on the expense management component. Comments included: the proposed rule does not elaborate as to what key expenses will be analyzed or what standard they will be compared to such as budget, prior years or an industry standard; if an organization manages its finances well, the financial statements (which produce the first two indicators) will show this, and therefore how the funds are spent and classified should be left to the organization. With respect to the last comment, the commenter stated that money spent wisely will show in the financial statements and the physical condition of the property; therefore, this indicator should not be included.

HUD believes the use of expense ratios benchmarked against peers of similar size and programs is a valuable measure of efficiency. It permits HUD and PHAs to analyze information. The goal is to determine how efficient a PHA is, expense category by expense category.

The calculation is made by assessing the dollars spent per each unit for certain expense categories. The actual expense categories that will be measured are: administrative salaries; auditing fees; outside management fees; compensated absences; employee benefit contribution; tenant services; water; electricity; gas; fuel; utility labor and other; ordinary maintenance and

operations; protective services; insurance; bad debt; extraordinary maintenance; other operating expenditures; HAP payments; and fraud loss.

*Comments on Energy Consumption Component.* There were also several comments on the energy consumption component and these included the following: the energy consumption component should be measured only if a PHA fails a reserve-related component; what are the details of this component; and there is a point of diminishing returns below which it is not cost effective to do additional conservation measures—if all possible cost-effective measures have already been implemented, the PHA should receive a high rating for this component.

PHAs that have taken the initiative to complete cost effective energy conservation measures should compare favorably to their peers of similar size and region when measured by expense ratios.

*Comments on Net Income or Loss Divided by the Expendable Fund Balance Component.* Comments on this component included the following: the proposed rule states that the net income/loss divided by expendable fund balance indicator measures how the year's operations have affected the PHA's viability, however, it fails to adequately describe why or how this ratio hopes to accomplish that stated goal; exclude capital and nonroutine expenditures from this component; and the proposed factor of "Net Income or Loss divided by the Expendable Fund Balance" is not a valid or useful measure of a PHA's viability and should be eliminated—there are very valid long term planning implications relative to the fluctuations in expendable fund balance, such as accumulating dollars for a major capital activity over several years and then the single year when the event occurs, a major reduction of expendable fund balance shows up. The commenter of this last comment stated that if this ratio is to be used, it should be modified to reflect the results of each of the most recent three years.

Net income (loss) provides a measure of how the year's operations have affected the PHA's viability. It is intended to show how well the PHA has performed this year compared to its peers. The calculation will be made against the Expendable Fund Balance (or retained earnings) which is the unrestricted and unreserved portion of the total fund balance.

*Comments on Additional Components That May Be Added to Indicator.* A few commenters stated that they were concerned about the authorization to

REAC to create additional components and new components should be added after opportunity for notice and public comment. Other commenters asked what determines when additional criteria will come into consideration. Their comments are as follows: any further component, as well as any revisions to components should only be added following appropriate public notice and opportunity for comment; is there a set criterion for additional fraud detection components or will it be customized to the PHA; what determines when the additional criteria will come into consideration; and additional components may be used to detect fraud and may be used to provide a PHA with benchmark information to allow the PHA to measure its own performance against its peers but how are peers determined—by size, type of housing stock, age of the buildings?

HUD understands the concerns about additional components. As part of the analysis of the financial health of a PHA including an assessment of the potential or actual waste, fraud or abuse at a PHA, HUD will look to the Audit Opinion to provide an additional basis for accepting or adjusting financial indicator scores. Please see the discussion concerning what additional components will be used to identify waste, fraud or abuse, above, for a summary of the types of audit opinions and the number of total financial points that will be deducted if a PHA receives such an audit opinion from its IPA. The determination of PHA peers is done by comparing those PHAs with like programs that are similar in size (number of units).

#### *E. Comments on Subpart D—PHAS Indicator #3: Management Operations*

*HUD Should Allow PHAs to Develop Own Management Performance Standards.* A few commenters stated that HUD should allow PHAs to develop their own performance standards, based on local market conditions that can be documented, verifiable, and subject to HUD audit.

Section 6(j) of the U.S. Housing Act of 1937 establishes a method that uniformly assesses the management performance of PHAs. Not only does the PHAS assess a PHA's management performance that will be verified as part of the independent auditor's audit, it also provides for an independent third party assessment of the physical condition of a PHA's housing stock, independent third party assessment of financial operations, and a resident service and satisfaction assessment. REAC was created to effectively and fairly measure a PHA's performance

based on standards that are objective, uniform and verifiable. Standards based on local market conditions would not provide standards that are as uniform as possible.

*How Will Management Operations Performance Standards be Weighted and Scored?* Several commenters asked how each management indicator be weighted and scored? The commenters also asked for further information about the management indicators and suggested that the final rule should state that the PHMAP methodology, to the extent consistent with PHAS, will be preserved. Another commenter asked whether the definitions, exclusions and exemptions based on the existing PHMAP rule carryover into the new rule for this or any other PHAS indicator.

HUD notes that a listing of the approximate weights/points for each indicator, sub-indicator and component was provided earlier in this preamble. The approximate relative weights/points for the PHAS management operations indicator are listed below. Of the total 100 points available for a PHAS score, a PHA may receive up to 30 points based on Indicator #3, Management Operations.

#### APPROXIMATE RELATIVE WEIGHTS/ POINTS

Sub-Indicator/Component	Approx. Points
Vacancy Rate/Progress to Reduce .....	8.0
Vacancy Rate .....	(4.0)
Unit Turnaround Time .....	(4.0)
Modernization .....	6.0
Unexpended Funds .....	(1.0)
Timeliness of Fund Obligation .....	(1.5)
Contract Administration .....	(1.0)
Quality of the Physical Work .....	(2.0)
Budget Controls .....	(0.5)
Rents Uncollected .....	4.0
Work Orders .....	4.0
Emergency Work Orders .....	(2.0)
Non-Emergency Work Orders .....	(2.0)
Inspection of Units and Systems .....	4.0
Inspection of Units .....	(2.0)
Inspection of Systems .....	(2.0)
Security .....	4.0
Tracking/Rpt. Crime-Related Problems .....	(1.0)
Screening of Applicants .....	(1.0)
Lease Enforcement .....	(1.0)
Grant Program Goals .....	(1.0)

The PHMAP methodology, to the extent consistent with PHAS, will be preserved. The definitions and exemptions in the current PHMAP rule will also apply to the PHAS. The need for modifications and exclusions has been significantly diminished in the PHAS because all of the PHAS

indicators, sub-indicators and components will be independently verified by the third party independent auditor. Therefore, modifications and exclusions have been eliminated from the PHAS rule. A PHA's certification will be transmitted electronically to the REAC via the internet.

*What Does "Independent Verification" Mean?* A few commenters asked what is meant by the reference to "independent verification" and if the reference is to an auditor, what are the guidelines.

The independent auditor will verify all of the sub-indicators and components under the PHAS Indicator #3. The audit guidelines are as published in the OMB A-133 Compliance Supplement, dated May 1998. The PIH compliance supplement is in the process of being revised to reflect the PHAS.

*Comments on "Vacancy Rate/Unit Turn-around" Component.* There were several comments on the vacancy component of the Management Operations Indicator. One commenter stated that unit turn-around should be removed from PHAS. Another commenter stated that because vacancies are included in both Indicator #2, Financial Condition, and Indicator #3, Management Operations, this creates a level of confusion. The commenter asked whether vacancies is a financial concern or a management concern? Another commenter stated that the definition of vacancy rate needs to make clear that units off line are excluded. Other commenters stated that the rule does not state how vacancy/unit turnaround will be calculated. They noted that vacancy/unit turn-around varies with each tenant, and this hurts a PHA's score particularly if the previous tenant did serious damage to the unit. A couple of commenters remarked that the vacancy and unit turn-around indicators conflict with the lease enforcement and "get rid of the criminals" policies. They stated that PHAS should have at least one year from the date of eviction to reoccupy the unit without being penalized. Another commenter stated that there should be a management indicator for lease enforcement, and one questioned whether adjustments would be made for the "One Strike and You're Out" provisions that are currently in the PHMAP.

With respect to these comments, HUD notes that because unit turnaround time is a statutory factor, the Department cannot arbitrarily drop the assessment of this factor. In order for unit turnaround time to be eliminated, a change would have to be made to the

1937 Act at section 6(j). On the issue of possible duplicativeness of this component, HUD points out that PHAS Indicator #2, Financial Condition, analyzes vacancy loss, e.g., the amount of income lost due to units being vacant. Indicator #3, Management Operations, measures the rate of vacancies over the entire year being assessed. The definition of vacancy rate is the same as in the current PHMAP rule, e.g., the total actual vacancy days divided by the total days available for occupancy. The exemptions that apply to the current PHMAP will also apply to the PHAS. Vacancy rate and unit turnaround will be calculated the same as in the current PHMAP rule. A PHA will be required to certify to unit turnaround time, but it will not be scored on unit turnaround time unless it has less than a grade of C as stated in the current PHMAP rule.

Although unit turnaround time may vary with each resident, a PHA should be able to establish an average unit turnaround time that does not exceed 30 calendar days, which is the norm. Over the fiscal year being assessed, the cases of severe resident damage to a unit should be minimized through the provision of resident orientation, ongoing housekeeping education, prompt eviction due to lease violations and annual inspection of units. In addition, unit turnaround time is the average time it took for all units turned around during the fiscal year being assessed.

On the matter of lease enforcement, HUD believes that one year from the date of eviction to reoccupy a unit is an unreasonable amount of time. The current unit turnaround time component provides for an average of 30 calendar days between the time when a unit is vacated and a new lease takes effect for a grade of C. A PHA should be able to turn a vacant unit around, have a sufficient waiting list of applicants, and sufficient screening and intake procedures to enable it to lease a unit within 30 calendar days.

A management sub-indicator for lease enforcement will be considered as part of possible future changes to the PHAS. In order to make the transition from the PHMAP to the PHAS, it was determined to make as few changes as possible between the current PHMAP and the management operations indicator under the PHAS, but this is a valid comment, and HUD will consider this issue.

*Comments on "Modernization" Component.* Comments on this component are as follows. A few commenters stated that in assessing modernization, quality of physical work should be linked to the broad physical inspection conducted under the



physical condition indicator, and contract administration should be measured during the independent audit. They asked will the "quality of physical work" in modernization be done through the physical inspection. Other commenters stated that the physical condition of sites, rather than timeliness of expending modernization funds, should be the measure used to assess success of modernization. A few commenters objected to this indicator if HUD intends to expand the application of the modernization sub-indicator to the HOPE VI and Vacancy Reduction programs. The commenters stated that these programs are not universal but targeted to individual PHA needs and situations; and that the HOPE VI assistance program is a major program, distinct and separate from both the Comprehensive Grant Program and Comprehensive Improvement Assistance Program, which should be reviewed and rated separately under its own indicator.

HUD's response to these questions and concerns is as follows. The quality of the physical work will be examined as part of the annual modernization review of PHAs performed by the HUB/Program Center, with reports issued in accordance with the current PHMAP modernization indicator. PHAs will certify to responses that encompass all five modernization components, and a PHA's certification will be verified by the independent auditor's audit.

All five of the components under sub-indicator #2, modernization, are statutory; therefore, PHAs will be required to certify to this indicator under the PHAS. Sub-indicator #2, modernization, will examine the HOPE VI and Vacancy Reduction Program under components #3, #4 and #5 as in the current PHMAP program.

**Comments on "Rents Uncollected" Component.** Comments on this component are as follows. A few commenters stated that "rents uncollected" should be addressed in the Financial Indicator and moved from the Management Indicator. Other commenters stated that suspense accounts (accounts pending write off) should be deducted from rents uncollected. Some commenters stated the standard allowance for bad debts among many industries collecting money from a wide cross-section of incomes is 2%, and it does not seem reasonable to expect the same standard from PHAs that are working with the nation's poorest population as one would expect from institutions that are working with a cross-section of income levels.

Rents uncollected is one of the three basic components of management

operations; the other two are vacancies and the condition of the units. Since Indicator #3 examines management operations, it is appropriate that rents uncollected be examined under this indicator. Rents uncollected will be calculated the same as in the current PHMAP rule. In order to make the transition from the PHMAP to the PHAS, it was determined to make as few changes as possible between the current PHMAP and the management operations indicator under the PHAS. HUD believes that PHAs are in the business of providing housing, keeping the units in good repair, and collecting rents due. Although PHAs are working with the nation's poorest population, the rent due by residents is based on a percentage of the resident's adjusted income. The fact that a resident's rent is based on a percentage of the adjusted income total housing cost in and of itself does consider the public housing population.

