COMMUNITY
PLANNING
&
DEVELOPMENT

HOME and NSP

A Guide for Successfully and Effectively Combining Funding Sources

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Contents

Introduction

Purpose of this Guidebook

HOME and NSP provides technical guidance to States and local jurisdictions on how to use U.S. Department of Housing and Urban Development (HUD) funding from the HOME Investment Partnerships Program (the HOME Program) and the Neighborhood Stabilization Program (NSP). This guidebook highlights the differences between the two programs, and provides instruction on how to successfully implement activities and projects that use both sources of funds while remaining in compliance with the Federal requirements of each program.

Reasons to Combine HOME and NSP

Grantees should invest their HOME and NSP funds strategically in order to maximize the impact of their investments. For instance, a jurisdiction may choose to use NSP funds to acquire and rehabilitate foreclosed upon homes and residential properties in a target neighborhood, and use HOME funds to assist existing homeowners in rehabilitating their homes in the same neighborhood. In some instances, however, grantees may choose to combine the funding sources either into a single project (such as the rehabilitation of a foreclosed substandard home in a neighborhood), or for a single program (such as a down payment assistance program).

Grantees may choose to combine funds for a number of reasons, for instance:

- To stretch scarce resources
- To address a range of eligible projects and costs to target local housing needs
- To develop mixed-income properties
- To reach diverse clientele with same program activity (such as low- and middle-income residents).

When combining the two sources of funds, grantees must comply with the requirements of ***both*** programs. Generally, this can be achieved by complying with the most restrictive requirement.

Background on HOME and NSP

HOME and NSP originate from different legislative histories and program purposes; therefore, each program can be used in different ways to address a variety of housing conditions or problems. The HOME Program was created to address the growing affordable housing crisis in America in the early 1990s. Its purpose is to increase the supply of affordable housing for low-and very low-income households by providing jurisdictions with a dedicated funding stream to undertake four key affordable housing activities.

The U.S. Congress created NSP in 2008 for the purpose of stabilizing communities that have suffered from foreclosures and abandonment. All five eligible NSP activities are connected to this primary focus.

As of this writing, Congress has appropriated NSP funds in three rounds, known as NSP1, NSP2, and NSP3. With each funding round, Congress and HUD have made a limited number of changes to NSP requirements; however, the primary purpose of stabilizing communities remains unchanged.

Important Guidebook Terminology

This guidebook uses the term ***NSP*** to refer to all three NSP programs. The guidebook specifies the funding round (NSP1, NSP2, or NSP3) only when the requirements differ.

The guidebook uses the term ***grantee*** to refer to the State or local government agency that receives a direct allocation of either HOME and/or NSP funds. It uses the term “participating jurisdiction” or “PJ” to specifically refer to HOME direct funding recipients.

Who Should Read This Guidebook?

HOME and NSP program managers and staff should refer to this guidebook if they are considering combining these two funding sources.

How is the Guidebook Organized?

This guidebook has the following chapters:

Chapter 1, Overview of HOME and NSP, reviews the overall purposes of the HOME Program and NSP and identifies some of the similarities and differences in the key requirements of each program, including eligible and ineligible activities and income targeting.

Chapter 2, Key Program Management Issues, describes the administrative requirements of the two programs. This chapter discusses methods to distribute funds; deadlines for using, committing, and disbursing funds; administrative costs; determining level of investment; match; program income; recordkeeping; and reporting.

Chapter 3, Homebuyer Activities Using HOME and NSP, provides detailed guidance on how to administer a homebuyer program using both HOME and NSP funds. This chapter addresses the HOME and NSP requirements for development-based programs (where funding is provided to developers to acquire, rehabilitate, and/or newly construct for-sale housing), and for programs that provide direct homebuyer assistance (such as down payment and closing cost assistance programs, or mortgage lending programs).

Chapter 4, Opportunities for Rental Development with HOME and NSP, provides detailed guidance on how to administer rental housing programs using both HOME and NSP funds. This chapter discusses a range of rental development approaches, financing methods, property eligibility, property standards, and continued affordability upon project completion.

Chapter 5, Applicability of Cross-Cutting Federal Requirements to HOME and NSP, provides a brief overview of the cross-cutting Federal requirements that apply to any project or activity funded with HOME and NSP and identifies where these Federal requirements differ between the two programs.

For More Information

For more information and program administration guidance, go to:

- The *HOME Program* website at www.hud.gov/homeprogram/ and the HOME TA website at www.hometa.info
- The *NSP Resource Exchange* at www.hud.gov/nspta

Chapter 1: Overview of HOME and NSP

This chapter provides background on the HOME Investment Partnerships (HOME) Program and the Neighborhood Stabilization Program (NSP). The chapter explains how and when the two programs might be used together, describes what activities HOME and NSP funds can be used for and who can be served with these sources, and summarizes the major regulatory differences between the programs.

Purpose and Legislative Background of the HOME and NSP

HOME and NSP originate with different legislative histories and program purposes. As a housing block grant, the HOME Program provides considerable flexibility to its participating States and localities to determine the best way to use the funds to address a range of housing needs. NSP, on the other hand, provides targeted funds for neighborhood stabilization in communities with high rates of abandoned and foreclosed properties. Each program can be used in different ways to address a variety of housing conditions or problems.

HOME Program

Created by the National Affordable Housing Act of 1990 (NAHA), the HOME Program is the largest Federal block grant available to communities to create affordable housing. The purposes of the HOME Program are to:

- Increase the supply of decent, affordable housing to low- and very low-income households
- Expand the capacity of nonprofit housing providers
- Strengthen the ability of State and local governments to provide housing
- Leverage private sector participation.

Every year, the U.S. Department of Housing and Urban Development (HUD) determines the amount of HOME funds that States and local governments—known as HOME Participating Jurisdictions (PJs)—are eligible to receive, using a formula designed to reflect relative housing need. After money has been set aside for America's insular areas[1] and for nationwide HUD technical assistance, the remaining funds are divided between States (40 percent) and units of general local government (60 percent). In FY 2010, Congress authorized approximately $1.825 billion in HOME funds.

Neighborhood Stabilization Program

NSP was established for the purpose of providing emergency assistance to stabilize communities with high rates of abandoned and foreclosed homes, and to assist households whose annual incomes are up to 120 percent of the area median income (AMI). At this writing, the U.S. Congress has appropriated three rounds of NSP funding:

- **NSP1.** Under this first round of NSP funding, NSP1 provided $3.92 billion to State and local governments on a formula basis. NSP1 was established by Section 2301(b) of the Housing and Economic Recovery Act of 2008 (Pub. L.110–289, approved July 30, 2008), also known as HERA. HERA created NSP and is the basis for subsequent NSP funding rounds.
- **NSP2.** Under this second round of NSP funding, NSP2 was authorized under the American Recovery and Reinvestment Act of 2009, (Pub. L. 111–5, approved February 17, 2009), also

1 This includes American Samoa, Guam, Northern Mariana Islands, and the U.S. Virgin Islands.

referred to as ARRA or “the Recovery Act.” $1.93 billion in NSP2 funds were made available on a competitive basis to states, local governments, nonprofits, and consortia of nonprofit entities.

- **NSP 3.** Under this third round of NSP funding, an additional $1 billion was made available on a formula basis to State and local governments. NSP3 was authorized by Section 1497 of the Wall Street Reform and Consumer Protection Act of 2010 (Pub. L. 111–203, approved July 21, 2010), also known as the “Dodd-Frank Act.”

All three rounds of funding are collectively referred to as NSP. Generally, the requirements governing the use of NSP funds are substantially the same for each funding round. However, where there are differences in the requirements among funding rounds, the differences are noted in this guidebook.

The authorizing legislation for NSP states that NSP funds are considered Community Development Block Grant (CDBG) funds, authorized under the Housing and Community Development Act of 1974 (HCD Act), as amended (42 U.S.C. 5301 *et seq.*). This means the CDBG requirements generally govern the use of NSP funds. However, where NSP and CDBG requirements conflict, the NSP requirements take precedence. Note, in a number of regulatory areas, State grantees must adhere to the entitlement program CDBG regulations rather than the State-specific regulations. Further, State NSP grantees may carry out activities directly or through nonprofit and for-profit entities, and/or through units of local government. States are also permitted to provide NSP funding for activities in CDBG entitlement areas, including in jurisdictions that receive their own allocations of NSP funding.

Where to Find HOME and NSP Implementing Regulations

- **HOME.** 24 CFR Part 92.

  A copy of the regulations and detailed information on the HOME Program are available on the HOME Program website at www.hud.gov/homeprogram/.
- **NSP.**
  - **NSP1.** *Federal Register* Notice, October 6, 2008 provides the regulatory framework for NSP. Amendments made to HERA by ARRA are implemented in “the Bridge Notice,” *Federal Register* Notice, June 19, 2009. Changes to the NSP1 funding reallocation process are implemented in the *Federal Register* Notice, August 23, 2010.
  - **NSP2.** The Notice of Funding Availability for NSP2 was issued in the *Federal Register* on May 4, 2009. It provides the regulatory requirements for NSP2. Three corrections to this NOFA were issued on June 11, 2009, November 9, 2009, and January 21, 2010.
  - **NSP3.** *Federal Register* Notice October 19, 2010 makes available NSP3 funding and provides unified regulatory requirements for NSP1 and NSP3.

  A copy of all applicable *Federal Register* Notices and detailed information on the Neighborhood Stabilization Program can be found at the *NSP Resource Exchange* at www.hud.gov/nspta.
- **CDBG.** 24 CFR Part 570.

