U. S. Department of Housing and Urban Development

Office of Public and Indian Housing

Special Attention of:

Administrators, Offices of Native American Programs; Tribes; Tribally Designated Housing Entities (TDHEs); Indian Housing Authorities

NOTICE PIH 2000-18 (TDHEs)

Issued: May 30, 2000

Expires: May 31, 2001

Cross References:
Notice PIH 2000-18 (THDEs)

Attachments:

- Allowable Expense Level (AEL)
- Schedule of Maximum Allowable Dwelling Construction and Equipment Costs Per Unit As Of 10/1/97
- Table of Tribes included in Cost Areas

Subject: Updated Notice - Accounting for program income under the Native American Housing Assistance and Self-Determination Act (NAHASDA)

1. Purpose. This Notice transmits the updated Notice PIH 2000-18 (THDEs), dated April 20, 2000 which is superseded and redated.

2. Updates. Minor corrections were made in the text. An additional Appendix was added that contains the listing of Tribes by cost area. Tribes should refer to the Appendix, “Table of Tribes Included in Cost Areas” to find their cost area. Tribes should then locate their cost area in the Appendix, “Schedule of Maximum Allowable Dwelling Construction and Equipment Costs Per Unit as of 10/1/97” to find their Dwelling Construction and Equipment Costs (DC&E) data.

3. Questions about the Notice. Should Tribes have any questions regarding the Notice, please contact your Area Office of Native American Programs.

/s/
Harold Lucas, Assistant Secretary
for Public and Indian Housing

Attachment

_____PI:Distribution: W-3-1, R-3-1(PIH), R-9, 138-7, 138-8

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NOTICE PIH 2000-18 (TDHEs)

Issued: May 30, 2000

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Cross References:

SUBJECT: Accounting for Program Income under the Native American Housing Assistance and Self-Determination Act (NAHASDA).

I. **Purpose:** This notice provides guidance on accounting for program income generated by the use or disbursement of Indian Housing Block Grant (IHBG) funds.

II. **Background:** The Negotiated Rulemaking Committee, charged with developing regulations to implement the Native American Housing Assistance and Self-Determination Act (NAHASDA), recognized the need for the regulation of funds generated from the use or disbursement of IHBG funds. The Committee crafted language in the program regulations (24 CFR Part 1000 at §1000.62 to satisfy this purpose. In addition, the Committee recognized the need for guidance on accounting for program income generated by the combined use of NAHASDA (IHBG) grants and other funds. The preamble to §1000.62 indicated that this guidance would be developed jointly by HUD and tribal representatives.

A seven member workgroup consisting of four tribal/tribally designated housing entities (TDHEs) and three HUD representatives was appointed by the Co-Chairs of the Committee. This document is the product of that workgroup. The language in this notice was drafted during a series of meetings with tribal/TDHE and HUD workgroup members that began in March 1999 and ended in December 1999.

3. What is Program Income?

3.1. Definition.

Program income is defined as any income realized (generated) from the disbursement or use of IHBG funds; it is income to the IHBG Program of a recipient. Accordingly, it must be income received by the recipient or its subrecipient or received by a contractor <u>on behalf</u> of the recipient or subrecipient.
EXAMPLE: If the recipient or subrecipient makes IHBG loans to Indian families for the purchase of housing, the loan payments made by the families to the recipient or subrecipient are IHBG program income. If a contractor is servicing the IHBG loans and receives the payments on behalf of the recipient or subrecipient, the payments are IHBG program income.

EXAMPLE: Rent received by the recipient or subrecipient from rental housing constructed with IHBG funds and owned by the recipient or subrecipient is program income <u>if</u> there is any income remaining <u>after</u> the rental income is used to pay the expenses of generating the income, e.g., salaries for operating and maintenance staff, owner-paid utilities, insurance, janitorial supplies, normal repairs, and upkeep of the grounds. Program income is net income. If a contractor is managing this housing on behalf of the recipient or subrecipient and collects the rent from the tenants, the net income is IHBG program income.

3.2. Program income <u>includes</u>:

- Fees for services performed.