**Comments on "Work Orders" Component.** There were comments on this component. One commenter stated that evaluation of nonemergency work orders should be dropped. Another commenter stated that the time allowed to complete non-emergency work orders is far too lax. The commenter noted that the current PHMAP allows for up to 25 days to qualify for an "A" and this standard should be less than 5 days in order to receive an "A."

HUD believes that the response time to non-emergency work orders should be measured under the PHAS, and calculated in the same way as it is measured under the current PHMAP. HUD will consider changes to this sub-indicator as possible future changes to the PHAS. In order to make the transition from the PHMAP to the PHAS, it was determined to make as few changes as possible between the current PHMAP and the management operations indicator under the PHAS.

**Comments on "Annual Inspection of Units" Component.** Comments on this component included the following. A few commenters stated that the new physical condition standards conflict with the traditional annual inspection requirement. They stated that HUD requires PHAs to use HUD's proposed new uniform physical condition standards in performing annual inspections of units and systems, but this is a deviation from HUD's statements in the preamble to the proposed rule on Uniform Physical Condition Standards that the new physical inspection standards would not pre-empt the existing PHA inspection procedures nor the investment PHAs may have made in computer hardware and software to

carry out those procedures. HUD should permit PHAS to use their existing inspection systems. Another commenter stated that the inspection indicator should be dropped because this indicator will be measured under the PHAS Indicator #1, Physical Condition. Another commenter asked whether the management inspection was a physical inspection, or HQS inspection?

HUD has no objection if a PHA determines that use of the HUD software for its own purposes is in its best interests. HUD encourages PHAs to use its inspection software when conducting their own annual inspections in order to promote uniformity in inspections, but HUD is not proposing at this time to require PHAs to use HUD's inspection software for two reasons: (1) PHAs may, as a part of their operating procedures, combine other inspections (e.g., housekeeping, preventive maintenance, etc.) with their annual inspection of units; and (2) PHAs may have existing software for operations that may be incompatible with the HUD software. It would be uneconomical and unreasonable to require PHAs to change their existing systems. The REAC will inspect using the HUD software, and PHAS indicator #3 requires a PHA's inspection to utilize the HUD uniform physical inspection standards set forth in subpart B of this part.

HUD believes that the inclusion of this sub-indicator in the PHAS is very important because the PHAS indicator #1 will inspect a statistically valid sample of units and systems, whereas this sub-indicator requires PHAs to inspect and initiate repairs on all occupied units and all systems on an annual basis. This inspection is a management assessment of a PHA's ability to determine the maintenance and modernization needs of its developments. This sub-indicator is assessed by measuring the extent to which a PHA performed a physical inspection of 100% of the units and systems within each development. A PHA must use the HUD uniform physical inspection standards set forth in subpart B of this part. The HQS is no longer used as a standard for inspection of public housing subject to this part.

**Comment on "Security" Component—Clarify Nature of Security Component.** A few commenters stated that the security indicator should not evaluate the PHA's relationship with police or grant performance, and the name should be changed from Security to Applicant Screening and Lease Enforcement.

HUD has determined that changes to this sub-indicator will be considered as



possible future changes to the PHAS. In order to make the transition from the PHMAP to the PHAS, it was determined to make as few changes as possible between the current PHMAP and the management operations indicator under the PHAS.

*Resident Services and Satisfaction Should Not Be a Separate PHAS Indicator but a Component of Management Indicator.* Several commenters stated that the elimination of PHMAP Indicator #7, Resident Services and Community Building is supported. Other commenters stated that if "Resident Satisfaction" is to be a rating factor, it should be included as a component of this indicator, not elevated to the status of a separate indicator.

Because residents are stakeholders in the PHAS process, it was determined that resident service and satisfaction should be elevated to the status of a separate indicator. The opinions of the residents that live in public housing should be considered in the overall operation of a PHA.

#### *F. Comments on Subpart E—PHAS Indicator #4 Resident Service and Satisfaction*

*Surveys Should Not Be Independent Indicator, but a Component of Management Indicator.* Some commenters wrote in opposition to the proposed survey requirement. Two of the commenters stated that, if used at all, this indicator should be included as a component of PHAS Indicator #3 (Management Operations), and only as a pass/fail requirement that each PHA employ some form of resident satisfaction survey on a regular basis.

HUD has determined that residents' opinions of their living conditions are very important to the PHAS assessment process. Therefore, HUD has decided that the resident service and satisfaction indicator will be separate. HUD has designed an initial survey instrument for completion by a statistically valid sample of residents selected by HUD, and HUD anticipates to begin testing the survey instrument in the near future.

*Small PHAs Should be Excluded from Indicator #4.* Two commenters wrote that PHAS indicator #4 should exclude small housing authorities from issues concerning resident organizations and resident initiative programs, as PHMAP does.

HUD has determined that due to the importance of residents' opinions of their living conditions, small housing authorities will not be excluded from the assessment process, including the assessment of resident service and satisfaction.

*PHAs Should be Allowed to Develop Own Surveys.* Two commenters recommended that the rule be amended to permit PHAs to design their own resident surveys. One commenter remarked that local PHAs could do a better job designing surveys that take regional and demographic factors into account. The other commenter wrote that PHAs should be allowed to develop surveys in accordance with HUD-established guidelines.

The REAC is responsible for the development of a uniform standard assessment of all PHAs and a Customer Satisfaction Survey to assess residents' living conditions. HUD allowing PHAs to develop individual surveys would create different tools for measuring the physical, financial and management condition of properties, as well as resident satisfaction of living conditions. HUD has determined that there must be a standard measurement tool to compare and score the results of the survey.

*Surveys Should Not be Conducted by PHAs.* Several commenters objected to PHA-administered resident surveys. Several of the commenters wrote that there is often a lack of trust and forthrightness between a PHA and residents. These commenters remarked that a survey administered by a local or regional resident organization, or an independently administered survey, would be preferable. Another commenter wrote that fear of retaliation will prevent honest answers from being given to a survey administered by the PHA. One commenter suggested that the surveys should be administered and monitored by HUD.

HUD has determined that PHAs will manage the Customer Satisfaction Survey. A resident against whom a PHA is taking retaliation should report such action to HUD's Inspector General Hotline at 1-(800)-347-3735.

*Good Management Practices May Produce Unfavorable Ratings.* Several commenters remarked that good management practices, such as evictions for failure to pay rent or abide by rules and regulations, may not always translate into popular management practices. These commenters wrote that high-performing PHAs should not be singled out negatively under this indicator for aggressive management. The commenters recommended that such factors should be taken into consideration in computing the score for this indicator.

HUD agrees that good management practices, such as lease enforcement, may not always be viewed by those being evicted with favor. Therefore, this

issue will be considered during the refinement of the survey's questions.

*Comments on Sample of Residents to Be Surveyed.* There were several comments on the sample of residents. Several commenters remarked that the proposed rule did not state what constitutes a statistically significant sample of residents. Some of the commenters recommended that the rule require that survey samples be obtained from all developments in a PHA's jurisdiction. One commenter suggested that the resident samples include a cross-section of tenants that reflects racial, ethnic, economic, age, and length of tenancy characteristics. Another commenter remarked that to conduct a truly valid survey, it is essential that the respondents be pre-identified as actual leaseholders in good standing. Five commenters wrote that PHAs should not be penalized if only a small number of residents respond to the surveys. One of these commenters wrote that a lack of response could indicate that the residents think the PHA is doing a good job. This commenter worried that only dissatisfied tenants might complete the survey. One commenter questioned how resident samples would be drawn in areas (such as Alaska), where a PHA's projects are widely dispersed geographically. The commenter worried about the costs involved if each project must be sampled.

With respect to these comments, HUD responds as follows. HUD has not finalized its decision to use a response rate for measurement at this time. HUD will use a standard proven survey methodology to improve PHAs' response rates. This includes, but is not limited to, providing technical assistance to PHAs by preparing the survey in several languages, providing recommendations to promote the survey process by distributing lead letters, bulletin board communications, and resident meetings.

HUD is in the process of testing the various collection and sampling methods. The sampling process includes testing the survey in a statistically valid sample of developments selected by HUD. The widely dispersed geographical units will be considered during the selection process.

*Scoring System Is Vague.* Many commenters wrote that the proposed rule was unclear regarding how the resident services and satisfaction component would be scored and weighted. One of the commenters asked whether adjustments would be made for the PHA's size, population density, and social and economic environment.

HUD has determined that the final PHAS rule will only score the first two components as published in the proposed PHAS rule (survey results; and level of implementation/follow-up action process), with a value of five points each. The third component, verification that the survey process was managed in a manner consistent with guidance provided by HUD, will not be scored, but is a threshold requirement. A PHA will not receive any points under this indicator if the survey process is not managed in a manner consistent with the guidance provided by HUD or the survey results are determined to be altered. Section 901.53 is revised accordingly.

**Concerns about Objectivity of Surveys.** Several commenters expressed concern about the objectivity of the resident surveys. Four of the commenters remarked that in an assessment system designed to be objective, this indicator appears to be entirely subjective, since the rating will be based on resident evaluation or opinion. Another commenter asked whether the reasonableness of the resident comments will be evaluated.

The measurement of residents' living conditions is measuring how residents perceive the performance of management providing the housing services. The opinions of the residents are important. There is an assumption made that if the majority of those surveyed identify the same problem, the problem is most likely a factual problem. The residents' perception plays a key role in responding to the survey questions. However, HUD will not rely on the residents' response alone, but compare it to the other assessment indicators under the PHAS to identify and address other issues.

**Data Collection and Verification of Survey Data.** Several commenters submitted comments on collection and verification of survey data. Five of the commenters asked about the methods HUD will use to verify the data. Two of the commenters inquired about the format the PHAs would be required to use to maintain data. Another commenter asked that HUD provide greater specificity regarding the records PHAs must maintain to demonstrate that the surveys were distributed and collected properly.

HUD is in the process of testing the various survey data collection methods. A methodology for collecting, verifying and maintaining the survey data will be finalized after the testing of the survey instrument.

**Conditions Outside PHA Control.** Several commenters wrote that several of the areas to be covered by the survey

are outside the control of the PHA. Several of these comments focused on community services provided by entities other than the PHA. For example, two of the commenters remarked that a PHA does not control electric, gas, and water/sewer service works. Other commenters wrote that the survey should not include questions about the effectiveness of the local police department or religious institutions. These commenters remarked that PHA management should not be judged according to the resident's trust of the local Police Department, or of other institutions not controlled by the PHA. Some commenters wrote that there are several aspects of public housing that residents are often dissatisfied with that are beyond the control of the PHA, either due to HUD regulation, prohibitive cost, or in conflict with higher priority needs of other residents. Examples would include the lack of air conditioning in individual units; the definition for rent not having more exclusions from gross income; and the 30% of income formula for tenant payments.

HUD has determined to include questions that will not be scored but used strictly for information purposes. However, HUD will make every effort to finalize the questions within the survey instrument to include elements that are the responsibility of the PHA.

**Cost and Administrative Burden Issues.** Several commenters expressed concern about the costs and administrative burdens that would be faced by PHAs in conducting the surveys. Two of the commenters wrote that the survey requirement constituted an unfunded mandate imposed on PHAs. Several commenters recommended that HUD reimburse PHAs for the costs of conducting the resident surveys. Four commenters remarked that this indicator amounts to another unfunded mandate on PHAs and further erodes the financial capability of PHAs to carry out day-to-day operations with limited staff and resources.

HUD has determined that if the survey process imposes a financial burden on PHAs, HUD reserves the right to implement other cost-effective methods for implementing the survey process.

**Language and Educational Barriers May Affect Survey Results.** Five commenters expressed concern that language and educational barriers, such as illiteracy, might skew the survey results. Three of the commenters remarked that the survey would need to be translated to the appropriate language for many residents. These

commenters asked whether HUD would supply the PHAs with translated surveys. One of the commenters asked that the final rule provide greater specificity regarding the conduct of surveys with non-English speaking residents and persons with disabilities.

HUD has considered the language barrier concerns associated with the survey process. At this time, HUD plans to offer the survey in at least two languages. Other languages may be considered if a significant portion of the population remains underrepresented by the selected survey languages. HUD is seeking the highest possible response from the selected population. This includes considering methods which will alleviate potential obstacles to survey response.