  A copy of the regulations and detailed information on the CDBG program are available at http://www.hud.gov/offices/cpd/communitydevelopment/programs/

Using HOME and NSP Together

Grantees generally fund distinct housing activities with a single funding source (either HOME or NSP). Given HOME and NSP’s different program purposes and requirements, this approach enables the grantee to target a variety of housing and community development needs in the jurisdiction and facilitates program administration.

The grantee's decision to fund projects with these two different funding sources often results from one of two key differences in the programs (both discussed in detail in the next two sections of this chapter, *Selecting NSP and HOME Eligible Activities* and *Income Targeting*):

- **Eligible Activities.** The range of housing activities that a grantee can undertake with NSP funds is more limited than with HOME funds, because NSP funds are highly targeted to neighborhoods that suffer from high rates of foreclosures and abandonment. HOME funds are more flexible by definition; these are housing block grant funds designed to address a wide range of housing needs, jurisdiction-wide. It is important for the grantee to understand the eligible properties and the eligible activities under each program in order to make good choices about the best way to use each source of funds.
- **Income Targeting.** The clientele served by these two funding sources is also different, although there is some overlap. The HOME Program is designed to increase the supply of affordable housing for low- and very low-income persons. NSP, on the other hand, with its focus on neighborhood stabilization, provides the grantee greater flexibility to serve higher income households — up to middle-income.

HOME and NSP funds can also be combined effectively. There may be good reasons for a grantee to combine HOME and NSP funds to address certain housing and neighborhood stabilization needs, such as:

- **Investing in a single project to stretch scarce resources.** This might be desirable in complex or large projects where the financial needs of the project exceed the HOME per unit subsidy limits.
- **Investing in a single program activity to reach a diverse clientele.** For instance, a grantee might provide homebuyer assistance funds to low-income households with HOME funds and to middle-income households with NSP funds.
- **Investing in a single project to pay for eligible project costs in a strategic way** for each funding source. For example, in the case of a project in an active housing market, where acquisition costs are high, a grantee may want to use HOME funds to acquire a property (since there is no purchase price discount requirement and it can pay full cost) and use NSP funds for rehabilitation costs.
- **Investing in a single neighborhood for a variety of eligible rental and homebuyer projects to increase its impact in the neighborhood.** For instance, a grantee might want to use NSP funds to acquire and rehabilitate foreclosed and abandoned properties in a neighborhood, and use HOME funds to administer a homeowner rehabilitation program in the same neighborhood.

> ***Basic Strategies for Using HOME and NSP Together***
>
> There are many ways to use HOME and NSP together in a single project or neighborhood:
>
> - Use NSP funds for acquisition and/or rehabilitation and use HOME for direct assistance to low-income homebuyers.
> - Use NSP funds for acquisition/demolition of foreclosed units that are blighted and use HOME for new construction of units for resale to low-income buyers.
> - Use NSP for acquisition and use HOME for rehabilitation of multifamily or scattered-site rental units.
> - Use NSP and HOME together for new construction of demolished/vacant units.
> - In mixed-income projects, use HOME for units serving families with incomes below 80 percent of the area median income and use NSP to serve families with incomes between 81-120 percent of area median income.

Selecting NSP and HOME Eligible Activities

Grantees are able to use both HOME and NSP funds only in certain types of projects. Foremost, **only housing activities** can be funded with both HOME and NSP assistance, since HOME funds can only be used for activities that result in affordable housing. Among housing activities, NSP is highly targeted to those properties and activities that will best promote neighborhood stabilization. Further, projects funded with NSP funds must meet a CDBG national objective. Prior to committing HOME or NSP funds, grantees need to ensure that planned activities and properties are eligible under the planned funding program(s).

NSP Eligible Uses and Activities

In selecting an NSP-eligible project, the grantee must consider:

- **Area of greatest need.** Grantees can only undertake NSP activities in their areas of greatest need (as measured by actual and expected percentage of home foreclosures and percentage of homes financed by subprime mortgages). Grantees define the boundaries of the areas of greatest need within their action plans.
- **NSP eligible use.** HERA authorized five eligible uses of NSP funds. These eligible uses are a function of both the type of activity (rehabilitation, demolition, etc.) and the type of property that will be used (foreclosed, abandoned, etc.).
- **Related CDBG eligible activities.** Because NSP is considered CDBG funding, the NSP eligible uses must also correlate with one or more of the CDBG eligible activities. Exhibit 1-1 identifies the NSP eligible uses and the corresponding CDBG eligible activities. In addition, the project must meet a CDBG national objective. These are explained in the following subsection, *Meeting a National Objective with NSP Funds*.
- **Property eligibility.** For each eligible NSP activity, only certain types of properties are eligible. Exhibit 1-2 defines the eligible properties for each NSP activity, and defines each of the key terms.

Exhibit 1-1: NSP Eligible Uses and Related CDBG Eligible Activities

	NSP Eligible Use	Related CDBG Eligible Activities
A.	Financing mechanisms for purchase and redevelopment of ***foreclosed*** upon homes and residential properties for low- and moderate-income homebuyers (such as soft-second loans, loan loss reserves, and shared equity loans)	▪ Activity delivery costs ▪ Financing to carry out one of the other NSP eligible uses listed below
B.	Purchase and rehabilitate homes and residential properties that have been ***abandoned*** or ***foreclosed*** upon in order to sell, , rent, or redevelop such homes and properties	▪ Acquisition ▪ Disposition ▪ Relocation ▪ Direct homeownership assistance ▪ Rehabilitation ▪ Preservation, including counseling
C.	Establish and operate land banks for homes that have been ***foreclosed*** upon. Land banks: ▪ Are operated by public or nonprofit entities ▪ Operate in a defined area ▪ Must have a plan that enables re-use of the property within 10 years	▪ Acquisition ▪ Disposition
D.	Demolish ***blighted*** structures	▪ Clearance Note: ***Only*** blighted properties may be demolished with NSP funds. In addition, under NSP2 and NSP3, the grantee can use only up to 10% of its funds for demolition, unless a greater amount is approved by HUD.
E.	Redevelop ***demolished*** *or* ***vacant*** properties	▪ Acquisition ▪ Disposition ▪ Public facilities and improvements ▪ Public services for housing counseling (limited to potential purchasers or tenants of the redeveloped properties) ▪ Relocation ▪ Rehabilitation or preservation ▪ Direct homeownership assistance ▪ Activities by community-based development organizations (CBDOs) ▪ New housing construction (allowed only under NSP) Note: Under NSP2 and NSP3, all redevelopment activities must be for housing.

Exhibit 1-2: NSP Definitions of Eligible Property Types

Property Type	Definition
Foreclosed upon **(Eligible Uses A, B, and C)**	A home or residential property where any of the following conditions apply: (a) The property's current delinquency status is at least 60 days delinquent under the Mortgage Bankers of America delinquency calculation and the owner has been notified. (b) The property owner is 90 days or more delinquent on tax payments. (c) Under State, local, or tribal law, foreclosure proceedings have been initiated or completed. (d) Foreclosure proceedings have been completed and title has been transferred to an intermediary aggregator or servicer that is not an NSP grantee, contractor, subrecipient, developer, or end user.
Abandoned **(Eligible Use B)**	A home or residential property where any of these conditions apply: (a) Mortgage, tribal leasehold, or tax payments are at least 90 days delinquent. (b) A code enforcement inspection has determined that the property is not habitable and the owner has taken no corrective actions within 90 days of notification of the deficiencies. (c) The property is subject to a court-ordered receivership or nuisance abatement related to abandonment pursuant to State or local law. (d) The property otherwise meets a State definition of an abandoned home or residential property.
Blighted **(Eligible Use D)**	A structure is blighted when it exhibits objectively determinable signs of deterioration sufficient to constitute a threat to human health, safety, and public welfare. Grantees define blight further in their action plans.
Demolished **(Eligible Use E)**	A property is demolished when it was once developed, but the structure(s) have been removed.
Vacant **(Eligible Use E)**	A property is vacant if it is zoned residential and was once developed. This includes vacant land, as well as vacant buildings. This also includes vacant land that has infrastructure development only, and previously undeveloped land that is zoned residential, such as infill or incomplete subdivisions. However, this does not include green space or farmland that has never been developed.

Relationship between NSP Eligible Uses, Activities, and Property Requirements

Some additional clarifications about property and activity eligibility:

- **The NSP-eligible activities are tied to NSP-eligible properties.** For instance, demolition is an eligible activity only if it is undertaken on blighted structures (eligible property). When a grantee wants to use NSP funding for several activities on a single project, then the property requirements must be met for each different eligible activity. Consider the scenario where the grantee wants to acquire and demolish a 10-unit rental property and then newly construct 10 units of affordable housing:
  - If the property is vacant, the grantee can use NSP to fund the property's acquisition, construction, and resale under Eligible Use E.

- If the property is abandoned or foreclosed upon, the grantee can use NSP to fund the acquisition, rehabilitation, and resale under Eligible Use B.
- If the property is blighted, the grantee can use NSP funds for the demolition under Eligible Use D. Once it is demolished, the property meets the definition of vacant and new units can be constructed under Eligible Use E.
- If the property is not blighted, the grantee cannot use NSP funds for the demolition.