- Income from the use or rental of real property that was acquired, constructed or rehabilitated with IHBG funds and that is owned by the recipient or subrecipient.

- Income from the sale of commodities or items developed or acquired with IHBG funds.

- Proceeds from the sale or lease of real property acquired, constructed, or rehabilitated (and owned by the recipient) with IHBG funds.

- Sale proceeds from the disposition of any current assisted stock owned by the recipient or entity funded by the recipient. (Note the exception set forth below for proceeds from the sale of homeownership units developed under the 1937 Housing Act.)

- Proceeds from disposition of equipment and supplies bought with IHBG funds.

- Payments of principal and interest on loans made using IHBG funds.

- Proceeds from sale of loans made with IHBG funds.

- Proceeds from sale of obligations secured by loans made with IHBG funds.

- Income from payments of principal and interest earned on IHBG funds prior to disbursement, i.e., interest earned on grant funds which are invested pursuant to §1000.58.

- Interest earned on funds in an IHBG revolving fund pending its use for eligible housing loans.

- Any interest earned on program income pending its use for eligible activities.

Please note that this list is <u>not</u> exclusive and therefore other types of funds may also constitute IHBG program income. Reference: §1000.62(a) & 1000.134

3.3. **Program income <u>does not include</u>:**

- Income generated from the operation of 1937 Act units <u>unless</u> the units are assisted with IHBG grant amounts and the income is attributable to such assistance. [See section 3.4 below.]

- Income which would otherwise be considered program income from IHBG grants if the total income received by a recipient and all its subrecipients in a single program year does not exceed $25,000. Reference §1000.62(b)

- Fees charged to borrowers to recover IHBG funds used to pay the costs of issuing and servicing loans made with IHBG funds. The fees are not program income but are "applicable credits" to the IHBG program in accordance with OMB Circular A-87, Attachment A, paragraph C.3.

- Proceeds from the sale of homeownership units developed under the 1937 Act. [See Question 42A and Answer 42A in the revision to the Transition Notice published in the Federal Register on April 1, 1999 (64 FR 15778).]

Please note that this list is <u>not</u> all-inclusive. Reference: §1000.62.

3.4. Income generated from the operation of 1937 Housing Act units assisted with IHBG grants.

IHBG funds may be used for the operation and maintenance and the rehabilitation of 1937 Housing Act units. When 1937 Housing Act units are assisted with IHBG funds, the income from the units is program income if it is attributable to the IHBG assistance.

To determine how much of the income is program income when the IHBG funds are used for operation and maintenance of rental units, the amount of income received from such units before the date of the enactment of NAHASDA (10/01/1997) must be considered. Instead of having to determine and track the actual amount of rent received for each 1937 Housing Act rental unit as of the date of the enactment of NAHASDA, a surrogate will be used. This surrogate is 46% of the Allowable Expense Level (AEL) for the recipient. This number reflects the national average for rents received for 1937 Housing Act units in the last year of the 1937 Housing Act programs for Indians. The AEL and 46% of the AEL for each Indian tribe with 1937 Housing Act units are set forth in the Appendix. The AEL is defined in §1000.302. Program income is the amount of total income for a project identified as Formula Current Assisted Stock (FCAS) on the tribe's Formula Response Form that exceeds 46% of the per unit AEL times the number of units in the project. The calculation may be done monthly or annually.

EXAMPLE: The recipient received $9600 during its program year ($800 per month) of rental income from a low-rent 1937 Housing Act project consisting of 4 units and identified as FCAS on the tribe's Formula Response Form. The AEL is $4800 per unit per year ($400 per unit per month) and 46% of AEL per unit per year is $2208 ($184 per unit per month). Multiplying 46% of AEL times 4 units gives us $8832 per project per year ($736 per project per month). The amount of program income for the year for that project is $9600 minus $8832 or $768 per year ($800 minus $736 or $64 per month). If this example is changed so that the rent received during the program year for the project is $8832 or less, there is no program income generated by the project.