**Points for Resident Satisfaction Indicator Should Be Increased.** Many commenters recommended that the 10 points allocated for the resident services and satisfaction indicator be increased. Those commenters recommending specific point values, suggested that 20–25 points would be appropriate for this indicator.

HUD has determined that the 10 points allocated for this indicator is appropriate at this time.

#### *G. Comments on Subpart F—PHAS Scoring*

**Data Submission Deadlines Should be Extended.** Three commenters suggested that HUD extend the 60-day deadline for submission of data set forth in proposed § 901.60 (now § 902.60). One of the commenters wrote that HUD should be open to extenuating circumstances if there is a delay in submitting data by the deadline.

HUD believes that the 60-day data submission deadline is reasonable. Under the current PHMAP rule, PHAs are required to submit certifications within 60 calendar days after fiscal year end (FYE) and are required to submit year end financial statements within 45 calendar days after FYE.

**Process for Fair Housing Adjustments of Scores is Unclear.** One commenter wrote that HUD should provide additional details regarding the conditions under which PHAS scores can be modified due to a fair housing review. The commenter remarked that proposed § 901.60(e) (now § 902.60(e)) refers to HUD's ability to change scores through reviews and investigations by HUD's Office of Fair Housing and Equal Opportunity (FHEO). The commenter wrote that in the absence of clear criteria, the meaning of this provision is unclear. The commenter also asked whether PHAs would be able to appeal

fair housing related adjustments of their PHAS scores.

Section 902.60(f)(3) refers to data included in the independent audit report or reviews conducted by various HUD offices, including FHEO, where management deficiencies are identified that were not reflected in a PHA's certification submission. For purposes of reassessment, the REAC will schedule a reinspection and/or acquire audit services, if appropriate.

**Questions Regarding Appeals Process.** Many commenters raised questions regarding the appeals process set forth in proposed § 901.69 (§ 902.69). Several of the commenters recommended that HUD expand the appeals process to include all PHAs, and not just those that are designated as "troubled." One of these commenters wrote that since PHAS will have a much more complex scoring system than PHMAP, there may be greater room for error in the calculation of PHAS scores. The commenter urged that all PHAs be granted the right to appeal PHAS scores. Other commenters suggested that HUD expand the appeals process to permit the appeal of the scores for the individual PHAS components, as well as the overall PHAS score. Two other commenters, however, asked how scores could be disputed or appealed given the vagueness of the proposed rule. Another commenter recommended that the current PHMAP appeals process be incorporated into PHAS. The commenter remarked that appeals are particularly important for PHAs seeking non-HUD financing, since lenders look at assessment scores.

Section 6(j) of the U.S. Housing Act of 1937 provides for the petition for the removal of troubled and mod-troubled designations, and the appeal of a denial of such petition. These appeals are preserved in the PHAS. Since all of the indicators under the PHAS will be verified by independent third parties, the requirement for an extensive appeal process has been greatly diminished. As appropriate, and for purposes of reassessment, the REAC will schedule a reinspection and/or acquire audit services.

**Board of Review Composition.** There were a few comments on the composition of the Board of Review. Two commenters wrote that the Board of Review should include a resident representative. One commenter recommended that, to insure the integrity of the appeals process, HUD should create an independent PHAS Appeals Board, similar to HUD's Board of Contract Appeals and Mortgage Review Boards.

These comments are noted by HUD. As stated in the proposed PHAS rule, the third member of the Board will be from such other office or representative as the Secretary may designate (excluding, however, representation from the TARC).

**PHAS Scores Should Be Provided to Residents.** One commenter recommended that HUD automatically provide all inspection results, resident satisfaction surveys, and PHAS scores to all local resident organizations, at the time they are made available to the PHAs.

The REAC will provide the results of the assessment of the four PHAS indicators, as well as the overall PHAS score to PHAs. At that time, the results of the PHAS assessment becomes public information and will be available to all interested parties. In addition, § 902.63(d) requires a PHA to post a notice of its final score and status in appropriate conspicuous and accessible locations in its offices within two weeks of its final score and status.

**PHAs Should Be Notified and Have Opportunity to Review Score Before Issuance.** One commenter wrote that prior to issuing and posting a PHA's score, the grade and how it was arrived at should be reviewed with the PHA. Another commenter remarked that the proposed rule did not seem to include a provision regarding PHA notification of its PHAS score.

A PHA's final PHAS score will be issued by the REAC after independent verification of all four indicators. As in the current PHMAP rule, a PHA's PHAS score will be issued without prior review by the PHA. Section 902.63(a) states that an overall PHAS score will be issued by REAC for each PHA 60 to 90 days after the end of the PHA's fiscal year.

**Questions Regarding Designation Status.** Several commenters raised questions regarding designation status. One of these commenters asked whether a PHA that scores below the threshold on any component would be referred to a TARC. The commenter also asked whether a PHA that does not receive a passing score on any PHAS indicator would be designated as a troubled PHA. Another commenter wrote that the proposed rule did not state whether the PHAS score would be a measure of the PHA's absolute performance, or reflect the PHA's relative performance against other PHAs. The commenter also asked whether PHAs would, for scoring purposes, be divided by factors such as size, age and location. One commenter expressed confusion regarding the definition of "top performer." The commenter asked whether top

performers constitute the top 10% of all PHAs, or PHAs with an overall PHAS score of 90% or greater. One commenter expressed concern that the proposed rule would "debase" the troubled PHA designation. The commenter wrote that under the proposed assessment system, a housing authority that scores below 60 percent on Indicators 1, 2, or 3 will receive a troubled designation even if the overall score is well over 60. This commenter remarked that this requirement would unfairly force many housing authorities to become troubled. According to the commenter, this designation should be an indication recognized by all that the housing authority has serious problems. The commenter suggested that instead of receiving a troubled designation, a PHA that scores above 60% overall but fails to achieve 60% on indicators 1, 2, or 3 should be referred to for technical assistance rather than some form of punitive action. Another commenter suggested that the rule should make compliance with fair housing laws and regulations a prerequisite to designation as a high performer.

With respect to these comments, HUD notes that § 902.67(a)(3) states that a PHA that achieves a total PHAS score of less than 60%, or achieves a score of less than 60% of the total points available under PHAS indicators #1, #2 or #3 shall be designated as troubled, and referred to the TARC as described in § 902.75.

Under PHAS Indicators #1, #2 and #4, the PHAS score will reflect the PHA's relative performance against other PHAs. Under indicator #3, the PHAS score will be a measure of the PHA's absolute performance. As in the current PHMAP rule, PHAs will not be divided by factors such as size, age or location for scoring purposes.

The term "top performer" refers to a high performer PHA. To avoid confusion, HUD has only used the term "high performer" in the final rule.

HUD agrees that a PHA that scores below 60% under indicators #1, #2 and #3 has serious problems, and troubled designation is warranted. Referral to the TARC should be viewed as a remedial action rather than a punitive action. If a PHA is referred to the TARC, it will develop a Recovery Plan and MOA in conjunction with the TARC, and receive intense technical assistance to improve the physical condition of the properties, the financial health of the agency, and/or overall management operations.

On the fair housing issue, HUD has determined that changes to the requirements for high performer designation will be considered as possible future changes to the PHAS. In order to make the transition from the

PHMAP to the PHAS, it was determined to make as few changes as possible between the current PHMAP and the management operations indicator under the PHAS.

#### *H. Comments on Subpart G—PHAS Incentives and Remedies*

*Comments on Incentives for High Performers.* Comments on this subject (addressed in § 902.71 of the final rule) are as follows: the rule is vague on incentives; the incentives for high performers are inadequate; how will PHAS incentives differ from PHMAP incentives; physical condition inspections for high performers should be every three years (less frequently than annual); bonus points should be provided on all HUD competitive funding; permit PHAs to establish development-based applicant waiting lists, subject to fair housing requirements; continue the current relief measures provided to high performers which include flexibility in the Comprehensive Grant program (CGP) on maximum percentages allowed for management improvements and administrative costs, and using CGP funds from troubled PHAs to increase the funds available to PHAs that perform well; provide high performers with the option to refuse to renew the lease for those tenants who have lease violations (poor payment history, poor housekeeping habits, evidence of tenant abuse to PHA property, history of causing disturbances in the community, etc.); provide high performers with significantly reduced reporting requirements; permit high performers to use the equity from properties to leverage financing for development purposes; and allow high performers to review income and conduct re-certification on flexible schedules or every two years.

HUD agrees that incentives under the PHAS should be meaningful and reflect high performer designation. HUD intends to consult further with industry groups to develop such incentives.

*Clarify Rule's Relationship to Moving to Work Initiative.* Since PHAs participating in HUD's Moving To Work (MTW) Initiative have largely been assured freedom from HUD oversight, the applicability of the proposed rule to them needs to be clarified. The incentives proposed for high performers under the rule are the same as those under MTW.

A PHA that is participating in the MTW incentive will receive less oversight from HUD, as will those PHAs that are high performers but not participating in the MTW initiative.

*Field Office Discretion to Impose Program Requirement Waived by REAC Should Be Eliminated.* A few commenters objected to the provision in §§ 902.67(b) and 902.71(d) that would accord the field office the discretion to impose on a PHA any program requirement that had been waived by REAC as a high-performer incentive. The rule should not provide the field office any mechanism to achieve a back-door nullification of the PHAS process or results.

HUD agrees with this comment, and these sections have been removed from the final PHAS rule.

*Comments on Referral to an Area/HUB Program Center.* Commenters offered the following comments on the provisions of § 902.73—Referral to an Area HUB/Program Center: what uniform criteria will HUD use to determine which "standard" agencies will be required to submit improvement plans? This is vague. HUD should define the deficiencies and make sure they will be applied consistently across the HUBs; where does the authority and expertise lie in the HUBs to make these determinations; is there a link to Central Office PIH; are HUBs reporting to HUD Headquarters, to REAC, or somewhere else; and will HUBs be assigned the task of deciding what PHAs will file Improvement Plans. Another commenter stated that a standard PHA should not be required to submit a corrective action plan for any indicator or component for which it receives a passing score. One commenter stated that the requirement for "standard performers" to submit an improvement plan should be based solely on the PHAS scores.

To address these concerns, HUD offers the following. The requirement at § 902.73(a) (§ 901.73(a) in the proposed rule) states that a PHA that receives a total PHAS score of less than 70% but not less than 60% shall be required to submit an Improvement Plan to eliminate deficiencies in the PHA's performance. This requirement is similar to the current PHMAP rule which requires an Improvement Plan for any indicator that scored a grade of F. The requirement at § 902.73(b)(2) states that the HUD/Program Center may require, on a risk management basis, a standard performer PHA with a score of not less than 70% to submit within 30 days after receipt of its PHAS score an Improvement Plan. This requirement is similar to the current PHMAP rule which states that a Field Office may require, on a risk management basis, a PHA to submit an Improvement Plan for each indicator that a PHA scored a grade D or E.

The intent of this language in both the PHMAP and PHAS rules is for HUD and PHAs to be proactive regarding potential problem areas, and for HUD to provide technical assistance to a PHA before troubled designation is assigned. Since the local Office has the most frequent contact with the PHAs under its jurisdiction, it is in the best position to make such determinations.

A deficiency is defined in § 902.7 as any PHAS score below 60% of the available points in any indicator or component. This definition has been revised in this final rule to read: any PHAS score below 60% of the available points in any indicator, sub-indicator or component.

HUB/Program Centers report to the Assistant Secretary for PIH. The requirement to submit Improvement Plans is based solely on the PHAS scores, e.g., on a PHA receiving a score of less than 70% but not less than 60%. However, a HUB/Program Center may require, on a risk management basis, a PHA with a score of not less than 70% to submit an Improvement Plan.

*Response Time to Correct Deficiencies Is Too Short.* A few commenters stated that the response time allowed for an agency to correct any identified deficiency is too short.

HUD believes that 30 days is sufficient time for a PHA to submit an Improvement Plan for the correction of identified deficiencies. Since the deficiencies would have been identified by the PHAS assessment, a PHA should be able to develop a plan to correct identified deficiencies within 30 days. The longer a deficiency is present without corrective action being taken, the worse the deficiency becomes, and the more costly it is to remedy. Comments on Referral to TARC. Commenters offered the following comments on the provisions of § 902.75—Referral to a HUB/Program Center.