- **Properties must be located in the grantee's area of greatest need,** as defined in its action plan. However, NSP 1 and NSP3 grantees may undertake a limited number of units that are located outside of established target areas if the units are located in adjacent neighborhoods and are reasonably related to addressing the overall foreclosure and abandonment problem in the community. NSP2 grantees must always submit an amendment to HUD to undertake an activity in a new target area. Since NSP2 funds were awarded competitively, a change in a grantee's target area could potentially affect a rating factor.
- **Homes and residential properties can be used under Eligible Uses A and B.** This includes vacant land that is zoned as residential and multifamily properties.
- **Only foreclosed upon homes can be land banked (Eligible Use C)**.
- **Any property (residential or nonresidential) can be used under Eligible Uses D (demolition) and E (redevelopment),** as long as the property is located in an area of greatest need and meets a national objective. Under NSP2 and NSP3, these properties must be redeveloped for housing. Under NSP1, these properties can also be redeveloped for public facilities or improvements that benefit the target area.
- **Properties that meet the definition of abandoned or vacant and also meet the definition of foreclosed must be treated as foreclosed.** This means that the properties must be appraised, and they must be acquired at a discount. The appraisal and discount requirements are discussed in Chapter 2, in the subsection entitled *NSP Purchase Price Discount*.
- **Properties that are acquired through a short sale are generally considered foreclosed.** A short sale involves a sale of real property in which a lender agrees to accept the proceeds of the sale in satisfaction of an outstanding mortgage loan when the sale amount is less than the amount the borrower owes on the loan. (Note, this may not release the mortgagor from all other obligations.)

For more information on property eligibility, see *NSP Policy Alert: Guidance on the Impact of New Definitions for NSP-Eligible Properties*, available on the *NSP Resource Exchange* at http://hudnsphelp.info/index.cfm?do=viewResource&ResourceID=484.

Meeting a National Objective with NSP Funds

All NSP activities must meet a CDBG national objective, in accordance with NSP requirements. Grantees must qualify NSP activities under the low- and moderate-income national objective under CDBG. The prevention/elimination of slums and blighted conditions or urgent need national objectives cannot be used. Under the low- and moderate-income national objective, 100 percent of NSP-assisted activities must benefit LMMI persons using one of the following categories:

- **Housing activities (LMMH).** A housing activity is an activity undertaken for the purpose of providing or improving permanent residential structures that, upon completion, are occupied by LMMI households. (For properties with more than one unit, the grantee has some options about how to achieve this. These options explored in Chapters 3 and 4, which are related to homebuyer and rental housing, respectively.) In accordance with CDBG requirements, housing assistance activities (such as rehabilitation or homebuyer assistance) must be categorized under the housing activity, and may not be categorized under any of the other activities listed below. Thus, the majority of NSP activities fall under the LMMH national objective. In addition, only activities that meet the requirements of this category count toward the NSP low-income set-aside requirement. (The low-income set-aside requirement is discussed later in this chapter.)

- **Area benefit activities (LMMA).** An area benefit activity must benefit all residents in a particular area (i.e., the service area) where at least 51 percent of the residents are LMMI persons. The service area must be primarily residential and the activity must meet the identified needs of LMMI persons. Under NSP, the grantee can meet this national objective with either demolition (Eligible Use D) or land banking (Eligible Use C), under certain circumstances:
  - Land banking activities must involve acquisition and maintenance, demolition, or redevelopment that provides an area benefit.
  - Stand-alone demolition of a blighted structure that either (1) poses a very serious public health and safety risk ***to the LMMI area***, or (2) is undertaken in concert with a coordinated program of redevelopment (rehabilitation, new construction, and/or other improvements in a target area which is expected to improve the area). Note, NSP2 and NSP3 demolition costs are subject to a 10 percent cap (unless HUD has approved an exception).
  - In general, demolition and land banking activities are considered interim uses, and the national objective should be based on the reuse of the site. Eligible end uses include housing, sale or donation of property to LMMI neighbors for side lots, donation of property to community garden groups, etc.
- **Limited clientele (LMMC).** Limited clientele activities benefit a limited number of people and are eligible under only NSP1, as long as at least 51 percent of those served are LMMI persons. This category should be used for public facilities projects under Eligible Use E. For instance, it can be used for special needs projects that are not permanent housing, such as homeless shelters or group homes. Note, since redevelopment under NSP2 and NSP3 can only be used for housing, and homeless shelters and group homes are considered public facilities under CDBG, these are not eligible activities under NSP2 and NSP3.

> HERA supersedes the CDBG's income targeting requirements and permits grantees to assist households whose income is at or below 120 percent of area median income. HUD retains the use and definition of the terms "low-income" and "moderate-income" households, in accordance with the CDBG program, and (for NSP) refers to the households whose incomes are between 80 and 120 percent of area median income as "middle-income." Thus, the assisted households under NSP are referred to as low-, moderate-, or middle-income, or LMMI.

NSP grantees who are not familiar with the CDBG eligible activities and national objectives should refer to the CDBG *Program Guide to National Objectives and Eligible Activities for the Entitlement Program*, available at www.hud.gov/offices/cpd/communitydevelopment/library/deskguid.cfm

HOME Eligible Activities

Given the broader program purposes of the HOME Program, it follows that HOME offers grantees more options than NSP for how funds can be used. In concert with NSP, it provides grantees opportunities to combine approaches to leverage greater impact in their target areas.

HOME Program funds can be used to support four general affordable housing activities for low- and very low-income households:

- **Homeowner rehabilitation.** PJs provide HOME assistance to existing owner-occupants to finance the repair, rehabilitation, or reconstruction of their homes.
- **Homebuyer activities.** PJs finance the acquisition and/or rehabilitation, reconstruction, or new construction of homes for homebuyers with HOME funds.
- **Rental housing.** PJs finance the acquisition and/or rehabilitation, new construction, or reconstruction of affordable rental housing.
- **Tenant-based rental assistance (TBRA).** PJs provide HOME funds to tenants for rent, security deposits, and/or utility deposits. Note, grantees can provide utility deposit assistance only in conjunction with monthly rental or security deposit assistance.

Generally, HOME funds can be used for the following costs as long as they support the affordable housing activities identified above:

- **New construction** of rental or ownership housing. This includes any project that involves the addition of dwelling units outside the existing walls of a structure.
- **Rehabilitation.** The alteration, improvement, or modification of an existing structure. This includes moving an existing structure to a foundation constructed with HOME funds, and/or adding rooms outside the existing walls of a structure. Note, adding a housing unit is considered new construction.
- **Reconstruction** or rebuilding of a structure on the same lot where housing is standing at the time of project commitment. This may include building a new foundation or repairing an existing foundation. For reconstruction, the number of rooms in a structure may change, but the number of units in a structure may not. Reconstruction also includes replacing a substandard manufactured house with a new manufactured house.
- **Conversion** of an existing structure from another use to affordable residential housing. This is usually classified as rehabilitation. If conversion involves adding units beyond the walls of an existing structure, the entire project is new construction. Conversion of a structure to commercial use is not eligible under HOME.
- **Onsite improvements** that are consistent with improvements to surrounding standard projects and new, off-site utility connections to an adjacent street.
- **Acquisition of existing standard property or substandard property** in need of rehabilitation.
- **Acquisition of vacant land,** if construction on the HOME project begins within 12 months of purchase. (Land banking is prohibited.)
- **Demolition,** if construction on the HOME project begins within 12 months of demolition.
- **Relocation costs,** including permanent and temporary relocation assistance related to a HOME project. Note that the Uniform Relocation Act (URA) applies to HOME, although it does not apply to homeownership activities that are undertaken with FY04-FY07 American Dream Downpayment Initiative (ADDI) funds.
- **Refinancing existing debt** on single family, owner-occupied properties in connection with HOME-funded rehabilitation when the property meets certain conditions imposed by HUD.
- **Capitalization of project reserves** for the initial rent-up period, up to 18 months.

- **Project-related soft costs** that are reasonable and necessary, such as:
  - Finance-related costs
  - Architectural, engineering, and related professional services
  - Tenant and homebuyer counseling, provided the recipient of counseling ultimately becomes the tenant or owner of a HOME-assisted unit
  - Project audit costs
  - Affirmative marketing and fair housing services to prospective tenants or owners of a HOME-assisted project
  - PJ staff costs directly related to HOME-assisted projects (not including TBRA).

Ineligible Activities and Costs

Both HOME and NSP legislation and regulations prohibit certain activities and costs. These are summarized in Exhibit 1-3.