In the Mutual Help Program, each homebuyer is required to make a monthly payment based on a percentage of income. The minimum required monthly payment is equal to the administration charge. The administration charge is the amount budgeted per-unit per-month for operating expenses of the recipient. The recipient would adjust (increase or decrease) the administration charge yearly (if necessary) to ensure that adequate funds were received for its operating expense. Based upon the fact that the operating expenses should equal the administration charge and the recipient is required to use the administration charge to pay for the operating expenses of the project, no net income should ever be generated from the administration of the Mutual Help Program. Any amount paid by the homebuyer over the administration charge is credited to the homebuyer's monthly equity account and is used to purchase the unit. These payments are not considered program income. However, should any reserves (administration charges which are in excess of operating expenses) be accumulated by the recipient from the Mutual Help Program, these reserves would be considered program income.

When IHBG assistance is used for rehabilitation of a 1937 Housing Act rental unit, the amount of any income to the recipient from such a unit that is attributable to the use of IHBG assistance is related to the cost of rehabilitation. Again to simplify administration and tracking of funds, a surrogate will be used to represent the cost of rehabilitation or capital expenses for a unit which amounts to substantial rehabilitation or reconstruction. Once total IHBG funds spent for rehabilitation/capital expenditures for the 1937 Act unit meets or exceeds 40% of the dwelling construction and equipment cost (DC&E) effective the date of the enactment of NAHASDA (10/01/1997) for the specific type and size of unit, all the income from the unit is program income. The 40% threshold is only a concept for accounting for program income and will have no affect in determining what is eligible Formula Current Assisted Stock under the IHBG formula.

The DC&E amounts and 40% of DC&E amounts for each Indian tribe with 1937 Housing Act units in effect October 1, 1997, are set forth in the Appendix. DC&E costs include all construction costs of an individual dwelling within five feet of the foundation. Excluded from the DC&E are any administrative, planning, financing, site acquisition, site development more than five feet from the foundation, and utility development or connection costs. DC&E amounts are based on a moderately designed house or multi-family structure and were determined by averaging the current construction costs, as listed in not less than two nationally recognized residential construction cost indices, for publicly bid construction of a good and sound quality.

EXAMPLE: Forty percent of the DC&E for a specific unit type and size for the recipient effective on October 1, 1997, is $25,000. The recipient spent $15,000 of IHBG funds for rehabilitation of such a low-rent 1937 Housing Act unit last program year and will complete the rehabilitation work this program year with $15,000 of additional IHBG funds. Because the total amount of IHBG funds for rehabilitation of the unit will exceed $25,000, all future rental income (beginning the program year or month after the expenditure for rehabilitation which brings the total IHBG expenditures to $25,000–depending on whether the recipient chooses to calculate program income from 1937 Act units yearly or monthly) is program income.

In the Mutual Help Program, when IHBG assistance is used for rehabilitation, the same calculation noted above for the rental program would apply. However, the recipient would not realize the program income until the time of conveyance. Therefore, if IHBG funds are used to rehabilitate a Mutual Help unit and the cost meets or exceeds 40% of the DC&E for the specific type and size of unit, the Proceeds of Sale to the recipient at conveyance would be considered program income. If the cost of rehabilitation is less than 40% of DC&E, the Proceeds of Sale at the time of conveyance would not be considered program income and can be used in accordance with Answer 42A in the revision to the Transition Notice published in the Federal Register on April 1, 1999, (64 FR 15778).

EXAMPLE: Forty percent of the DC&E for a specific Mutual Help unit type and size for the recipient effective on October 1, 1997, is $25,000. The recipient spent $15,000 of IHBG funds for rehabilitation of this Mutual Help unit last program year and will complete the rehabilitation work this program year with $15,000 of additional IHBG funds. Because the total amount of IHBG funds for rehabilitation of the unit will exceed $25,000, all Proceeds of Sale for this unit at the time of conveyance are program income. If however, only a total of $15,000 is used for the rehabilitation of the unit, there is no program income and the Proceeds of Sale at the time of conveyance are not affected. These Proceeds of Sale can be used for eligible purposes based Answer 42A in the revision to the Transition Notice published in the Federal Register on April 1, 1999, (64 FR 15788).