*Receivership Determination Should Be Appealable to Assistant Secretary for PIH.* A few commenters stated that it appears that the rule mandates receivership for a PHA that does not show "substantial improvement" within one fiscal year. At the very least, such a PHA should be permitted to make its case to the Assistant Secretary for Public and Indian Housing, who should be given the final authority under the rule to determine if appointment of a receiver should be sought.

The PHAS proposed rule at § 901.77 states that the Enforcement Center is officially responsible for recommending to the Assistant Secretary for PIH that a troubled PHA be declared in substantial default.

*Rule Needs to Address Impact on Tenants When PHA Is Referred to TARC or Enforcement Center.* Some commenters stated that the rule does not discuss the implications upon the residents of referral of a PHA to the TARC or the Enforcement Center. Since the residents are the ultimate beneficiaries of the PHA and HUD and HUD's consumers, we expect that HUD would intend to protect their interests and legal rights, but the regulation is silent. The regulation should articulate what will happen to tenants, that all services will continue uninterrupted, and those services which the PHA may have been failing to properly deliver would be restored.

Language has been added to the final PHAS regulation at §§ 902.75 and 902.77 which states that to the extent feasible, all services to residents will continue uninterrupted.

*A One-Year Recovery Period Is Not Sufficient.* We do not agree that once a PHA is designated as troubled and is referred to a TARC for assistance that the time allotted...is sufficient time for recovery. Due to the severity of need, multiple year solutions may be required and to lock a PHA to one year in the TARC is unrealistic, especially in large troubled PHAs.

Initially, a PHA is afforded one year after the score is issued to the PHA to demonstrate substantial improvement (50% of the points needed to achieve a passing score). If the PHA demonstrates substantial improvement after one year, then the PHA will have an additional year to continue recovery efforts in the TARC.

*Recovery Plan Prepared by TARC Should Include a Timetable.* One commenter stated that the recovery plan prepared by the TARC should include a timetable.

The proposed PHAS regulation at § 901.75(c)(2) provides for annual and quarterly performance targets for the MOA. Since the MOA is part of the Recovery Plan, the Recovery Plan does include a timetable.

*Ten Days to Review Recovery Plan and MOA Are Insufficient.* Other commenters stated that ten days for a PHA to review the recovery plan and the MOA is not sufficient and should be extended.

Within 30 days of notification of the designation of a troubled PHA within its jurisdiction, the appropriate TARC will be on-site at the PHA to develop a Recovery Plan. Since the PHA will be involved in the development of both the Recovery Plan and the MOA, a ten day review period is not unreasonable.

*Is Process for Developing MOA Between Troubled PHAs and HUD*

*Consistent with PHMAP Statute.* A few commenters asked whether the process for developing a MOA between troubled agencies and HUD is consistent with the law? One commenter noted that section 6(j)(2)(B) of the 1937 Act states that "the Secretary shall provide for an on-site, independent assessment of the management of the agency" and provides a definition of the independent assessors. The Secretary should seek to enter into an agreement with the troubled public housing agency only after consulting with the assessment team and reviewing its report. The proposed rule appears to be inconsistent with the statute.

The independent assessment will be undertaken by the appropriate TARC, which within 30 days of notification of the designation of a troubled PHA within its area, will deploy an on-site team to develop a Recovery Plan (§ 902.75(a)).

*Rule Should Provide More Detail on Credible Source.* Two commenters stated that HUD should provide more detail on what or who a credible source might be, and should be clear about what documentation is required.

The proposed regulation did not include examples of a credible source because it may differ in each case. However, language will be added to the final PHAS regulation that gives examples of a credible source, including but not limited to, the Office of Fair Housing and Equal Opportunity, judicial referral, Mayor, etc.

*Comment on Resident Petitions for Remedial Action (§ 901.85).* One commenter stated that the 20% requirement may be good for larger PHAs, but works against smaller ones.

Although a fewer number of residents is required to equate to the 20% of residents required in order to petition HUD to take remedial action, in accordance with § 902.79(b), HUD is required to advise a PHA of such action, and a PHA will have the opportunity to initiate corrective action, or to demonstrate that the information is incorrect.

#### **IV. Findings and Certifications**

##### *Paperwork Reduction Act Statement*

The information collection requirements in this rule have been approved by the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520) and assigned OMB control number 2535–0106. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the

collection displays a valid control number.

##### *Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. This rule will not impose any Federal mandates on any State, local, or tribal governments or the private sector within the meaning of the Unfunded Mandates Reform Act of 1995.

##### *Environmental Review*

During the development of the June 30, 1998 proposed rule, a Finding of No Significant Impact with respect to the environment was made in accordance with HUD regulations in 24 CFR part 50 that implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4223). That Finding continues to apply to this final rule, and is available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC.

##### *Impact on Small Entities*

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed and approved this rule, and in so doing certifies that this rule is not anticipated to have a significant economic impact on a substantial number of small entities. This rule revises HUD's previous regulations for the assessment of public housing (PHMAP). The new PHAS incorporates the statutory indicators of PHMAP, and adds three additional indicators. One of the new indicators—physical condition—would assess the extent to which PHAs are providing public housing that is decent, safe, and sanitary. Public housing has always been subject to a statutory standard of "decent, safe, and sanitary." This rule simply provides a clear and objective statement of the standard. This indicator also entails an annual independent HUD inspection of public housing, but it does not impose additional inspection requirements upon PHAs. The clarity and consistency of this new indicator provides a fair, accurate, and reliable assessment of the physical condition of the large public housing portfolio. However, since this rule does not alter the statutory standard for physical condition, nor impose additional inspection obligations, the new physical condition indicator will not have a

significant economic impact on a substantial number of small entities.

The second indicator—financial condition—assesses the financial condition of PHAs, requiring them to submit financial reports to HUD electronically and in accordance with GAAP. HUD estimates that electronic submission of financial information will be less burdensome to PHAs, since many PHAs are making more extensive use of automated systems. This rule allows exceptions if the cost of electronic submission will be excessive. GAAP-based accounting reports, which are widely accepted and recognized, are not substantially different than the reports that PHAs previously submitted. A number of PHAs were already required to use GAAP or are otherwise using GAAP, and the majority of the PHAs with which HUD has consulted support the change to GAAP. For those PHAs that were not yet using GAAP, HUD is taking several steps to ease the conversion, including making only simple additions to the current PHA accounting guide and chart of accounts, and providing other conversion guidance and training, particularly to small entities. Increasing the speed of information exchange (through electronic submission) and the consistency and accuracy of the information (through GAAP) will greatly enhance the assessment of a PHA's financial condition. However, this new indicator will not have a significant economic impact on a substantial number of small entities.

The fourth indicator—resident service and satisfaction—entails a new resident service and satisfaction survey. This survey is key to obtaining input from public housing residents, which is an important aspect of assessing public housing. HUD intends that this survey will be conducted through an automated process, and accordingly, will present a minimal administrative burden for PHAs in terms of administering and evaluating the survey. HUD intends to provide the survey format and the electronic reporting format, as well as software specifications. Therefore, this survey will not have a significant economic impact on a substantial number of small entities.

HUD is also seeking to minimize any burden on PHAs by allowing a significant transition period for converting to the new PHAS. PHAs will have at least 1 year before new scores are issued under the PHAS. During that transition period, HUD may issue advisory scores regarding physical condition and financial management to provide guidance to PHAs and to ease the conversion to the new PHAS.

The new PHAS is fundamentally designed to provide relevant and verifiable measures that directly relate to a PHA's performance and that result in an accurate and reliable score. This improved assessment process will allow HUD to target its oversight resources on those PHAs most in need of attention; high-performing PHAs will receive recognition, along with reduced HUD scrutiny and additional flexibility. Since the revised assessment system in this rule does not impose any significant new requirements upon PHAs, and since HUD will assist PHAs in their conversion to the system, this rule will not have a significant economic impact on a substantial number of small entities.

#### *Federalism*

The General Counsel, as the Designated Official under Executive Order 12612, Federalism, has determined that the policies contained in this rule will not have substantial direct effects on States or their political subdivisions, on the relationship between the Federal Government and the States, or on the distribution of power and responsibilities among the various levels of government. This rule is intended to promote good management practices by including, in HUD's relationship with PHAs, continuing review of PHAs' compliance with already existing requirements. The rule will not create any new significant requirements. As a result, the rule is not subject to review under the Order.

#### *Catalog of Federal Domestic Assistance*

The Catalog of Federal Domestic Assistance numbers for Public Housing is 14.850.

#### **List of Subjects in 24 CFR Parts 901 and 902**

Administrative practice and procedure, Public housing, Reporting and recordkeeping requirements.

Accordingly, Chapter IX 901 of title 24 of the Code of Federal Regulations is amended as follows:

#### **PART 901—PUBLIC HOUSING MANAGEMENT ASSESSMENT PROGRAM**

1. The authority citation continues to read as follows:

**Authority:** 42 U.S.C. 1437d(j); 42 U.S.C. 3535(d).

2. In § 901.1, paragraph (c)(1) is designated as paragraph (c)(1)(ii) and a new paragraph (c)(i) is added to read as follows:

#### **§ 901.1 Purpose, program scope and applicability.**

\* \* \* \* \*

(c)(1)(i) The provisions of this part remain applicable to PHAs and RMC/ AMEs as described in paragraph (c)(1)(ii) until September 30, 1999.

\* \* \* \* \*

3. A new part 902 is added to read as follows:

#### **PART 902—PUBLIC HOUSING ASSESSMENT SYSTEM**

##### **Subpart A—General Provisions**

Sec.

902.1 Purpose and general description.

902.3 Scope.

902.5 Applicability.

902.7 Definitions.

##### **Subpart B—PHAS Indicator #1: Physical Condition**

902.20 Physical condition assessment.

902.23 Physical condition standards for public housing—decent, safe, sanitary and in good repair (DSS/GR).

902.25 Physical condition scoring and thresholds.

902.27 Physical condition portion of total PHAS points.

##### **Subpart C—PHAS Indicator #2: Financial Condition**

902.30 Financial condition assessment.

902.33 Financial reporting requirements.

902.35 Financial condition scoring and thresholds.

902.37 Financial condition portion of total PHAS points.

##### **Subpart D—PHAS Indicator #3: Management Operations**

902.40 Management operations assessment.

902.43 Management operations performance standards.

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Appendix A to Part 902—Areas and Items to be Inspected

**Authority:** 42 U.S.C. 1437d(j), 3535(d).

#### Subpart A—General Provisions

##### § 902.1 Purpose and general description.

(a) *Purpose.* The purpose of the Public Housing Assessment System (PHAS) is to enhance trust in the public housing system among public housing agencies (PHAs), public housing residents, HUD and the general public by providing a comprehensive management tool for effectively and fairly measuring the performance of a public housing agency in essential housing operations, including rewards for high performers and consequences for poor performers.

(b) *Responsible office for PHAS assessments.* The Real Estate Assessment Center (REAC) is responsible for assessing and scoring the performance of PHAs.

(c) *PHAS indicators of a PHA's performance.* REAC will assess and score a PHA's performance based on the following four indicators:

(1) PHAS Indicator #1—the physical condition of a PHA's properties (addressed in subpart B of this part);

(2) PHAS Indicator #2—the financial condition of a PHA (addressed in subpart C of this part);

(3) PHAS Indicator #3—the management operations of a PHA (addressed in subpart D of this part); and

(4) PHAS Indicator #4—the resident service and satisfaction feedback on a PHA's operations (addressed in subpart E of this part).

(d) *Assessment tools.* REAC will make use of uniform and objective protocols for the physical inspection of properties and the financial assessment of the PHA, and will gather relevant data from the PHA on the Management Operations Indicator and the Resident Service and Satisfaction Indicator. On the basis of this data, REAC will assess and score the results, advise PHAs of their scores and identify low scoring and failing PHAs so that these PHAs will receive the appropriate attention and assistance.

(e) *Limitation of change of PHA's fiscal year.* To allow for a period of consistent assessment of the PHAS indicators, a PHA is not permitted to change its fiscal year for the first 3 full fiscal years following October 1, 1998.

##### § 902.3 Scope.

The PHAS is a strategic measure of a PHA's essential housing operations. The PHAS, however, does not evaluate a PHA's compliance with or response to every Department-wide or program specific requirement or objective. Although not specifically referenced in

this part, PHAs remain responsible for complying with such requirements as fair housing and equal opportunity requirements, requirements under section 504 of the Rehabilitation Act of 1973 (29 U.S.C. 794) and requirements of programs under which the PHA is receiving assistance. PHAs' adherence to these requirements will be monitored in accordance with the applicable program regulations and the PHA's annual contributions contract.