Exhibit 1-3: HOME and NSP Ineligible Activities and Costs

HOME Ineligible Activities and Costs	NSP Ineligible Activities and Costs
▪ Non-housing activities ▪ Operating subsidies ▪ Project-based rental assistance (however, project-based assistance from another source may be used in a HOME-assisted unit when HOME funds are used for other eligible costs) ▪ Project reserve accounts (except for initial operating deficit reserves) ▪ Certain mandated existing rental assistance programs (such as Housing Choice Voucher Program) ▪ Match for other Federal programs ▪ Development, operations, or modernization of public housing ▪ Payment of delinquent taxes, fees, or charges on properties to be assisted with HOME funds ▪ Properties receiving assistance under certain programs that are no longer funded by HUD [Prepayment of Low-Income Housing Mortgages, the Low-Income Housing Preservation and Resident Homeownership Act (LIHPRHA), or the Emergency Low-Income Housing Preservation Act (ELIHPA)] ▪ Properties that have previously received HOME assistance and are still in the period of affordability, unless they are within the 12 months following project completion, with exceptions for the provision of TBRA and direct assistance to homebuyers ▪ Acquisition of PJ-owned property, unless the property is specifically acquired with PJ funds for a HOME project and HOME funds are used to reimburse the PJ	▪ Foreclosure prevention activities (expressly prohibited by HERA) ▪ Demolition of non-blighted structures, except as integral part of reconstruction or new construction ▪ Acquisition of property or structures that are not abandoned, foreclosed, or vacant ▪ Acquisition costs for units already owned by the grantee (for example, the grantee cannot provide assistance to a homebuyer to purchase a tax-foreclosed unit from itself. However, the grantee can pay for reasonable title transfer costs for such a purchase.) ▪ Acquisition, rehabilitation, or construction of buildings for the general conduct of government (e.g., city hall) ▪ General government expenses ▪ Political activities ▪ Purchase of construction equipment or furnishings and personal property (except under certain limited circumstances) ▪ Operating and maintenance expenses (of public facilities, improvements, and services), except for those associated with public service activities, interim assistance, and office space for program staff employed in carrying out the NSP program ▪ Income payments

Income Targeting

HOME and NSP have different income targeting requirements, and the grantee must comply with the most restrictive requirements in any project that uses both funding sources. In general, the HOME income targeting requirements are more restrictive. Housing that is HOME-assisted must be occupied by households whose annual gross income is at or below 80 percent of area median income; while NSP may serve households that have higher incomes (at or below 120 percent of the area median income). However, both programs have additional income targeting requirements that may apply: HOME rental housing has even deeper income targeting requirements, and 25 percent of NSP funds must benefit households with incomes at or below 50 percent of the area median income. Therefore, the income targeting requirements of any specific project may vary depending on certain project elements. This section describes the general income targeting rules for HOME and NSP, including the NSP low-income set-aside requirement, and provides guidance on how to determine household income under both programs.   Chapters 3 and 4 provide detailed guidance on how to reconcile the income targeting requirements of HOME and NSP in homebuyer and rental activities, respectively.

HOME Income Targeting

All beneficiaries of HOME funds—homebuyers, homeowners, and tenants—must be low-income or very low-income.

- A ***low-income*** household has an annual gross income that does not exceed 80 percent of area median income, as adjusted by household size.
- A ***very low-income*** household has an annual gross income that does not exceed 50 percent of area median income, as adjusted by household size.

HUD establishes HOME income limits for different localities and adjusts them for household size, from one to eight persons. HUD issues the HOME income limits annually, and makes them available at www.hud.gov/offices/cpd/affordablehousing/programs/home/limits/income.

HOME rental activities are subject to additional income targeting requirements:

- **Program rule.** For all the PJ's rental activities (including all the PJ's TBRA and rental development activities combined), initially, 90 percent of household occupants must have annual gross incomes that are at or below 60 percent of area median income.
- **Project rule.** For rental projects with five or more HOME-assisted units, 20 percent of those units must be rented to households with annual gross incomes that are at or below 50 percent of area median income, at the Low HOME rent. This rule applies throughout the affordability period.

Chapter 4 discusses these requirements and HOME rents in more detail.

NSP Income Targeting

Under NSP, grantees can serve households with gross annual incomes that are at or below 120 percent of the area median income. In addition, however, a minimum of 25 percent of all NSP funds (including program income generated that year) must be expended for projects benefiting households with annual incomes at or below 50 percent of area median income, known as very low-income households. This requirement is referred to as the "low-income targeting" or "low-income set-aside" requirement.

Grantees can invest in rental or homeownership housing to satisfy the low-income targeting requirement, using any NSP-eligible property.[2] The occupant of the assisted unit must be income-eligible upon initial occupancy and throughout the affordability period. The unit must count as ***permanent*** housing. Under CDBG rules, and therefore NSP rules, temporary housing (such as homeless shelters and group homes) are public facilities, not permanent housing. Therefore, these expenditures cannot count toward the low-income set-aside. Under NSP1, expenditures for these types of projects may be eligible under Eligible Use E (redevelopment), but the expenditures do not count toward the set-aside.

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2 Initially, HERA restricted the use of the low-income set-aside funds to the purchase and redevelopment of abandoned and foreclosed homes or residential properties only. This restriction was rescinded by the Dodd-Frank Act, effective July 21, 2010 (the date of passage). This means grantees can now use any NSP-eligible property type to meet its low-income set-aside requirement, including vacant properties that are not abandoned or foreclosed, or commercial properties that are converted to housing for income-eligible individuals and families. The Dodd-Frank amendment applies to NSP3 and any unobligated NSP1 and NSP2 funds.

However, under NSP2 and NSP3, redevelopment can be done only for housing; and therefore these public facilities are not an eligible use. If a grantee defines assisted living and transitional housing projects as permanent housing in their programs, these may be eligible under NSP1, NSP2, and NSP3. In these cases, expenditures for these activities would be considered housing activities, and therefore would qualify for the 25 percent low-income targeting set-aside.

Determining the Low-Income Set-Aside Amount

The amount of the low-income set-aside is 25 percent of the annual grant amount, including 25 percent of the program income that is generated in the year.

The low-income set-aside is calculated based on expenditures and not households. This means that if a grantee has a mixed-income project where only some units are occupied by very low-income households, only the expenditures for those units would count toward the set-aside.

- For example, assume that a grantee spends $1,000,000 of NSP funds on a 10-unit project in which all units were acquired with NSP funds. Of the 10 units, six rent to households with incomes between 80 to 120 percent of area median income, and four rent to households with incomes at or below 50 percent of area median income. Since only 40 percent of the units rent to very low-income households, only 40 percent of the NSP expenditure counts toward the 25 percent very low-income targeting rule.

The grantee must satisfy the low-income set-aside requirement program-wide, not project by project. This means that the grantee might have some projects with no very low-income units and some projects composed entirely of very low-income units.

HUD will verify that the grantee has planned activities to meet this set-aside requirement upon review and approval of the action plan substantial amendment or abbreviated plan. Prior to and at grant closeout, HUD will also verify that the grantee has complied with this provision to ensure that 25 percent of grant funds have been expended to house very low-income households.

Income Eligibility and Verification

The grantee must determine a household's income-eligibility prior to providing assistance. The income determination process is nearly the same for HOME and NSP:

A household's income-eligibility is determined based on its annual income. Annual income is the gross amount of income anticipated to be earned by all adults in the household during the 12 months following the effective date of the determination.

To calculate a household's annual income in order to determine its income-eligibility, the grantee chooses from three definitions of income:

- **Part 5 (Section 8) annual gross income.** The grantee uses the Part 5 definition of annual income.
- **IRS adjusted gross income.** The grantee uses the calculation for "adjusted gross income" outlined in the Federal income tax IRS Form 1040.
- **U.S. Census long form annual income.** The grantee uses the definition that is used in the U.S. Census long form for the most recent decennial Census.

Note that State NSP grantees may choose to use one of these three definitions, or they can choose their own definition of income. HUD gives maximum feasible deference to the State's choice of an income definition.

Under both HOME and NSP, the income targeting requirements remain in place throughout the affordability period. For rental housing, the program requirements differ slightly:

- Under HOME, PJs are required to verify tenant incomes on an annual basis throughout the affordability period to determine that the occupants of HOME-assisted housing are low- and very low-income. If the tenant's income increases and the tenant is no longer income-eligible, the property owner must take certain steps to restore compliance in the property.
- Under NSP, the grantee must verify the occupant's income-eligibility prior to occupancy, and at unit turnover during the affordability period.

Summary of Other Key HOME and NSP Requirements

There are number of other key requirements that impact how NSP and HOME funds can be invested to foster HUD's commitment to long-term affordable housing, housing quality, and reasonable costs. These key requirements are summarized below. These requirements are explained in greater detail in the subsequent chapters of this guidebook.

- **Key partners.** HOME and NSP grantees generally work with a number of other partners, including nonprofit and for-profit developers, and private lenders. At least 15 percent of the annual HOME allocation must be invested in housing that is owned, developed, or sponsored by special nonprofits called ***community housing development organizations***. NSP does not have a comparable requirement.
- **Subrecipients and developers.** There are some differences between HOME and NSP's characterization of whether certain public and private nonprofit organizations are considered subrecipients or developers under each program. These designations have implications for how the entities are procured, what kinds of fees they can receive, and what uniform administrative requirements may apply. This issue is explained in detail in Chapter 2.
- **Administrative costs.** HOME and NSP each permit the grantee to spend up to 10 percent of its annual allocation, plus 10 percent of its program income, for eligible administrative and planning costs.
- **Commitment and expenditure deadlines.** NSP funds are subject to more restrictive use and expenditure deadlines than HOME: All NSP1 funds must be expended within four years and NSP2 and 3 within three years; and all HOME funds within five. The grantee should consider project timelines when making funding selections and commitments for each funding source. When using both NSP and HOME in a single project, the grantee may want to consider using NSP funds for costs that are incurred first.
- **Match.** HOME PJs must contribute at least 25 cents for every $1 of HOME funds expended for project costs per program year. NSP has no match requirement but does encourage leveraging. When combining funds in a project, only the HOME funds must be matched; however, NSP funds cannot be the match source.
- **Property value /sales price limits.** Certain restrictions on property purchase price/value under both programs might impact program design or property selection:

  - Properties used for HOME-assisted homebuyer housing must not have an acquisition price or after-rehabilitation value that exceeds 95 percent of area median purchase price.
  - Foreclosed properties that are acquired with NSP funds must be acquired at a discount that is at least one percent (1%) below current fair market value. The grantee may want to consider using HOME funds to acquire properties that cannot be purchased at a discount, and use NSP funds for rehabilitation costs, as necessary.
- **Amount of investment.** HOME imposes a minimum and maximum per unit subsidy limit (an average of $1,000 per unit and the 221(d)(3) limit, respectively). NSP does not impose subsidy limits. HOME also requires grantees to conduct a subsidy layering analysis when combining public sources to ensure that only the amount of public funds needed is invested. Note, HOME and NSP can be used to pay only reasonable eligible costs; further, grantees must ensure that there is no undue enrichment to developers.
- **Rents.** Both HOME and NSP require the grantee to ensure that rental housing is affordable to income-eligible renters. HOME imposes High and Low HOME Rents for low- and very low-income occupants, respectively. These are updated annually by HUD and issued by area and bedroom size. Under NSP, the grantee has the flexibility to adopt its own definition of "affordable rents." When combining HOME and NSP in a project, the grantee should consider adopting the HOME rents for administrative ease.
- **Unit quality.** Both the HOME and NSP programs require grantees to adhere to property standards to ensure assisted properties are decent and safe. HOME imposes specific standards based on the HOME activity undertaken. NSP grantees have some flexibility to choose applicable rehabilitation standards. NSP2 and 3-assisted gut rehabilitation and new constructed housing is also subject to certain green building standards.
- **Long-term affordability.** Properties assisted with HOME and NSP must remain affordable to income-eligible households for some period of time. Exhibit 1-4 summarizes the requirements for each program.