Reference: §1000.62(b)

3.5. Program income from activities funded with IHBG and other funds.

If program income is realized from an eligible activity that was funded both with IHBG funds and with other funds, the amount of income to the IHBG program will be based on a percentage calculation that represents the proportional share of IHBG funds provided for the activity generating the program income.

EXAMPLE: If a recipient used $100,000 of Indian Community Development Block Grant (ICDBG) funds to buy land and $300,000 of IHBG funds to construct houses on this land, the money from the sale of the properties to low-income families would be split between the ICDBG and IHBG programs in accordance with the percentage of funding from each program so that one-fourth of the sales proceeds would be ICDBG program income and three-fourths would be IHBG program income. This percentage calculation is used to determine program income no matter if the program income would be less than, equal to, or more than the amount of IHBG funds used for the activity.

Reference: §1000.62(c).

4. Use of Program Income.

The IHBG regulations [§1000.62(b)] and NAHASDA [section 104(a)] permit recipients to retain program income received provided that it is used for affordable housing activities in accordance with section 202 (Eligible Affordable Housing Activities) of NAHASDA. This means that the use of program income is subject to all applicable requirements governing the use of IHBG funds. The receipt and expenditure of program income must be recorded as part of the financial transactions of the IHBG program. It is also required that recipients substantially disburse program income for eligible activities before additional IHBG funds are drawn down from the U.S. Treasury.

Reference: §1000.62(b) & 24 CFR 85.21 as referenced in §1000.26(a)(5).

5. Examples of Determining Program Income.

Example 1: A recipient uses $100,000 of IHBG funds to buy land. The recipient builds low-income rental houses on the land using non-IHBG funds. After the houses are built, is any of the rental income received by the recipient program income?

Answer 1: The rental income received by the recipient was directly generated from the use of IHBG funds which were used to buy the property. The rent is gross income from the rental of real property acquired by the recipient with IHBG funds (§1000.62(a)). "Costs incidental to the generation of such income" (§1000.62(d)) are subtracted from the gross income when determining IHBG program income. Therefore, the costs of operating and maintaining the housing units, and any other costs incidental to generating the income, may be deducted from the gross rental income. In most cases, there will not be any money remaining from gross rental receipts after incidental costs are netted out. If there is any money remaining, the percentage that would be consider IHBG program income would be equal to the ratio of land costs relative to total project costs.

Example 2: A recipient provides $100,000 of IHBG funds to a nonprofit housing organization to acquire undeveloped land to be used for low-income rental housing. After acquisition, the nonprofit sells the land to a private for-profit limited partnership for $40,000, as part of an agreement under which the limited partnership will build low-income rental housing (a Low-Income Housing Tax Credit project) on the land. After the housing is built, will any of the rent constitute program income? If the limited partnership sells the property at the end of the Low-Income Housing Tax Credit compliance period, will any of the sales proceeds be program income? Looking at all of these transactions, is any program income generated?

Answer 2: The initial entity receiving the IHBG assistance –the nonprofit organization-was a subrecipient, the $40,000 received by the nonprofit when it sold the property was directly generated from the use of IHBG funds. The cost incidental to the generation of the income produced from the sale of the land were closing costs which could be subtracted from the $40,000. Any funds remaining once closing costs are subtracted from the $40,000 would be attributable to the IHBG program and would be program income because no other sources of funds besides IHBG funds were used by the nonprofit subrecipient to acquire the property.

Once the land was sold, the limited partnership ultimately received the IHBG assistance. Because the limited partnership is neither the recipient nor a subrecipient, any income it receives cannot, by definition, be program income. However, the nonprofit subrecipient could require the limited partnership to share rental income with the nonprofit as a condition of providing the land write-down to the limited partnership. Under such circumstances, the possibility for program income exists if there was any income remaining after costs incidental to generating the income were netted out.

Because the limited partnership owns the property and is neither a recipient nor subrecipient, when the limited partnership sell the property, the sales proceeds are not program income unless the nonprofit subrecipient required all or part of the sales proceeds to be paid to the nonprofit as a condition of providing the land write-down to the developer.