##### § 902.5 Applicability.

(a) *PHAs, RMCs, AMEs.* (1) This part applies to PHAs, Resident Management Corporations (RMCs) and Alternate Management Entities (AMEs). The management assessment of an RMC/AME differs from that of a PHA.

Because an RMC/AME enters into a contract with a PHA to perform specific management functions on a development-by-development or program basis, and because the scope of the management that is undertaken varies, not every indicator that applies to a PHA would be applicable to each RMC/AME.

(2) This part is applicable beginning October 1, 1999.

(b) *PHA ultimate responsible entity under ACC.* Due to the fact that the PHA and not the RMC/AME is ultimately responsible to HUD under the Annual Contributions Contract (ACC), the PHAS score of a PHA will be based on all of the developments covered by the ACC, including those with management operations assumed by an RMC or AME (pursuant to a court ordered receivership agreement, if applicable).

(c) *Assumption of management operations by AME.* When a PHA's management operations have been assumed by an AME:

(1) If the AME assumes only a portion of the PHA's management operations, the provisions of this part that apply to RMCs apply to the AME (pursuant to a court ordered receivership agreement, if applicable); or

(2) If the AME assumes all, or substantially all, of the PHA's management functions, the provisions of this part that apply to PHAs apply to the AME (pursuant to a court ordered receivership agreement, if applicable).

##### § 902.7 Definitions.

As used in this part:

*Adjustment for physical condition (project age) and neighborhood environment* is a total of 3 additional points added to PHAS Indicator #1 (Physical Condition). The 3 additional points, however, shall not result in a total point value over the total points

available for PHAS Indicator #1 (established in subpart B of this part).

*Alternative management entity (AME)* is a receiver, private contractor, private manager, or any other entity that is under contract with a PHA, or that is otherwise duly appointed or contracted (for example, by court order or agency action), to manage all or part of a PHA's operations. Depending upon the scope of PHA management functions assumed by the AME, in accordance with § 902.5(c), the AME is treated as a PHA or an RMC for purposes of this part and, as appropriate, the terms PHA and RMC include AME.

*Assessed fiscal year* is the PHA fiscal year that has been assessed under the PHAS.

*Average number of days nonemergency work orders were active* is calculated:

(1) By dividing the total of—

(i) The number of days in the assessed fiscal year it takes to close active nonemergency work orders carried over from the previous fiscal year;

(ii) The number of days it takes to complete nonemergency work orders issued and closed during the assessed fiscal year; and

(iii) The number of days all active nonemergency work orders are open in the assessed fiscal year, but not completed;

(2) By the total number of nonemergency work orders used in the calculation of paragraphs (1)(i), (ii) and (iii) of this definition.

*Days Receivable Outstanding* is Tenant Receivables divided by Daily Tenant Revenue.

*Deficiency* means any PHAS score below 60 percent of the available points in any indicator, sub-indicator or component.

*Improvement plan* is a document developed by a PHA, specifying the actions to be taken, including timetables, that shall be required to correct deficiencies identified under any of the indicators and components within the indicator(s), identified as a result of the PHAS assessment when an MOA is not required.

*Reduced actual vacancy rate within the previous 3 years* is a comparison of the vacancy rate in the PHAS assessed fiscal year (the immediate past fiscal year) with the vacancy rate of that fiscal year that is 2 years previous to the assessed fiscal year. It is calculated by subtracting the vacancy rate in the assessed fiscal year from the vacancy rate in the earlier year. If a PHA elects to certify to the reduction of the vacancy rate within the previous 3 years, the PHA shall retain justifying



documentation to support its certification for HUD post review.

*Reduced the average time nonemergency work orders were active during the previous 3 years* is a comparison of the average time nonemergency work orders were active in the PHAS assessment year (the immediate past fiscal year) with the average time nonemergency work orders were active in that fiscal year that is 2 years previous to the assessment year. It is calculated by subtracting the average time nonemergency work orders were active in the PHAS assessment year from the average time nonemergency work orders were active in the earlier year. If a PHA elects to certify to the reduction of the average time nonemergency work orders were active during the previous 3 years, the PHA shall retain justifying documentation to support its certification for HUD post review.

*Vacancy loss* is vacant unit potential rent divided by gross potential rent.

*Work order deferred for modernization* is any work order that is combined with similar work items and completed within the current PHAS assessment year, or will be completed in the following year if there are less than 3 months remaining before the end of the PHA fiscal year when the work order was generated, under the PHA's modernization program or other PHA capital improvements program.

#### **Subpart B—PHAS Indicator #1: Physical Condition**

##### **§ 902.20 Physical condition assessment.**

(a) *Objective.* The objective of the Physical Condition Indicator is to determine whether a PHA is maintaining its public housing in a condition that is decent, safe, sanitary and in good repair (DSS/GR), as this standard is defined § 902.23.

(b) *Physical inspection under PHAS Indicator #1.* REAC will provide for an independent physical inspection of, at minimum, a statistically valid sample of the units in the PHA's public housing portfolio to determine compliance with DSS/GR standard.

(c) *PHA physical inspection requirement.* The HUD-conducted physical inspections required by this part do not relieve the PHA of the responsibility to inspect public housing units as provided in section 6(j)(1) of the U.S. Housing Act of 1937 (42 U.S.C. 1437d(j)(1)), and § 902.43(a)(5).

(d) *Compliance with State and local codes.* The physical condition standards in this subpart do not supersede or preempt State and local building and maintenance codes with which the

PHA's public housing must comply. PHAs must continue to adhere to these codes.

##### **§ 902.23 Physical condition standards for public housing—decent, safe, sanitary and in good repair (DSS/GR).**

(a) Public housing must be maintained in a manner that meets the physical condition standards set forth in this section in order to be considered decent, safe, sanitary and in good repair. These standards address the major areas of public housing: the site; the building exterior; the building systems; the dwelling units; the common areas; and health and safety considerations.

(1) *Site.* The site components, such as fencing and retaining walls, grounds, lighting, mailboxes/project signs, parking lots/driveways, play areas and equipment, refuse disposal, roads, storm drainage and walkways must be free of health and safety hazards and be in good repair. The site must not be subject to material adverse conditions, such as abandoned vehicles, dangerous walks or steps, poor drainage, septic tank back-ups, sewer hazards, excess accumulations of trash, vermin or rodent infestation or fire hazards.

(2) *Building exterior.* Each building on the site must be structurally sound, secure, habitable, and in good repair. Each building's doors, fire escapes, foundations, lighting, roofs, walls, and windows, where applicable, must be free of health and safety hazards, operable, and in good repair.

(3) *Building systems.* Each building's domestic water, electrical system, elevators, emergency power, fire protection, HVAC, and sanitary system must be free of health and safety hazards, functionally adequate, operable, and in good repair.

(4) *Dwelling units.* (i) Each dwelling unit within a building must be structurally sound, habitable, and in good repair. All areas and aspects of the dwelling unit (for example, the unit's bathroom, call-for-aid, ceiling, doors, electrical systems, floors, hot water heater, HVAC (where individual units are provided), kitchen, lighting, outlets/switches, patio/porch/balcony, smoke detectors, stairs, walls, and windows) must be free of health and safety hazards, functionally adequate, operable, and in good repair.

(ii) Where applicable, the dwelling unit must have hot and cold running water, including an adequate source of potable water.

(iii) If the dwelling unit includes its own sanitary facility, it must be in proper operating condition, usable in privacy, and adequate for personal

hygiene and the disposal of human waste.

(iv) The dwelling unit must include at least one battery-operated or hard-wired smoke detector, in proper working condition, on each level of the unit.

(5) *Common areas.* The common areas must be structurally sound, secure, and functionally adequate for the purposes intended. The basement/garage/carport, restrooms, closets, utility, mechanical, community rooms, day care, halls/corridors, stairs, kitchens, laundry rooms, office, porch, patio, balcony, and trash collection areas, if applicable, must be free of health and safety hazards, operable, and in good repair. All common area ceilings, doors, floors, HVAC, lighting, outlets/switches, smoke detectors, stairs, walls, and windows, to the extent applicable, must be free of health and safety hazards, operable, and in good repair.

(6) *Health and safety concerns.* All areas and components of the housing must be free of health and safety hazards. These areas include, but are not limited to, air quality, electrical hazards, elevators, emergency/fire exits, flammable materials, garbage and debris, handrail hazards, infestation, and lead-based paint. For example, the buildings must have fire exits that are not blocked and have hand rails that are undamaged and have no other observable deficiencies. The housing must have no evidence of infestation by rats, mice, or other vermin, or of garbage and debris. The housing must have no evidence of electrical hazards, natural hazards, or fire hazards. The dwelling units and common areas must have proper ventilation and be free of mold, odor (e.g., propane, natural gas, methane gas), or other observable deficiencies. The housing must comply with all requirements related to the evaluation and reduction of lead-based paint hazards and have available proper certifications of such (see 24 CFR part 35).

(b) Appendix A to this part lists the areas to be inspected and the items in each area to be inspected.

##### **§ 902.25 Physical condition scoring and thresholds.**

(a) *Scoring.* Under PHAS Indicator #1, REAC will calculate a score of the overall condition of the PHA's public housing portfolio that reflects weights based on the relative importance of the individual inspectable areas and the relative severity of the deficiencies observed.

(b) *Adjustment for physical condition (project age) and neighborhood environment.* In accordance with section 6(j)(1)(I)(2) of the 1937 Act (42



U.S.C. 1437d(j)(1)(I)(2)), the physical score for a project will be upwardly adjusted to the extent that negative conditions are caused by situations outside the control of the PHA. These situations are related to the poor physical condition of the project or the overall depressed condition of the immediately surrounding neighborhood. The intent of this adjustment is to not unfairly penalize the PHA, and to appropriately apply the adjustment.

(1) *Adjustments in three areas.*

Adjustments to the PHA physical project score will be made in three factually observed and assessed areas (inspectable areas):

- (i) Physical condition of the site;
- (ii) Physical condition of the common areas on the project; and
- (iii) Physical condition of the building exteriors.

(2) *Definitions.* Definitions and application of physical condition and neighborhood environment factors are:

(i) Physical condition applies to projects over 10 years old and that have not had substantial rehabilitation in the last 10 years.

(ii) Neighborhood environment applies to projects located where the immediate surrounding neighborhood (that is a majority of the population that resides in the census tracts or census block groups on all sides of the development) has at least 51 percent of families with incomes below the poverty rate as documented by the latest census data.

(3) Adjustment is for physical condition (project age) and neighborhood environment. HUD will adjust the physical score of a PHA's project subject to both the physical condition (project age) and neighborhood environment conditions. The adjustments will be made to the scores assigned to the applicable inspectable areas so as to reflect the difficulty in managing. In each instance where the actual physical condition of the inspectable area (site, common areas, building exterior) is rated below the maximum score for that area, 1 point will be added, but not to exceed the maximum number of points available to that inspectable area.

(i) These extra points will be added to the score of the specific inspectable area, by project, to which these conditions may apply. A PHA is required to certify on form HUD-50072, PHAS Certification (which is available from the Department of Housing and Urban Development, HUD Customer Service Center, 451 Seventh Street, SW, Room B-102, Washington, DC 20410; telephone (800) 767-7468), the extent to which the conditions apply, and to the

inspectable area the extra scoring point should be added.

(ii) A PHA that receives the maximum potential weighted points on the inspectable areas may not claim any additional adjustments for physical condition and/or neighborhood environments for the respective inspectable area(s). In no circumstance shall a PHA's score for the inspectable area, after any adjustment(s) for physical condition and/or neighborhood environments, exceed the maximum potential weighted points assigned to the respective inspectable area(s).

(4) *Scattered site projects.* The Date of Full Availability (DOFA) shall apply to scattered site projects, where the age of units and buildings vary, to determine whether the projects have received substantial rehabilitation within the past 10 years and are eligible for an adjusted score for the Physical Condition Indicator.

(5) *Maintenance of supporting documentation.* PHAs shall maintain supporting documentation to show how they arrived at the determination that the project's score is subject to adjustment under this section.

(i) If the basis was neighborhood environments, the PHA shall have on file the appropriate maps showing the census block groups surrounding the development(s) in question with supporting census data showing the level of poverty. Projects that fall into this category but which have already been removed from consideration for other reasons (permitted exemptions and modifications and/or exclusions) shall not be counted in this calculation.