Exhibit 1-4: Summary of Long-Term Affordability Requirements for HOME and NSP

	NSP	HOME
Rental Housing	▪ Rents must remain restricted at affordable levels during affordability period. ▪ Rental units must be occupied by income-eligible households. ▪ Grantee defines affordability and establishes rent levels.	Same as NSP, plus: ▪ Properties must be inspected periodically to ensure compliance with housing quality standards. ▪ HUD defines affordability and issues HOME rent levels (High and Low HOME rents) annually.
Homebuyer housing	▪ Grantee permitted to define affordability and determine how to ensure continued affordability. Can adopt HOME requirements as minimum level of affordability.	PJ must do one of the following: ▪ Restrict resale of assisted properties to income-eligible households at an affordable sales price. ▪ Recapture the initial HOME investment and reinvest it in another affordable unit.

- **Program income.** The grantee should consider program designs that generate program income as a way to stretch scarce HOME and NSP resources. With a few exceptions, gross income that is received by the grantee or a subrecipient is generally treated as program income under both programs. Grantees can permit subrecipients to retain program income. Program income must be reinvested in HOME- or NSP-eligible activities.

Chapter 2: Key Program Management Issues

This chapter reviews the HOME and NSP requirements related to program administration. It covers methods of distributing funds, timeliness of funds commitment and disbursement, administrative cost requirements, determining the appropriate level of investments, match requirements, and rules governing the use and tracking of program income.

Methods of Distributing Funds

Before committing NSP or HOME funds to a project, the grantee should:

- Determine the best ways to invest funds to address the jurisdiction's housing needs
- Identify eligible housing partners that are most likely to use the funds successfully to meet the housing needs
- Develop a project selection process to secure a housing partner.

Distribution to Address Housing Needs

Jurisdictions articulate their plans and priorities for investing HUD Community Planning and Development funds (including HOME, CDBG, and NSP, among others) in their consolidated plans and annual action plans. Development of these plans involves collecting data, making program decisions, sharing a written plan with the public for comment, and securing HUD approval. Jurisdictions cannot fund programs or activities that are not identified in the consolidated plan and action plan without amending the action plan.

At this writing, NSP grantees have submitted action plan amendments to specify how their NSP funds will be used. HERA requires NSP grantees to target NSP funds to areas with the greatest need. This means that grantees must use NSP to focus on areas in the jurisdiction with the greatest percentage of home foreclosures, highest percentage of homes financed by a subprime mortgage-related loan, and/or that are most likely to face a significant rise in the rate of home foreclosures.

HERA also specifies that the grantees must consider investing in "metropolitan areas, metropolitan cities, urban areas, rural areas, low- and moderate-income areas." Therefore, State grantees may distribute funds within any jurisdiction within the State that has the greatest need, even if that jurisdiction receives a direct formula allocation of funds from HUD. This requirement supersedes the State CDBG Program requirement that prohibits States from distributing CDBG funds to entitlement communities and Tribes.

Eligible Housing Partners

The key partners in the HOME and NSP programs include:

- **PJ.** Any State, local government, or consortium that has been designated by HUD to administer HOME program funds.
- **NSP Grantee.** A State or local government that receives a direct allocation of NSP funds. In addition, for NSP2, any nonprofit organization or consortium of nonprofit organizations that receives a direct allocation of NSP2 funds from HUD.
- **State Recipient or Unit of General Local Government (UGLG)/ Subrecipient.** Under the HOME Program, a State recipient is a local town, county, or village that manages a program on behalf of

a State PJ. The CDBG program uses the term “unit of general local government” to refer to the community funded by a State CDBG grantee to undertake eligible CDBG activities. A unit of local government is a town, county, or village. Under NSP, when a State provides NSP funds to a UGLG, the UGLG is a subrecipient.

- **Nonprofit organization.** A nonprofit organization can be involved in HOME or NSP in a number of ways, including as a subrecipient, developer, owner, sponsor, community-based development organization, and/or community housing development organization. In addition, under NSP2, a nonprofit organization may be a grantee. Any single nonprofit organization may be involved in different projects or programs in one or more of these capacities.
- **Subrecipient.** Whether an entity is a subrecipient or not depends on a number of factors, including the type of entity, the activity the entity undertakes, and whether the grantee has selected or procured that entity. There are also differences based on the funding source.
  - NSP adopts the first sentence of the CDBG definition of subrecipient found at 24 CFR 570.500(c): “Subrecipient means a public or private nonprofit agency, authority, or organization, or a for-profit entity authorized under 570.201(o), receiving CDBG funds from the recipient or another subrecipient to undertake activities eligible for such assistance under subpart C of [the CDBG rule]. “
  - HOME defines subrecipient at 24 CFR 92.2 as “. . . a public agency or nonprofit organization selected by the participating jurisdiction to administer all or a portion of the participating jurisdiction’s HOME program. A public agency or nonprofit organization that receives HOME funds solely as a developer or owner of housing is not a subrecipient. . . .”
  - Under both NSP and HOME, a subrecipient is an external public agency or nonprofit organization that administers all or part of the HOME or NSP program on behalf of the grantee (or another subrecipient, under NSP). For instance, under both programs, a nonprofit organization that administers a homebuyer assistance program is a subrecipient.
  - Under HOME, it is primarily the entity’s function/role that dictates whether it is a subrecipient. Under NSP, the type of entity must also be considered. For instance, under NSP, a grantee has the discretion to designate a ***private nonprofit*** that is doing construction work as a developer or a subrecipient; however, it must designate a ***governmental entity*** (such as a public housing authority or redevelopment authority) as a subrecipient. Under HOME, when an external public agency or nonprofit organization receives HOME funds solely as developer, owner, or sponsor of housing; the PJ cannot designate it as a subrecipient. For instance, consider a nonprofit organization that acquires and rehabilitates property for rental housing. This nonprofit is always considered a developer under HOME, but the grantee could choose to designate it as a developer or a subrecipient under NSP.
  - If an entity is considered a subrecipient under either program, the same subrecipient rules apply to that entity.

> **Exhibit 2-1** compares when an entity is a subrecipient and when it is a developer for NSP and HOME.
>
> **Exhibit 2-2** summarizes the key rules that differ for subrecipients and developers. These requirements are described in detail in Chapter 5.

- **Community Housing Development Organization (CHDO).** A CHDO is a private, nonprofit organization that meets a series of qualifications prescribed in the HOME regulation at 24 CFR 92.2. PJs evaluate organizations’ qualifications and designate them as CHDOs. Each PJ must use a minimum of 15 percent of its annual allocation for housing that is owned, developed, or sponsored by CHDOs. A CHDO also may be involved in the HOME Program as a subrecipient, if it implements or administers all or part of the PJ's HOME program, but the use of HOME funds in this capacity is not counted towards the 15 percent CHDO set-aside.

  - The term "CHDO" is not used in NSP. However, an organization that qualifies as a CHDO under the HOME Program may participate in NSP. It may be considered either a nonprofit subrecipient or developer, depending upon how it is selected, what activity it undertakes, and the grantee's designation, per Exhibit 2-1.