Example 3: The recipient uses $400,000 of IHBG funds to acquire and renovate a closed school building for use as senior housing with resident services. The building includes a community room for the residents which is occasionally rented for other uses. The services include dining services and recreational and social activities. None of these activities receive IHBG assistance. Which of the following are potential sources of program income?

- Proceeds from fees charged for the dining services. The proceeds are used to pay for the food and the salaries of the food workers.
- Fees charged for certain senior citizen activities to help cover the cost of those activities.
- Fees charged to private groups for use of the community room for private functions occasionally held there.

Answer 3: In the first case, the funds from the fees charged for dining services are not "directly generated" from the use of IHBG funds. Instead, they are generated from the dining services which are not paid with IHBG funds. Hence, these fees are not program income.

In the second case, the funds from the fees for the activities are also not "directly generated" from the use or rental of the building, but rather to pay for senior citizen activities. Again, there is no program income.

In the third case, these funds are "directly generated" from the rental of the real property acquired and rehabilitated with IHBG funds. Because costs incidental to the generation of real property rehabilitated with IHBG funds can be netted out from gross income, it is unlikely that, when operating and maintenance expenses and other incidental costs are subtracted from gross income, any income would remain. (§1000.62(d)) Any income remaining after incidental costs are netted out would belong to the IHBG program since the example lists only one source of funds used to acquire and rehabilitate the property.

Example 4: A recipient enters into a contract with a bank to provide financing for the rehabilitation of single-family owner-occupied housing. A revolving fund is established with IHBG program income in the amount of $100,000. The funds in the revolving fund are used by the bank to provide low-interest supplemental loans to low-income families who also borrow bank (non-IHBG) funds. The repayment of the IHBG supplemental loans will be deposited in the revolving fund and would be used to make additional supplemental rehabilitation loans. Which of the following are sources of program income?

- Payments of principal and interest on the supplemental loans made with IHBG program income?
- Payments of principal and interest on the primary loans made with bank (non-IHBG) funds?
- Interest earned on funds in the revolving fund account established with the IHBG program income?
- Proceeds from the sale of a house rehabilitated using the bank (non-IHBG) funded loan and the IHBG-funded supplemental loan?

Answer 4: The payments of principal and interest on the IHBG-funded supplemental loans are received by the recipient, though its contractor, the bank. The money is "directly generated" from the use of IHBG funds which are being provided for rehabilitation assistance. If IHBG funds provided a loan covering 100% of the costs of the rehabilitation, all of the loan repayments would belong to the IHBG program. However, because IHBG funds only partially assisted the rehabilitation activity, only the supplemental loan repayments are program income.

Payments of principal and interest on primary loans made with bank (non-IHBG) funds are owed directly to the bank. These funds are not generated from the use of IHBG funds. Hence, the primary loan repayments are not program income.

Interest earned on funds in the revolving fund account established with the IHBG program income is received by the recipient because the funds are administered the bank, which is acting in the capacity of a contractor. The money is "directly generated" from the use of IHBG funds.

In the last case, what if the homeowner sell his house which was rehabilitated with the bank and IHBG loan funds? The sale proceeds are not income to the IHBG program because the homeowner is not the recipient, subrecipient, or a contractor who is administering part of the recipient's IHBG program.

6. Administrative Requirements for Program Income Pursuant to §1000.26 and applicable provisions of 24 CFR Part 85

6.1. Financial Management Systems.

All IHBG program income that is received and expended must be recorded as part of the financial transactions of the grant program. The "Administrative Requirements for Grants and Cooperative Agreements to State, Local and Federally Recognized Indian Tribal Governments" (24 CFR Part 85) establish minimum standards for financial management systems in §85.20(b). These standards require recipients' accounting records to contain information which adequately identifies the source and application of funds provided for any IHBG-assisted activity. The financial reporting must be structured to allow for accurate, current, and complete disclosure of the financial results of IHBG-assisted activities.