(ii) For the physical condition factor, a PHA would have to maintain documentation showing the age and condition of the projects and the record of capital improvements, indicating that these particular projects have not received modernization funds.

(iii) PHAs shall also document that in all cases, projects that were exempted for other reasons were not included in the calculation.

(c) *Thresholds.* In order to receive a passing score under the Physical Condition Indicator, the PHA's score must fall above a minimum threshold of 18 points or 60 percent of the available points under this indicator. Further, in order to receive an overall passing score under the PHAS, the PHA must receive a passing score on the Physical Condition Indicator.

**§ 902.27 Physical condition portion of total PHAS points.**

Of the total 100 points available for a PHAS score, a PHA may receive up to

30 points based on the Physical Condition Indicator.

**Subpart C—PHAS Indicator #2: Financial Condition**

**§ 902.30 Financial condition assessment.**

(a) *Objective.* The objective of the Financial Condition Indicator is to measure the financial condition of a PHA for the purpose of evaluating whether it has sufficient financial resources and is capable of managing those financial resources effectively to support the provision of housing that is decent, safe, sanitary and in good repair.

(b) *Financial reporting standards.* A PHA's financial condition will be assessed under this indicator on the basis of the annual financial report provided in accordance with § 902.33.

**§ 902.33 Financial reporting requirements.**

(a) *Annual financial reports.* PHAs must provide to HUD, on an annual basis, such financial information, as required by HUD. The financial information must be:

- (1) Prepared in accordance with Generally Accepted Accounting Principles (GAAP) as further defined by HUD in supplementary guidance;
- (2) Submitted electronically in the electronic format designated by HUD; and
- (3) Submitted in such form and substance prescribed by HUD.

(b) *Annual financial report filing dates.* The financial information to be submitted to HUD in accordance with paragraph (a) of this section, must be submitted to HUD annually, no later than 60 days after the end of the fiscal year of the reporting period, and as otherwise provided by law.

(c) *Reporting compliance dates.* The requirement for compliance with the financial reporting requirements of this section begins with PHAs with fiscal years ending September 30, 1999 and thereafter. Unaudited financial statements will be required 60 days after the PHA's fiscal year end, and audited financial statements will then be required no later than 9 months after the PHA's fiscal year end, in accordance with the Single Audit Act and OMB Circular A-133. (See 24 CFR 84.26). A PHA with a fiscal year ending September 30, 1999 that elects to submit its unaudited report earlier than the due date of November 30, 1999 must submit its financial report as required in this section. On or after September 30, 1998, but prior to November 30, 1999 (except for a PHA with its fiscal year ending September 30, 1999), PHAs may submit their financial reports in accordance with this section.

**§ 902.35 Financial condition scoring and thresholds.**

(a) *Scoring.* Under PHAS Indicator #2, REAC will calculate a score that relies on the key components of financial health and management as well as audit and internal control flags.

(1) The key components of PHAS Indicator #2 include:

(i) *Current Ratio*—current assets divided by current liabilities;

(ii) *Number of Months Expendable Fund Balance*—number of months a PHA can operate on the Expendable Fund Balance without additional resources; Expendable Fund Balance is the portion of the fund balance representing expendable available financial resources; unreserved and undesignated fund balance;

(iii) *Days Receivable Outstanding*—average number of days tenant receivables are outstanding;

(iv) *Vacancy Loss*—loss of potential rent due to vacancy;

(v) *Expense Management/Energy Consumption*—expense per unit for key expenses, including energy consumption, and other expenses such as utilities, maintenance, security; and

(vi) *Net Income or Loss divided by the Expendable Fund Balance*—measures how the year's operations have affected the PHA's viability.

(2) *Additional components.* Additional components may be used to identify circumstances in which there exists the possibility of higher risk of waste, fraud and abuse. These components will be used to detect fraud and will be used to generate "flags" that will signal field staff, Enforcement Center staff, or fraud investigators to take appropriate action. These components will primarily relate to financial management, but may also be used to provide a PHA with benchmarking information to allow the PHA to measure its own performance against its peers.

(b) *Thresholds.* In order to receive a passing score under the Financial Condition Indicator, the PHA's score must fall above a minimum threshold of 18 points or 60 percent of the available points under this indicator. Further, in order to receive an overall passing score under the PHAS, the PHA must receive a passing score on the Financial Condition Indicator.

**§ 902.37 Financial condition portion of total PHAS points.**

Of the total 100 points available for a PHAS score, a PHA may receive up to 30 points based on the Financial Condition Indicator.

**Subpart D—PHAS Indicator #3: Management Operations****§ 902.40 Management operations assessment.**

(a) *Objective.* The objective of the Management Operations Indicator is to measure certain key management operations and responsibilities of a PHA for the purpose of assessing the PHA's management operations capabilities.

(b) *Management assessment.* PHAS Indicator #3 pertaining to Management Operations incorporates the majority of the statutory indicators of section 6(j) of the U.S. Housing Act of 1937, and an additional nonstatutory indicator (security), as provided in § 902.43.

**§ 902.43 Management operations performance standards.**

(a) *Management operations indicators.* The following indicators will be used to assess a PHA's management operations:

(1) *Management Indicator #1—Vacancy rate and unit turnaround time.* This management indicator examines the vacancy rate, a PHA's progress in reducing vacancies, and unit turnaround time. Implicit in this management indicator is the adequacy of the PHA's system to track the duration of vacancies and unit turnaround, including down time, make ready time, and lease up time.

(2) *Management Indicator #2—Modernization.* This management indicator is automatically excluded if a PHA does not have a modernization program. This management indicator examines the amount of unexpended funds over 3 Federal fiscal years (FFY) old, the timeliness of fund obligation, the adequacy of contract administration, the quality of the physical work, and the adequacy of budget controls. All components of this management indicator apply to the Comprehensive Grant Program (CGP), the Comprehensive Improvement Assistance Program (CIAP), the HOPE VI assistance, vacancy reduction, and lead based paint risk assessment funding (1992–1995), and any successor program(s) to the CGP or the CIAP.

(3) *Management Indicator #3—Rents uncollected.* This management indicator examines the PHA's ability to collect dwelling rents owed by residents in possession during the immediate past fiscal year by measuring the balance of dwelling rents uncollected as a percentage of total dwelling rents to be collected.

(4) *Management Indicator #4—Work orders.* This management indicator examines the time it takes to complete or abate emergency work orders, the

average number of days nonemergency work order were active, and any progress a PHA has made during the preceding 3 years to reduce the period of time nonemergency maintenance work orders were active. Implicit in this management indicator is the adequacy of the PHA's work order system in terms of how a PHA accounts for and controls its work orders, and its timeliness in preparing/issuing work orders.

(5) *Management Indicator #5—PHA annual inspection of units and systems.*

This management indicator examines the percentage of units that a PHA inspects on an annual basis in order to determine short-term maintenance needs and long-term modernization needs. This management indicator requires a PHA's inspection to utilize the HUD uniform physical condition standards set forth in subpart B of this part. All occupied units are required to be inspected.

(6) *Management Indicator #6—Security.* This management indicator evaluates the PHA's performance in tracking crime related problems in their developments, reporting incidence of crime to local law enforcement agencies, the adoption and implementation, consistent with section 9 of the Housing Opportunity Program Extension Act of 1996 (One-Strike and You're Out) (42 U.S.C. 1437d(r)), of applicant screening and resident eviction policies and procedures, and, as applicable, PHA performance under any HUD drug prevention or crime reduction grant(s). A PHA may receive credit for performance under non-HUD funded programs if it provides auditable financial and statistical documentation for these programs.

(b) *Reporting on performance under the Management Operations Indicator.* Each PHA will provide to HUD a certification on its performance under each of the management indicators in paragraph (a) of this section. The certifications shall comply with the requirements of § 902.60.

**§ 902.45 Management operations scoring and thresholds.**

(a) *Scoring.* Under PHAS Indicator #3, REAC will calculate a score of the overall management operations of a PHA that reflects weights based on the relative importance of the individual management indicators.

(b) *Thresholds.* In order to receive a passing score under the Management Operations Indicator, the PHA's score must fall above a minimum threshold of 18 points or 60 percent of the available points under this PHAS Indicator #3. Further, in order to receive an overall passing score under the PHAS, the PHA

must receive a passing score on the Management Operations Indicator.

**§ 902.47 Management operations portion of total PHAS points.**

Of the total 100 points available for a PHAS score, a PHA may receive up to 30 points based on the Management Operations Indicator.

**Subpart E—PHAS Indicator #4: Resident Service and Satisfaction**

**§ 902.50 Resident service and satisfaction assessment.**

(a) *Objective.* The objective of the Resident Service and Satisfaction Indicator is to measure the level of resident satisfaction with living conditions at the PHA.

(b) *Reporting information on resident service and satisfaction.* The assessment will be performed through the use of a resident service and satisfaction survey. The survey process will be managed by the PHA in accordance with a methodology prescribed by HUD. The PHA will be responsible for maintaining original copies of completed survey data, subject to independent audit, and for developing a follow-up plan to address issues resulting from the survey.

**§ 902.53 Resident service and satisfaction scoring and thresholds.**

(a) *Scoring.* Under the PHAS Indicator #4, REAC will calculate a score based upon two components that receive points and a third component that is a threshold requirement. One component will be the point score of the survey results. The survey content will focus on resident evaluation of the overall living conditions, to include basic constructs such as: maintenance and repair (i.e., work order response); communications (i.e., perceived effectiveness); safety (i.e., perception of personal security); services (i.e., recreation and personal programs); and neighborhood appearance. The second component will be a point score based on the level of implementation and follow-up or corrective actions based on the results of the survey. The final component, which is not scored for points, but which is a threshold requirement, is verification that the survey process was managed in a manner consistent with guidance provided by HUD.

(b) *Thresholds.* A PHA will not receive any points under PHAS Indicator #4 if the survey process is not managed as directed by HUD or the survey results are determined to be altered. A PHA will receive a passing score on the Resident Service and Satisfaction Indicator if it receives at

least 6 points, or 60% of the available points under this PHAS Indicator #4.

**§ 902.55 Resident service and satisfaction portion of total PHAS points.**

Of the total 100 points available for a PHAS score, a PHA may receive up to 10 points based on the Resident Service and Satisfaction Indicator.

**Subpart F—PHAS Scoring**

**§ 902.60 Data collection.**

(a) *Fiscal Year Reporting Period—limitation on changes after PHAS effectiveness.* An assessed fiscal year for purposes of the PHAS corresponds to a PHA's fiscal year. To allow for a period of consistent assessments to refine and make necessary adjustments to the PHAS, a PHA is not permitted to change its fiscal year for the first 3 full fiscal years following the effective date of this part (see § 902.1(e)).

(b) *Physical Condition information.* Information necessary to conduct the physical condition assessment under subpart B of this part will be obtained from HUD inspectors during the fiscal year being scored through electronic transmission of the data.

(c) *Financial Condition information.* Year-end financial information to conduct the assessment under subpart C, Financial Condition, of this part will be submitted by a PHA through electronic transmission of the data to HUD not later than 60 days after the end of the PHA's fiscal year. An audited report of the year-end financial information is due not later than 9 months after the end of the PHA's fiscal year.

(d) *Management Operations and Resident Service and Satisfaction Information.* A PHA shall provide certification to HUD as to data required under subpart D, Management Operations, of this part and subpart E, Resident Service and Satisfaction, of this part not later than 60 days after the end of the PHA's fiscal year.

(1) The certification shall be approved by PHA Board resolution, and signed and attested to by the Executive Director.

(2) PHAs shall maintain documentation for 3 years verifying all certified indicators for HUD on-site review.

(e) *Failure to submit data by due date.* If a PHA without a finding of good cause by HUD does not submit its certifications or year-end financial information, required by this part, or submits its certifications or year-end financial information more than 15 days past the due date, appropriate sanctions may be imposed, including a reduction

of 1 point in the total PHAS score for each 15-day period past the due date. If all certifications or year-end financial information are not received within 90 days past the due date, the PHA will receive a presumptive rating of failure in all of the PHAS indicators and components certified to, which shall result in troubled and mod-troubled designations.

(f) *Verification of information submitted.* (1) A PHA's certifications, year-end financial information and any supporting documentation are subject to verification by HUD at any time.