- **Community-based Development Organization (CBDO).** A CBDO is an organization that undertakes CDBG-funded activities as part of a neighborhood revitalization, energy conservation, or community economic development project. A CBDO can be a nonprofit or for-profit organization, but it cannot be a government entity. Note that the State CDBG Program uses different terminology and has a somewhat broader definition of organizations that undertake these activities than the CDBG Entitlement program. The State CDBG program generally calls these organizations "nonprofit development organizations working under Section 105(a)(15) of the statute." This guide generally refers to this type of organization as a CBDO but States are encouraged to review the *Guide to National Objectives and Eligible Activities for State CDBG Programs* for additional information. This guide is available on the HUD website at www.hud.gov/offices/cpd/communitydevelopment/library/stateguide/.
- **Developer.** Generally speaking, a developer puts together the housing deal. It secures the financing, acquires or controls the property (as applicable), transfers title to a homebuyer (for homebuyer programs), and oversees the development process. For a rental project, upon project completion, the developer may or may not retain ownership of the property. A developer can receive NSP or HOME assistance directly from a grantee or from a subrecipient.
  - Under HOME, individuals and entities that undertake the role and risks of a developer are treated as a developer, regardless of entity type. Nonprofit organizations, for-profit individuals and entities, and external governmental entities that are not the PJ itself (such as redevelopment authorities) can all be developers under HOME.
  - Under NSP, only for-profit or private nonprofit individuals or entities can be developers. In addition, developers can undertake only: (1) acquisition and rehabilitation of homes and residential properties for use or resale as housing, or (2) construction of new housing in connection with redevelopment of demolished or vacant properties. Developer-led rehabilitation for use or resale is undertaken pursuant to 24 CFR 570.202(b)(1) and new construction is undertaken pursuant to 24 CFR 570.204, or the NPS *Federal Register* Notice published on October 6, 2008, as amended. Developers cannot undertake stand-alone acquisition activities or land banking.
  - Under both HOME and NSP, a developer must own or control (through contract with the owner) the property.
  - Under both HOME and NSP, certain rules and requirements that apply to a developer differ from those that apply to a subrecipient. These differences are summarized in Exhibit 2-2.
- **Owner.** An owner is the entity that owns (and, for homebuyer housing , occupies) the property once it has been built, acquired, or rehabilitated. For rental property under HOME and NSP, the owner is responsible for the ongoing compliance of the property.
- **Sponsor.** Under the HOME Program, a sponsor is a nonprofit organization that works with another nonprofit organization to help this other entity to develop housing. Typically, the

sponsor owns the property during the development process and assists with assembling the financing; upon project completion, the sponsor sells its ownership to the second entity that becomes or remains the owner. The difference between a sponsor and a developer is that the sponsor develops the units on behalf of another nonprofit entity whereas the developer typically manages the project (selects site, secures financing, and oversees construction) for its own organization. Sponsor relationships often occur when a specialized nonprofit social services provider wishes to gain development experience. The term “sponsor” is not used in NSP.

- **Property manager.** The property manager of rental housing generally oversees the maintenance and marketing of units, and maintains documentation to demonstrate compliance with income and affordability requirements. An owner might carry out property management functions itself, or it may select another organization to do so once the property is complete. The property manager may or may not be legally or financially related to the ownership entity.
- **Lender.** Most HOME and NSP projects leverage or involve other financing, from a for-profit lender (such as banks or credit unions), or some other entity such as a foundation or community group. One special type of lender that may participate in either HOME or NSP is the Community Development Financial Institution (CDFI). CDFIs are community-based lenders working to address housing and economic development needs.
- **Contractor.** A range of other entities might work on the HOME or NSP programs, such as architects, planners, construction managers, real estate agents, or consultants. These professionals are generally contractors. Contractors provide goods and services at an agreed upon price and are responsible for specific, well-defined tasks that contribute to the grantee’s overall affordable housing activity, such as consolidated planning. Under both HOME and NSP, grantees and subrecipients must procure contractors competitively, in accordance with the requirements at 24 CFR 85.26.

Tips for Effective Use of Program Partners

- Avoid using too many partners — it can spread the work too thin and make it difficult to monitor progress and compliance.
- Before making funding commitments, evaluate the strengths and weaknesses of program partners, and plan for training and technical assistance that may be needed to build capacity.
- Where the grantee does not have sufficient technical expertise for a planned activity, secure that expertise by contracting out the work or hiring staff with the necessary skills to expedite program implementation.

For more information on when an entity is a developer, subrecipient, or contractors under NSP, see *NSP Policy Alert: Guidance on Developers, Subrecipients, and Contractors*, August 2010, available on the *NSP Resource Exchange* at http://hudnsphelp.info/index.cfm?do=viewResource&ResourceID=720.

In choosing partners, jurisdictions need to ensure that they adhere to the Federal requirements related to conflict of interest. In general, no “covered” person or entity may obtain a financial benefit due to his or her working relationship to the HOME or NSP programs. A covered person is a grantee employee, agent, or officer and their immediate family members and business partners. So, a grantee employee could not form a development firm and then request HOME or NSP assistance to build rental units.

In addition to these requirements, HOME imposes additional conflict of interest requirements related to the occupancy of units. In general, no owner, developer, or sponsor of HOME-assisted housing, including their officers, employees, agents, consultants, or elected officials may occupy a HOME-assisted unit. Note that there are exceptions for owner-occupied rehabilitation and rental property managers or maintenance workers.

Exhibit 2-1: Developer vs. Subrecipient under NSP and HOME

Activity	NSP	HOME
NONPROFIT ORGANIZATIONS*		
Acquisition and rehabilitation or new construction of rental or homebuyer housing	Developer or subrecipient, at grantee's discretion	Developer
Acquisition only	Subrecipient	Developer
Land banking	Subrecipient	N/A
Homeowner rehabilitation program administration	N/A	Subrecipient
Homebuyer assistance program administration	Subrecipient	Subrecipient
Rental housing program administration (select developers, monitor construction, recruit tenants, etc.)	Subrecipient	Subrecipient
TBRA program administration	N/A	Subrecipient
PUBLIC AGENCY (external)		
Acquisition and rehabilitation or new construction	Subrecipient	Developer
Acquisition only	Subrecipient	Developer
Land banking		
Homebuyer assistance program administration	Subrecipient	Subrecipient
Homeowner rehabilitation program administration	N/A	Subrecipient
Rental housing program administration (select developers, monitor construction, recruit tenants, etc.)	Subrecipient	Subrecipient
TBRA program administration	N/A	Subrecipient
UNIT OF LOCAL GOVERNMENT (receiving State funds)		
All eligible activities	Subrecipient	State recipient
PRIVATE FOR-PROFIT INDIVIDUAL OR ENTITY		
Acquisition and rehabilitation or new construction of rental or homebuyer housing	Developer	Developer
Acquisition only	N/A	Developer
Land banking	N/A	N/A

Activity	NSP	HOME
Homeowner rehabilitation program administration	Contractor**	Contractor**
Homebuyer assistance program administration	Contractor**	Contractor**
Rental housing program administration (select developers, monitor construction, recruit tenants, etc.)	Contractor**	Contractor**
* Developers and subrecipients may be selected by the grantee with or without a competitive procurement process. Many grantees use a qualification process to avoid the appearance of favoritism. **Contractors provide goods and services. Grantees and subrecipients ***must*** use a competitive procurement process that meets the requirements of 24 CFR Part 85 (for governmental entities) or 24 CFR Part 84 (for nonprofit organizations) to select contractors.		

Exhibit 2-2: Applicability of Program Administration Rules to Subrecipients and Developers

Program Administration Rule	Developers	Subrecipients
Cost principles	Not applicable.	Applicable. OMB Circular A-87 (governmental entities) OMB Circular Aj-122 (nonprofit organizations)
Financial management systems and procurement	Generally not applicable, however: CHDOs acting as owner, developer or sponsor (HOME) must meet financial management requirements at 24 CFR 84.21.	Applicable. 24 CFR Part 85 (governmental entities) 24 CFR Part 84 (nonprofit organizations)
Recordkeeping	Applicable. 24 CFR 570.506(h) (NSP) 24 CFR 92.508 (HOME)	Applicable. 24 CFR 570.506(h) (NSP) 24 CFR 92.508 (HOME)
Audit requirements	Not applicable.	Applicable. OMB Circular A-133
Revenues / program income	Not required to return excess revenues. Grantees implement mechanism to prevent undue enrichment (e.g., underwriting guidelines, etc.)	Excess revenues are program income (PI). Subrecipients must return PI or invest in other eligible activities, per direction of grantee.
Administrative and activity delivery costs /developer fee	May receive developer fee, with a reasonable profit margin, to offset these costs. May charge contractor or brokerage fee if	May receive administrative funds (subject to NSP and HOME 10% administrative caps). May receive NSP activity delivery

Program Administration Rule	Developers	Subrecipients
	performing these separate services. May not receive administrative or activity delivery (NSP) funds.	funds for direct costs. May receive funds for indirect costs with approved indirect cost allocation plan. May not receive developer's fee.

Nonprofit Consortia Grantees under NSP2

Under NSP2 only, a nonprofit organization or a consortium of nonprofit organizations may be a grantee that receives a direct allocation of NSP2 funds from HUD. In a consortium, each consortium member is considered to be a part of the grantee organization (a co-grantee of the lead entity). As such, the rules that apply to the nonprofit grantee also apply to each co-grantee (that is, each nonprofit consortium member):

- The co-grantee may retain program income, if this was the agreement among all the consortium members, rather than paying it back to the lead organization. However, the retained program income must be used before additional NSP2 funds are drawn down and must be used for eligible NSP2 activities in accordance with the NSP2 rules and the consortium's approved NSP2 application.
- The co-grantee cannot be a developer and thus cannot earn a developer fee because grantees cannot be developers.
- The co-grantee can have all NSP-eligible and related costs paid by NSP funds, including administrative and program delivery costs and indirect costs established in a cost allocation plan, if negotiated in the consortium agreement.
- The co-grantee can select subrecipients and developers without a competitive procurement process.
- The co-grantee must follow the procurement requirements at 24 CFR Part 84 whenever it purchases goods and services. If it (or its subrecipients) directly hire construction contractors or other service providers, it must follow Part 84 and undertake competitive selection.

Eligible Housing Partners for States

Under both HOME and NSP, grantees have considerable flexibility in how they choose to distribute funds to implement their action plans. Both programs permit States and units of local governments to spend funds directly to carry out eligible activities, or to work through housing partners.

For State grantees, NSP differs in this regard from the State CDBG Program. In the State CDBG program, States must distribute CDBG funds to units of local government in non-entitlement communities to carry out CDBG activities. In the NSP program, however, States are permitted to select projects, expend funds directly on projects, and implement eligible activities anywhere within the State. For States that choose to carry out NSP activities directly, HUD has imposed the following additional requirements:

1. The State must carry out reviews and audits and establish remedies for noncompliance for any subrecipients, public agencies, or units of general local government, as appropriate.
2. The State is subject to the change of use of real property requirements, as outlined in 24 CFR 570.489(j).