6.2. Safekeeping and Documentation

Section 85.20(b)(3) requires recipients to maintain adequate control for all grant and subgrant cash, real and personal property and other assets. In addition to other internal controls discussed above, the recipient must adequately secure all documents pertaining to loans and other assets that generate program income. For example, loans and security documents held by the recipient should be stored in a fireproof safe. The recipient must also take care to ensure that mortgages are properly recorded, Uniform Commercial Code (UCC) Financing Statements are promptly filed, etc.

6.3. Program Income Included as Part of Financial Transactions of the IHBG Program

To ensure that all IHBG program income is properly recorded and expended, there must first be in place an accounting system that will allow this to be done in an accurate and timely manner. The majority of recipients have established automated data processing systems to maintain information on financial transactions. Some recipients also may maintain records in addition to the automated system. Whether manual or computer-based, it is important that the accounting system:

- Protects against unauthorized access and modification.
- Traces financial transactions step-by-step from initiation to resulting financial statements.
- Conforms with legal requirements.
- Produces sufficient documentation to comply with appropriate requirements and reports.

The recipient's IHBG staff need to ensure that an adequate system for initially accounting for receipt of program income, e.g., for loan payments that may be mailed in, is in place and functioning. Separation of duties or functions is important to ensure that opportunities for fraud or abuse are minimized (e.g., the person receiving the payment should not be the same person that accounts for it). Recipients should have clear policies that result in prompt deposit of program income and that prohibit opportunities for such income to be held before it is entered into the official accounting system.

Recipients must also ensure that program income received by any of their subrecipients is adequately and appropriately accounted for and expended. To do so, recipients will need to track closely program income received and retained by these entities. This can be done through periodic reports from the subrecipient and the monitoring of subrecipient activities as required by §1000.502(a); program income reported must be reconciled periodically with subrecipients' records (e.g., through on-site review and audit, if required).

6.4. Tracking Loan Payments.

Many recipients carry out activities such as rehabilitation that involve repayment of loans. In some instances, loans are made on a deferred payment basis, i.e. not payable unless a property is sold. Whether loan accounts are maintained by the recipient, a subrecipient, a private financial institution or some other entity, a permanent loan account record must be maintained for each loan that is made. Recipients can develop or allow other entities to develop the type of system that will maintain these records provided the system can produce detailed information on:

- All transactions that affect the loan balance (e.g., the amount and due date of each payment, when payments are received, how payments are applied).

- Financial information on the loan (e.g., the latest outstanding balances for principal, escrow deposits, advances, unapplied payments, loan status as to delinquency or default).

If a loan is a deferred payment loan, the records should include information that reflects the terms of the deferral to ensure that the dates of future repayments, if any, are clearly indicated.

6.5. Tracking Sales of Real Property.

Recipients' record-keeping systems should identify all properties acquired or owned and rehabilitated by the recipient with IHBG funds. Such record-keeping is essential to ensure that, if and when such properties are sold, the proceeds are treated as program income

6.6. Tracking Sales of Equipment and Supplies.

Pursuant to §1000.26(a)(8) and (9), §85.32 and §85.33 set forth the procedures that recipients must comply with regarding equipment and supplies. "Equipment" is defined as "tangible, non-expendable, personal property having a useful life of more than one year and an acquisition cost of $5,000 or more per unit. A recipient may use its own definition of equipment provided that such definition would at least include all equipment defined above."

Property records to be maintained by the recipient must include:

- Description of the property.
- Serial number or other identification number.
- Source of the property.
- Name of the title holder.
- Acquisition date.
- Cost of the property.

- Percentage of IHBG participation in the cost of the property.
- Location, use and condition of the property.
- Any ultimate disposition data including the date of disposal and sale price of the property.

Proceeds for any equipment or supplies sold that was originally purchased with IHBG funds is program income (if applicable, prorated to reflect the percentage of IHBG funds used).

Should you have questions regarding accounting for program income under NAHASDA, please contact your local Area Office of Native American Programs.

/s/

Harold Lucas
Assistant Secretary
for Public and Indian Housing

Attachments