Appropriate sanctions for intentional false certification will be imposed, including civil penalties, suspension or debarment of the signatories, the loss of high performer designation, a lower score under individual PHAS indicators and a lower overall PHAS score.

(2) A PHA that cannot provide justifying documentation to REAC, or to the PHA's independent auditor for the assessment under any indicator(s) or component(s) shall receive a score of 0 for the relevant indicator(s) or component(s), and its overall PHAS score shall be lowered.

(3) A PHA's PHAS score under individual indicators or components, or its overall PHAS score, may be changed by HUD pursuant to the data included in the independent audit report, or obtained through such sources as HUD on-site review, investigations by HUD's Office of Fair Housing and Equal Opportunity, or reinspection by REAC, as applicable.

(g) *Management operations assumed by an RMC.* For those developments of a PHA where management operations have been assumed by an RMC, the PHA's certification shall identify the development and the management functions assumed by the RMC. The PHA shall obtain a certified questionnaire from the RMC as to the management functions undertaken by the RMC. Following verification of the RMC's certification, the PHA shall submit the RMC's certified questionnaire along with its own. The RMC's certification shall be approved by its Executive Director or Chief Executive Officer or responsible party.

**§ 902.63 PHAS scoring.**

(a) *Issuance of score by HUD.* An overall PHAS score will be issued by REAC for each PHA 60 to 90 days after the end of the PHA's fiscal year.

(b) *Computing the PHAS score.* Each of the four PHAS indicators in this part will be scored individually, and then will be used to determine an overall score for the PHA. Components within each of the four PHAS indicators will be

scored individually, and the scores for the components will be used to determine a single score for each of the PHAS indicators.

(c) *Adjustments to the PHAS score.* Adjustments to the score may be made after a PHA's audit report for the year being assessed is transmitted to HUD. If significant differences (as defined in GAAP guidance materials provided to PHAs) are noted between unaudited and audited results, a PHA's PHAS score will be raised or lowered, as applicable, in accordance with the audited results.

(d) *Posting and publication of PHAS scores.* Each PHA shall post a notice of its final PHAS score and status in appropriate conspicuous and accessible locations in its offices within 2 weeks of receipt of its final score and status. In addition, HUD will publish every PHA's score and status in the **Federal Register**.

#### **§ 902.67 Score and designation status.**

*Designation status corresponding to score.* A PHA will be scored with a corresponding designation of status as follows:

(a) *High Performer.* A PHA that achieves a score of at least 60 percent of the points available under each of the four PHAS Indicators (addressed in subparts B through E of this part) and achieves an overall PHAS score of 90 percent or greater shall be designated a high performer. A PHA shall not be designated a high performer if it scores below the threshold established for any indicator. High performers will be afforded incentives that include relief from reporting and other requirements, as described in § 902.71.

(b) *Standard Performer.* A PHA that achieves a total PHAS score of less than 90 percent but not less than 60 percent shall be designated a standard performer. All standard performers must correct reported deficiencies. A standard performer that receives a score less than 70 percent but not less than 60 percent shall be subject to other oversight, as described in § 902.73. A PHA that achieves a score of less than 60 percent of the total points available under PHAS Indicators 1, 2, or 3 shall not be designated a standard performer, but shall be designated a troubled performer, as provided in paragraph (c) of this section.

(c) *Troubled Performer.* A PHA that achieves a total PHAS score of less than 60 percent, or achieves a score of less than 60 percent of the total points available under PHAS Indicators 1, 2, or 3, shall be designated as troubled, and referred to the TARC as described in § 902.75. In accordance with section 6(j)(2) of the 1937 Act, a PHA that receives less than 60 percent of the

maximum calculation for the modernization indicator under PHAS Indicator #3 (Management Operations, subpart D of this part) may be subject to the following sanctions: under the Comprehensive Grant Program to a reduction of formula allocation or other sanctions (24 CFR part 968, subpart C); under the Comprehensive Improvement Assistance Program to disapproval of new funding or other sanctions (24 CFR part 968, subpart B); or disapproval of funding under the HOPE VI Program.

#### **§ 902.69 PHA right of petition and appeal.**

(a) *Appeal of troubled designation and petition for removal.* A PHA may:

- (1) Appeal designation as a troubled agency (including designation as troubled with respect to the modernization program);
- (2) Petition for removal of such designation; and
- (3) Appeal any refusal to remove such designation.

(b) *Appeal process.* The appeal shall be submitted by a PHA to the REAC within 30 days of a PHA's receipt of its score, and shall include supporting documentation and justification of the reasons for the appeal. An appeal submitted to the REAC without appropriate documentation will not be considered and will be returned to the PHA.

(c) *Consideration of appeal by REAC.* Upon receipt of an appeal from a PHA, the REAC will convene a Board of Review (the Board) to evaluate the appeal and its merits for the purpose of determining whether a reassessment of the PHA is warranted. Board membership will be comprised of a representative from REAC, the Office of Public and Indian Housing, and such other office or representative as the Secretary may designate (excluding, however, representation from the Troubled Agency Recovery Center). For purposes of reassessment, the REAC will schedule a reinspection and/or acquire audit services, as determined by the Board, and a new score will be issued, if appropriate.

(d) *Final appeal decisions.* HUD will make final decisions of appeals within 30 days of receipt of an appeal, and may extend this period an additional 30 days if further inquiry is necessary. Failure by a PHA to submit requested information within the 30-day period or any additional period granted by HUD is grounds for denial of an appeal.

#### **Subpart G—PHAS Incentives and Remedies**

##### **§ 902.71 Incentives for high performers.**

(a) *Incentives for high-performer PHAs.* A PHA that is designated a high

performer will be eligible for the following incentives:

(1) *Relief from specific HUD requirements.* A PHA that is designated high performer will be relieved of specific HUD requirements (for example, fewer reviews and less monitoring), effective upon notification of high performer designation.

(2) *Public recognition.* High-performer PHAs and RMCs that receive a score of at least 60 percent of the points available under each of the four PHAS Indicators and achieves an overall PHAS score of 90, will receive a Certificate of Commendation from HUD as well as special public recognition, as provided by the HUB/Program Center.

(3) *Bonus points in funding competitions.* A high-performer PHA will be eligible for bonus points in HUD's funding competitions, where such bonus points are not restricted by statute or regulation governing the funding program.

(b) *Compliance with applicable Federal laws and regulations.* Relief from any standard procedural requirement that may be provided under this section, does not mean that a PHA is relieved from compliance with the provisions of Federal law and regulations or other handbook requirements. For example, although a high performer or standard performer may be relieved of requirements for prior HUD approval for certain types of contracts for services, the PHA must still comply with all other Federal and State requirements that remain in effect, such as those for competitive bidding or competitive negotiation (see 24 CFR 85.36).

(c) *Audits and reviews not relieved by designation.* A PHA designated as a high performer or standard performer remains subject to:

- (1) Regular independent auditor (IA) audits.
- (2) Office of Inspector General (OIG) audits or investigations will continue to be conducted as circumstances may warrant.

#### **§ 902.73 Referral to an Area HUB/Program Center.**

(a) Standard performers will be referred to the HUB/Program Center for appropriate action. A standard performer that receives a total score of less than 70 percent but not less than 60 percent shall be required to submit an Improvement Plan to eliminate deficiencies in the PHA's performance. A standard performer that receives a score of not less than 70 percent may be required, at the discretion of the appropriate area HUB/Program Center,

to submit an Improvement Plan to address specific deficiencies.

(b) *Submission of an Improvement Plan.* (1) Within 30 days after a PHAS score is issued, a standard performer with a score less than 70 percent is required to submit an Improvement Plan, which includes the information stated in paragraph (d) of this section and determined acceptable by the HUB/Program Center, for each indicator and/or component identified as deficient as well as other performance and/or compliance deficiencies as may be identified as a result of an on-site review of the PHA's operations. An RMC that is required to submit an Improvement Plan must develop the plan in consultation with its PHA and submit the Plan to the HUB/Program Center through its PHA.

(2) The HUB/Program Center may require, on a risk management basis, a standard performer with a score of not less than 70 percent to submit within 30 days after receipt of its PHAS score an Improvement Plan, which includes the information stated in paragraph (d) of this section, for each indicator and/or component of a PHAS indicator identified as deficient.

(c) *Correction of deficiencies.* (1) *Time period for correction.* After a PHA's receipt of its PHAS score and designation as a standard performer or, in the case of an RMC, notification of its score from a PHA, a PHA or RMC shall correct any deficiency indicated in its assessment within 90 days, or within such period as provided in the HUD approved Improvement Plan if an Improvement Plan is required.

(2) *Notification and report to HUB/Program Center.* A PHA shall notify the HUB/Program Center of its action to correct a deficiency. A PHA shall also forward to the HUB/Program Center an RMC's report of its action to correct a deficiency.

(d) *Improvement Plan.* An Improvement Plan shall:

(1) Identify baseline data, which should be raw data but may be the PHA's score under each individual PHAS indicator and/or component that was identified as a deficiency;

(2) Describe the procedures that will be followed to correct each deficiency;

(3) Provide a timetable for the correction of each deficiency; and

(4) Provide for or facilitate technical assistance to the PHA.

(e) *Determination of acceptability of Improvement Plan* (1) The HUB/Program Center will approve or deny a PHA's (or RMC's Improvement Plan submitted to the HUB/Program Center through the RMC's PHA), and notify the PHA of its decision. A PHA that submits

an RMC's Improvement Plan must notify the RMC in writing, immediately upon receipt of the HUB/Program Center notification, of the HUB/Program Center approval or denial of the RMC's Improvement Plan.

(2) An Improvement Plan that is not approved will be returned to the PHA with recommendations from the HUB/Program Center for revising the Improvement Plan to obtain approval.

(f) *Submission of revised Improvement Plan.* A revised Improvement Plan shall be resubmitted by the PHA within 30 calendar days of its receipt of the HUB/Program Center recommendations.

(g) *Failure to submit acceptable Improvement Plan.* If a PHA fails to submit an acceptable Improvement Plan, or to correct deficiencies within the time specified in an Improvement Plan or such extensions as may be granted by HUD, the HUB/Program Center will notify the PHA of its noncompliance. The PHA (or the RMC through the PHA) will provide the HUB/Program Center its reasons for lack of progress in submitting or carrying out the Improvement Plan within 30 calendar days of its receipt of the noncompliance notification. HUD will advise the PHA as to the acceptability of its reasons for lack of progress and, if unacceptable, will notify the PHA that it will be referred to the TARC for remedial actions or such actions as the TARC may determine appropriate in accordance with the provisions of the ACC, this part and other HUD regulations. If the TARC determines that it is appropriate to refer the PHA to the Enforcement Center, it will only do so after the PHA has had 1 year since the issuance of the PHAS score (or, in the case of an RMC, notification of its score from a PHA) to correct its deficiencies.

#### **§ 902.75 Referral to a TARC.**

Upon designation of a PHA as troubled, in accordance with the requirements of section 6(j)(2)(B) of the 1937 Act and in accordance with this part, the REAC shall refer each troubled PHA to the PHA's area TARC for remedial action. The actions to be taken by the TARC and the PHA shall be as follows:

(a) *Recovery plan and MOA.* Within 30 days of notification of the designation of a troubled PHA within its area, the appropriate TARC will deploy an on-site team to develop a Recovery Plan. The Recovery Plan shall include recommendations for improvements to correct or eliminate deficiencies that resulted in a failing PHAS score and designation as troubled. The Recovery Plan will incorporate a memorandum of

agreement (MOA) as described in paragraph (c) of this section.

(b) *PHA review of recovery plan and MOA.* The PHA will have 10 days to review the recovery plan and the MOA. During this 10-day period, the PHA shall resolve any claimed discrepancies in the plan with its area TARC, and discuss any recommended changes and target dates for improvement to be incorporated in the final MOA. Unless the time period is extended by the TARC, the MOA is to be executed 15 days following issuance of the preliminary MOA.