3. The State is required to maintain records to facilitate review and audit by HUD of the State's administration of NSP funds.
4. HUD retains the right to determine whether the State has failed to carry out its certification in compliance with applicable program requirements.
5. The State must submit the certification and request for release of funds to HUD for approval for any activities it carries out directly, in accordance with environmental review requirements at 24 CFR 58.4.

Project Selection Process

Grantees have many options in terms of how to select projects. In general, grantees and subrecipients must select for-profit contractors using a competitive procurement process in accordance with 24 CFR 85.36. However, under both HOME and NSP, the grantee may select subrecipients and nonprofit developers without a formal competitive procurement process.

The grantee should determine the best way to select development partners that are experienced and most likely to succeed, and identify specific projects that are the most likely to move forward in a timely manner and result in housing that meets the jurisdiction's needs. Exhibit 2-3 summarizes the advantages and disadvantages of several common methods for project selection. When combining HOME and NSP funds, grantees must be especially careful to specify the applicable program requirements to potential housing partners to be sure that it receives project proposals that are eligible under both sets of program requirements.

Exhibit 2-3: Project Selection Methods

Type of Process	Advantages	Disadvantages
Formal Process **(e.g., Notice of Funds Availability, Request for Proposals, or Request for Qualifications)**	✓ Requires applicants to provide information necessary to assess organization's capacity and experience (RFQ) or project viability (RFP or NOFA) ✓ Helps to ensure consistency throughout the evaluation process	× Tends to favor more experienced applicants × Requires substantial grantee staff time to ensure consistency throughout the process × Limits applicants to preset timeframes each year
Solicitation of Applications from Targeted Entities	✓ Proactive process that focuses more directly on qualified organizations ✓ May result in less grantee staff time to administer ✓ Grantee is able to target specific nonprofits that might not otherwise participate in program, or that might need capacity-building	× Appearance of a "closed door" × May result in criticism of the grantee selection process × Lesser known or newer organizations may be overlooked

Type of Process	Advantages	Disadvantages
"Open Door" Process	✓ May allow opportunities for jurisdictions to more quickly respond to community needs	× Process is unplanned × May require crucial staff time and effort to respond because applications may not be complete and may come in at any time × May allow the commitment of funds to projects before more qualified applications are received × Tends to result in budget changes and project amendments throughout the year

Timeliness

Both HOME and NSP encourage grantees to use their affordable housing funds expeditiously by imposing use, commitment, and expenditure deadlines, as follows:

Exhibit 2-4: HOME and NSP Commitment, Use, and Expenditure Deadlines

	Commitment/Use of Funds	Expenditure of Funds
HOME (excluding CHDO set-aside funds)	Funds must be committed through legally binding agreement within two years of signing HOME Investment Partnerships Agreement.	Funds must be spent within five years of signing HOME Investment Partnerships Agreement.
HOME CHDO set-aside funds	Funds must be reserved in IDIS for a specific CHDO within two years.	Funds must be spent within five years of signing HOME Investment Partnerships Agreement.
NSP	NSP1's 18-month use (obligation) deadline has passed. NSP2 and NSP3 do not have deadlines for the use or commitment of funds, only for expenditure.	NSP1 funds and NSP1 program income combined must be ***expended*** in an amount equivalent to the NSP grant within four years of grantee's receipt of NSP funds. NSP2 and NSP3 grantees must expend 50% of their allocated funds within two years of the dates the funds are available and 100% of their grants within three years. Like NSP1, the amount of funds awarded plus program income must be expended by the applicable deadlines.

Note that HOME and NSP use slightly different definitions to show that funds have been committed (HOME) or used (NSP):

- Under the HOME Program, funds must be ***committed*** in a legally binding agreement to use the HOME funds for affordable housing, or a specific project, in accordance with the definition of "commitment" provided at 24 CFR 92.2.
- Under NSP1, funds were required to be ***used*** or ***obligated*** within 18 months. This means that funds are expended or that orders have been placed, contracts and subgrants awarded, goods and services received, and/or similar transactions are executed during a given period that will require payment by the grantee during the same or a future period, as defined at 24 CFR 85.3.

The HOME and NSP1, NSP2, and NSP3 expenditure deadlines apply to administrative funds. NSP2, NSP3 and HOME administrative funds are not subject to commitment or use/obligation deadlines. In HOME, the Integrated Disbursement and Information System (IDIS) earmarks these funds so that the commitment deadline does not apply.

Under both programs, program income must be spent before the grantee can request additional cash withdrawals from the U.S. Treasury. Under HOME, these deadlines are assessed by the amount of HOME funds committed and expended, regardless of how much program income has also been generated and spent in the same year. Program income is discussed in more detail later in this chapter.

For both programs, failure to meet these deadlines results in a return of funds to HUD.

Program Administration Tips to Expedite Expenditure of Funds

- Use clearly written policies and procedures and standardized forms to build staff competence, and implement the program consistently.
- Hire or contract out to experts for specific tasks, as needed.
- Build DRGR/IDIS capacity early in the process to ensure sound financial management and reporting.
- Network and share information with other grantees.
- Take the time up-front to design effective programs:
    - Secure market studies to make sure the housing will be marketable and consider end-use of the property.
    - Determine local programmatic goals.
    - Assess honestly whether grantee and partners have capacity and sufficient resources.
- Concentrate investments in a limited number of targeted areas to improve the odds of success.
- Plan in advance how to use program income.

Eligible Costs

A wide variety of costs can be paid for with HOME or NSP funds, including direct and indirect project costs, certain planning and predevelopment costs, and administrative costs.

Direct Project Costs

Direct project costs are those costs tied to delivering eligible housing units. They include hard construction costs, soft costs, and related staffing costs. Eligible direct project costs under HOME and NSP may include:

- Site acquisition
- Labor, materials, and other construction costs
- Energy efficiency improvements
- Utility connections
- Inspection, testing, and abatement of lead-based paint
- Relocation costs for displaced persons, businesses, or farms
- Soft costs such as: financing fees; credit reports; title binders and insurance; surety fees; recordation fees; transaction taxes; legal and accounting fees, including cost certification; appraisals; architectural and engineering fees, including specifications and job progress inspections; environmental reviews; builders' or developers' fees; affirmative marketing
- Accessibility improvements.

Under NSP, eligible activities and costs must also be associated with eligible properties. Each Eligible Use has specific property types with which it may be used. For instance, Eligible Use C (land banking) is limited to foreclosed homes and residential properties.

Note that HOME requires that all units be brought up to code and it has a minimum investment requirement of an average of $1,000 per HOME-assisted unit for the project. So, while accessibility and energy efficiency improvements are eligible costs as a part of construction, usually they are not stand-alone activities because these work items alone do not bring a property up to code. NSP does not have a minimum investment requirement but it also requires that rehabilitation meet applicable local or State codes.

For rental housing, HOME funds can also be used to cover the cost of funding an initial operating deficit reserve (up to 18 months) for new construction and rehabilitation projects.

- This reserve is meant to meet any shortfall in project income during the project rent-up period.
- The reserve can be used only for project operating expenses, scheduled payments to replacement reserves, and debt service.
- The disposition of any remaining funds at the end of the 18-month period should be determined in the agreement between the developer/owner and the PJ. (Reserves remaining at the end of 18 months may be retained for reserves at the PJ's discretion.)
- If the lender requires it, NSP can pay up-front a reasonable deposit for lease-up. In addition, NSP allows a reserve for replacements to be accrued with net income from the property over time.

Administrative and Planning Costs

Under NSP, HUD provides an alternative to the CDBG requirements related to the use of funds for administrative costs which is more consistent with the existing HOME Program requirements. For both the NSP and HOME programs, the grantee (including the State) can use up to ten percent of each year's allocation for reasonable administrative and planning costs. In addition, for each program, up to ten percent of the program income generated in a program year may also be used for administrative and planning costs. HOME and NSP1 administrative costs are not subject to the commitment/use deadlines; however, the expenditure deadlines apply to administrative funds for HOME and all rounds of NSP funding.

Under both programs, eligible administrative and planning costs include expenditures for salaries, wages, and related costs for staff persons responsible for overall program administration. Other planning and administrative costs under both programs might include:

- Goods and services necessary for administration (for example, utilities, office supplies, etc.)
- Administrative services under third party agreements (for example, legal services)
- Program administration costs (such as the costs for administering a tenant-based rental assistance program under HOME)
- Providing public information
- Fair housing activities
- Indirect costs under an indirect cost allocation plan prepared in accordance with applicable Office of Management and Budget (OMB) Circulars A-87 (for public agencies) and A-122 (for nonprofit organizations)
- Preparation of the consolidated plan
- Complying with cross-cutting Federal requirements (discussed in Chapter 5).

Note, there are some differences in the way HOME, NSP, and CDBG Entitlement and CDBG State Programs implement the administrative and planning caps:

- HOME calculates the administrative and planning cap based on each annual allocation amount, plus program income received.
- NSP calculates the administrative and planning cap based on the allocation amount, plus 10 percent of the program income received.
- CDBG Entitlement Program calculates the cap based on the obligation of funds for each 12-month program year.
- CDBG State Program (applicable to NSP State grantees) calculates the cap based on expenditures of funds, as a percentage of each annual grant allocation.
- For more detailed definitions of administrative costs, see 24 CFR 570.205 and 570.206 (CDBG), and 24 CFR 92.207 and 92.208 (HOME).