(c) *Memorandum of agreement (MOA).* The final MOA is a binding contractual agreement between HUD and a PHA. The scope of the MOA may vary depending upon the extent of the problems present in the PHA, but shall include:

(1) Baseline data, which should be raw data but may be the PHA's score in each of the PHAS indicators or components identified as a deficiency;

(2) Annual and quarterly performance targets, which may be the attainment of a higher score within an indicator that is a problem, or the description of a goal to be achieved;

(3) Strategies to be used by the PHA in achieving the performance targets within the time period of the MOA;

(4) Technical assistance to the PHA provided or facilitated by HUD, for example, the training of PHA employees in specific management areas or assistance in the resolution of outstanding HUD monitoring findings;

(5) The PHA's commitment to take all actions within its control to achieve the targets;

(6) Incentives for meeting such targets, such as the removal of troubled or mod-troubled designation and Departmental recognition for the most improved PHAS;

(7) The consequences of failing to meet the targets, including, but not limited to, such sanctions as the imposition of budget and management controls by the TARC, declaration of substantial default and subsequent actions, including referral to the Enforcement Center for judicial appointment of a receiver, limited denial of participation, suspension, debarment, or other actions deemed appropriate by the Enforcement Center; and

(8) A description of the involvement of local public and private entities, including PHA resident leaders, in carrying out the agreement and rectifying the PHA's problems. A PHA shall have primary responsibility for obtaining active local public and private entity participation, including the

involvement of public housing resident leaders, in assisting PHA improvement efforts. Local public and private entity participation should be premised upon the participant's knowledge of the PHA, ability to contribute technical expertise with regard to the PHA's specific problem areas and authority to make preliminary/tentative commitments of support, financial or otherwise.

(d) *Maximum recovery period.* Unless extended by the TARC and documented in the MOA, the maximum recovery period for a troubled PHA is the first full fiscal year following execution of the MOA.

(e) *Parties to the MOA.* An MOA shall be executed by:

(1) The PHA Board Chairperson and accompanied by a Board resolution, or a receiver (pursuant to a court ordered receivership agreement, if applicable) or other AME acting in lieu of the PHA Board;

(2) The PHA Executive Director, or a designated receiver (pursuant to a court ordered receivership agreement, if applicable) or other AME-designated Chief Executive Officer;

(3) The Director of the area TARC; and

(4) The appointing authorities of the Board of Commissioners, unless exempted by the HUD/Program Center.

(f) *Involvement of resident leadership in the MOA.* HUD encourages the inclusion of the resident leadership in the execution of the MOA.

(g) *Failure to execute MOA or make substantial improvement under MOA.*

(1) If a troubled PHA does not execute an MOA within the period provided in paragraph (b) of this section, or the TARC determines that the PHA does not show a substantial improvement toward a passing PHAS score following the issuance of the failing PHAS score by the REAC, the TARC shall refer the PHA to the Enforcement Center, which shall initiate proceedings for judicial appointment of a receiver, and other sanctions as may be appropriate. For purposes of this paragraph (g), *substantial improvement* is defined as 50 percent of the points needed to achieve a passing PHAS score as determined by the REAC. The maximum period of time for remaining in troubled status before being referred to the Enforcement Center is 2 years.

(2) The following example illustrates the provisions of paragraph (g)(1) of this section:

*Example:* A PHA receives a score of 50; 60 is a passing score. The PHA is referred to the TARC. Within 1 year after the score is issued to the PHA, the PHA must achieve a 5-point increase to continue recovery efforts in the TARC. If the PHA fails to achieve the 5-point increase, the PHA will be referred to the

Enforcement Center. The maximum period of time for remaining in troubled status before being referred to the Enforcement Center is 2 years.

(h) To the extent feasible, while a PHA is under a referral to a TARC, all services to residents will continue uninterrupted.

#### **§ 902.77 Referral to the Enforcement Center.**

(a) Failure of a troubled PHA to execute or meet the requirements of a memorandum of agreement in accordance with § 902.75 constitutes a substantial default in accordance with § 902.79 and shall result in referral to the Enforcement Center. The Enforcement Center is officially responsible for recommending to the Assistant Secretary for Public and Indian Housing that a troubled performer PHA be declared in substantial default. The Enforcement Center shall initiate the judicial appointment of a receiver or the interventions provided in § 902.83; and may initiate limited denial of participation, suspension, debarment, the imposition of other sanctions available to the Enforcement Center including referral to the appropriate Federal government agencies or offices for the imposition of civil or criminal sanctions.

(b) To the extent feasible, while a PHA is under a referral to the Enforcement Center, all services to residents will continue uninterrupted.

#### **§ 902.79 Substantial default.**

(a) *Events or conditions that constitute substantial default.* The following events or conditions shall constitute substantial default.

(1) HUD may determine that events have occurred or that conditions exist that constitute a substantial default if a PHA is determined to be in violation of Federal statutes, including but not limited to, the 1937 Act, or in violation of regulations implementing such statutory requirements, whether or not such violations would constitute a substantial breach or default under provisions of the relevant ACC.

(2) HUD may determine that a PHA's failure to satisfy the terms of a memorandum of agreement entered into in accordance with § 902.75, or to make reasonable progress to execute or meet requirements included in a memorandum of agreement, are events or conditions that constitute a substantial default.

(3) HUD shall determine that a PHA that has been designated as troubled and does not show substantial improvement, as defined in § 902.75(g), in its PHAS

score in 1 year following issuance of the failed score is in substantial default.

(4) HUD may declare a substantial breach or default under the ACC, in accordance with its terms and conditions.

(5) HUD may determine that the events or conditions constituting a substantial default are limited to a portion of a PHA's public housing operations, designated either by program, by operational area, or by development(s).

(b) *Notification of substantial default and response.* If information from an annual assessment or audit, or any other credible source (including but not limited to the Office of Fair Housing Enforcement, the Office of the Inspector General, a judicial referral or a referral from a mayor or other official) indicates that there may exist events or conditions constituting a substantial breach or default, HUD shall advise a PHA of such information. HUD is authorized to protect the confidentiality of the source(s) of such information in appropriate cases. Before taking further action, except in cases of apparent fraud or criminality, and/or in cases where emergency conditions exist posing an imminent threat to the life, health, or safety of residents, HUD shall afford the PHA a timely opportunity to initiate corrective action, including the remedies and procedures available to PHAs designated as troubled PHAs, or to demonstrate that the information is incorrect.

(1) *Form of notification.* Upon a determination or finding that events have occurred or that conditions exist that constitute a substantial default, the Assistant Secretary shall provide written notification of such determination or finding to the affected PHA. Written notification shall be transmitted to the Executive Director, the Chairperson of the Board, and the appointing authority(ies) of the Board, and shall include, but is not limited to:

(i) Identification of the specific covenants, conditions, and/or agreements under which the PHA is determined to be in noncompliance;

(ii) Identification of the specific events, occurrences, or conditions that constitute the determined noncompliance;

(iii) Citation of the communications and opportunities to effect remedies afforded pursuant to paragraph (a) of this section;

(iv) Notification to the PHA of a specific time period, to be not less than 10 calendar days, except in cases of apparent fraud or other criminal behavior, and/or under emergency conditions as described in paragraph (a)

of this section, nor more than 30 calendar days, during which the PHA shall be required to demonstrate that the determination or finding is not substantively accurate; and

(v) Notification to the PHA that, absent a satisfactory response in accordance with paragraph (b) of this section, HUD will refer the PHA to the Enforcement Center, using any or all of the interventions specified in § 902.83, and determined to be appropriate to remedy the noncompliance, citing § 902.83, and any additional authority for such action.

(2) *Receipt of notification.* Upon receipt of the notification described in paragraph (b)(1) of this section, the PHA must demonstrate, within the time period permitted in the notification, factual error in HUD's description of events, occurrences, or conditions, or show that the events, occurrences, or conditions do not constitute noncompliance with the statute, regulation, or covenants or conditions to which the PHA is cited in the notification.

(3) *Waiver of notification.* A PHA may waive, in writing, receipt of explicit notice from HUD as to a finding of substantial default, and voluntarily consent to a determination of substantial default. The PHA must concur on the existence of substantial default conditions which can be remedied by technical assistance, and the PHA shall provide HUD with written assurances that all deficiencies will be addressed by the PHA. HUD will then immediately proceed with interventions as provided in § 902.83.

(4) *Emergency situations.* In any situation determined to be an emergency, or in any case where the events or conditions precipitating the intervention are determined to be the result of criminal or fraudulent activity, the Secretary or the Secretary's designee is authorized to intercede to protect the residents' and HUD's interests by causing the proposed interventions to be implemented without further appeals or delays.

#### **§ 902.83 Interventions.**

(a) Interventions under this part (including an assumption of operating responsibilities) may be limited to one or more of a PHA's specific operational areas (e.g., maintenance, modernization, occupancy, or financial management) or to a single development or a group of developments. Under this limited intervention procedure, HUD could select, or participate in the selection of, an AME to assume management responsibility for a specific development, a group of developments

in a geographical area, or a specific operational area, while permitting the PHA to retain responsibility for all programs, operational areas, and developments not so designated.

(b) Upon determining that a substantial default exists under this part, HUD may initiate any interventions deemed necessary to maintain decent, safe, and sanitary dwellings for residents. Such intervention may include:

(1) Providing technical assistance for existing PHA management staff;

(2) Selecting or participating in the selection of an AME to provide technical assistance or other services up to and including contract management of all or any part of the public housing developments administered by a PHA;

(3) Assuming possession and operational responsibility for all or any part of the public housing administered by a PHA;

(4) Entering into agreements, arrangements, and/or contracts for or on behalf of a PHA, or acting as the PHA, and expending or authorizing the expenditure of PHA funds, irrespective of the source of such funds, to remedy the events or conditions constituting the substantial default;

(5) The provision of intervention and assistance necessary to remedy emergency conditions;

(6) After the solicitation of competitive proposals, select an administrative receiver to manage and operate all or part of the PHA's housing; and

(7) Petition for the appointment of a receiver to any District Court of the United States or any court of the State in which real property of the PHA is located.

(c) The receiver is to conduct the affairs of the PHA in a manner consistent with statutory, regulatory, and contractual obligations of the PHA and in accordance with such additional terms and conditions that the court may provide.

(d) The appointment of a receiver pursuant to this section may be terminated upon the petition to the court by the PHA, the receiver, or HUD, and upon a finding by the court that the circumstances or conditions that constituted substantial default by the PHA no longer exist and that the operations of the PHA will be conducted in accordance with applicable statutes and regulations, and contractual covenants and conditions to which the PHA and its public housing programs are subject.

(e) HUD may take the actions described in this part sequentially or simultaneously in any combination.

#### **§ 902.85 Resident petitions for remedial action.**

The total number of residents that petition HUD to take remedial action pursuant to sections 6(j)(3)(A)(i) through (iv) of the 1937 Act must equal at least 20 percent of the residents, or the petition must be from an organization or organizations of residents whose membership must equal at least 20 percent of the PHA's residents.

#### **Appendix A to Part 902—Areas and Items to be Inspected**

##### *AREA: Site*

##### *Items:*

Fencing and Retaining Walls  
Grounds  
Lighting  
Mail Boxes/Project Signs  
Market Appeal  
Parking Lots/Driveways  
Play Areas and Equipment  
Refuse Disposal  
Roads  
Storm Drainage  
Walkways

##### *AREA: Building Exterior*

##### *Items:*

Doors  
Fire Escapes  
Foundations  
Lighting  
Roofs  
Walls  
Windows

##### *AREA: Building Systems*

##### *Items:*

Domestic Water  
Electrical System  
Elevators  
Emergency Power  
Fire Protection  
HVAC  
Sanitary System

##### *AREA: Dwelling Unit*

##### *Items:*

Bathroom  
Cell-for-Aid  
Ceiling  
Doors  
Electrical System  
Floors  
Hot Water Heater  
HVAC System  
Kitchen  
Lighting  
Outlets/Switches  
Patio/Porch/Balcony  
Smoke Detector  
Stairs  
Walls  
Windows

##### *AREA: Common Areas*

##### *Items:*

Basement/Garage/Carport  
Closets/Utility/Mechanical  
Community Room  
Day Care

Halls/Corridors/Stairs  
Kitchen  
Laundry Room  
Lobby  
Office  
Other Community Spaces  
Patio/Porch/Balcony  
Pools and Related Structures  
Restroom  
Storage  
Trash Collection Areas

*AREA: Health and Safety*

Items:

Air Quality  
Electrical Hazards  
Elevator  
Emergency/Fire Exits  
Fire Escapes  
Flammable Materials  
Garbage and Debris  
Ground Fault Interrupters  
Handrails  
Hazards

Hot Water Heater  
Infestation  
Lead Paint  
Pools and Related Structures  
Smoke Detectors

Dated: August 27, 1998.

**Deborah Vincent,**

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and Indian Housing.*

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