Activity Delivery Costs

Certain administrative costs (known as “program delivery” or “activity delivery” costs under CDBG) are treated differently under the HOME and NSP programs. Activity delivery costs include specifications, inspections, underwriting, loan processing, and any other staff and contracted costs needed to deliver and oversee an eligible project. These costs are incurred by the grantee (or its State recipient or subrecipient) and are directly related to a specific project.

Under NSP, these types of costs are eligible when needed to deliver an assisted program or project. These costs are covered under the project activity and are not counted toward the administrative cap.

For State grantees, local activity delivery costs can, at the State's option, be classified as administrative or activity delivery costs.

Under HOME, these costs can be charged as project costs (not subject to the administrative cap) only when the cost is directly attributable to a specific HOME project. This means the jurisdiction must track the costs to specific units and must include these costs within the maximum per unit subsidy limit. If the costs cannot be attributed to a specific HOME project, they must be counted as administrative costs, and are subject to the administration cap. Note, NSP does not require this level of address-specific documentation for activity delivery costs.

Note that grantees may elect to use their CDBG funds to pay for administrative or project delivery costs related to providing housing and related services under HOME or NSP, provided that the costs are also CDBG-eligible. These costs might include:

- Housing counseling
- Energy auditing
- Preparation of work specifications
- Loan processing
- Inspections
- Tenant selection
- TBRA management.

However, if the grantee is using NSP funds to serve households whose incomes are between 80 and 120 percent of median income, these households are not considered low- and moderate-income under CDBG and these costs would ***not*** be eligible as a housing activity serving low- and moderate-income households.

Level of Investments

Both HOME and NSP impose certain requirements that impact the level of investment the grantee can make in a project. These include:

- HOME subsidy layering requirement
- HOME minimum and maximum per unit subsidy limits
- NSP purchase price discount for foreclosed properties
- HOME and NSP cost allocation (fair share)
- HOME and NSP cost reasonableness requirements.

Subsidy Layering

For both HOME and NSP, the financial needs of a project are assessed through the grantee's underwriting process. In addition, under HOME, whenever a project combines HOME funds with any other local, State, or Federal assistance (including NSP), the PJ must conduct a subsidy layering review. This review is an evaluation of the project financing in order to ensure that only the amount of public funds necessary are invested in the project. All HOME PJs must establish subsidy layering guidelines for their rental and homebuyer programs to ensure consistency in how this review is done. Each project file must contain the subsidy layering review.

NSP does not impose any equivalent subsidy layering requirement. However, both HOME and NSP require the grantee to ensure that all costs are necessary, appropriate, and reasonable in accordance with the OMB Circular A-87, discussed later in this chapter.

When HOME and NSP are combined in a project, the grantee is required to conduct a formal subsidy layering review in accordance with the HOME requirements and ensure cost reasonableness in accordance with OMB Circular A-87.

Minimum and Maximum per Unit Subsidy Limits

The minimum HOME investment in a project is an average of $1,000 per unit. This is calculated as the average per unit HOME investment across all the HOME-assisted units in single project.

HOME imposes a per unit subsidy limit that is set at the 221(d)(3) limits for the bedroom size in the community. These subsidy limits may be obtained by contacting the HUD Field Office or can be found online on the HOME Program website at www.hud.gov/offices/cpd/affordablehousing/programs/home/limits/subsidylimits.cfm. Generally, these limits are fairly generous.

NSP does not establish a minimum or maximum per unit investment. However, when NSP is used to acquire property, NSP limits the purchase price of foreclosed homes/properties. This purchase price discount is discussed in the following section.

HOME Cost Allocation

HOME funds may pay only the actual costs of HOME-assisted housing. PJs can use one of two methods to determine how to allocate costs to HOME-assisted units:

- If the assisted and non-assisted housing units in a project are comparable (in terms of size, features/amenities, and number of bedrooms), then the PJ can determine the HOME-assisted share of costs by pro-rating the total HOME-eligible development costs such that the proportion of HOME-assisted units to the total number of units equals the proportion of HOME costs to the total eligible development costs. (For example, if 20 percent of the units are HOME-assisted, then 20 percent of the total eligible costs can be paid with HOME funds.)
- If the assisted and non-assisted units in the project are ***not*** comparable, the PJ must allocate the HOME costs on a unit-by-unit basis, charging only actual costs to the HOME Program.
- These cost allocation requirements apply to all properties with multiple units, including rental and homebuyer housing of five or more units, and single family housing that consists of two to four units. Appendix 2 describes and illustrates the HOME cost allocation methodology in detail.

> ***Determining the Amount of the HOME Investment***
>
> The maximum subsidy that can be provided to a HOME project depends on the following four factors:
>
> 1. The proportion of the total project cost that is HOME-eligible, since some planned project costs may not be eligible expenses under the HOME Program
> 2. The total number of HOME-assisted units in the project
> 3. The 221(d)(3) maximum per unit subsidy limit, discussed above
> 4. The financial needs of the project (because HOME projects may not receive more subsidy than is required to make them financially feasible, in accordance with subsidy layering requirements, discussed above).

NSP Cost Allocation Guidance

Under NSP, housing projects must comply with the LMMH national objective. In a multi-unit structure, upon project completion, the grantee has three options to measure benefit:

- It can follow the existing CDBG requirements, wherein 51 percent of the households in an assisted structure must be income-eligible.
- It can adopt the HOME Program cost allocation method, described above and found at 24 CFR 92.205(d). A detailed explanation of the HOME cost allocation methods is provided in Appendix 2 at the end of this chapter.
- It can follow the NSP "pro-rated approach," wherein one or more of the units in a structure must be occupied by income-eligible households, but the remainder of the units may be market rate, provided that the proportion of units occupied by LMMI households to the total number of units is equal to or greater than the proportion of the NSP investment to the total eligible project development costs. (In other words, the proportion of income-eligible units must be at least proportional to the amount of assistance provided.) Units must be comparable in size and finishes. (Note, this approach is similar to the HOME approach where units are comparable; however, HOME also offers a method for cost allocation when the units are not comparable.) For example, consider a ten-unit project that has total eligible development costs of $500,000 and NSP pays for $100,000 (20 percent) of this total cost. The total number of NSP-assisted units must be at least 20 percent of the ten units, or two units.

NSP Purchase Price Discount

> The NSP purchase price discount requirement applies only to the acquisition of foreclosed property. Other properties that are acquired with NSP funds are not subject to the purchase price discount requirement.

NSP limits the purchase price of foreclosed homes/properties. When acquiring foreclosed-upon homes or residential properties with NSP funds, the grantee must purchase the property at the "maximum reasonable discount" from current market value. The NSP discount must be a minimum discount of one percent (1%) below the current market-appraised value for each individual residential property. This cap applies to the purchase price of the foreclosed property when NSP funds are used for acquisition, regardless of who makes the purchase (grantee, subrecipient, homebuyer, developer, etc.), or whether other funds are also used.

For instance, assume that a foreclosed property is appraised at $120,000. A homebuyer will use a combination of NSP funds and a private mortgage to buy the house. The grantee has agreed to provide the homebuyer with up to $50,000 in NSP mortgage financing, with the balance coming from the private mortgage. Even though NSP will not pay for the entire acquisition, since the NSP funds will be used for property acquisition, the cap on maximum purchase price applies. The maximum price that the homebuyer can pay for the home is $118,800 (appraised value of $120,000 minus the one percent discount of $1,200).

Note, if the NSP funding is invested in project costs that are clearly separable from the acquisition, the discount requirement does not apply.

Appraisal Requirements for Determining Purchase Price Discount

Market value must be established by an appraisal for properties valued at more than $25,000. The appraisal must be conducted or updated within 60 days of making a final offer to the owner and must conform to one of the following:

- The appraisal requirements of the Uniform Relocation Act appraisal standards specified at 49 CFR 24.103
- The Uniform Standards of Professional Appraisals Practice (USPAP)
- The appraisal requirements of the Federal Housing Administration (FHA) or government sponsored enterprise (GSE).

Generally, these standards mandate certain qualification criteria for appraisers, including that fee appraisers be State certified or licensed in accordance with FIERREA. Grantees (or their subrecipients and State recipients) must establish minimum qualifications for appraisers based on the nature of the appraisal assignments. They must further develop a scope of work for the appraisal and procure any fee appraisers in accordance with 24 CFR Part 85 (public agencies) or Part 84 (nonprofits) and State and local procurement requirements.

The appraisal must include a number of specific elements, including:

- A description of the physical characteristics of property
- Title information
- Location
- Zoning
- Present use
- At least five year sales history
- Known encumbrances
- Description of approach to value; if more than one is used, a reconciliation of the approaches
- Identification and description of all comparables used
- Statement of value
- Date
- Signature.

For properties whose anticipated value is estimated at $25,000 or less, when the acquisition is voluntary, the market value of the property may be established by a valuation of the property that is based on a review of available data and is made by a person that the grantee determines is qualified to make the valuation.

Additional guidance on the appraisal requirements is posted on the *NSP Resource Exchange* at www.hud.gov/nspta.

Example: Applying the NSP Purchase Price Discount and the HOME Subsidy Limits in a Project

When combining HOME and NSP in a project that involves acquiring a foreclosed property, the grantee must comply with ***both*** the NSP purchase price discount requirement and the HOME maximum per unit subsidy requirement. For example, consider the following project that involves the acquisition and rehabilitation of a foreclosed single family home:

Acquisition, appraised value	$100,000
HOME and NSP-eligible rehabilitation costs	$ 65,000
Maximum HOME subsidy limit (221(d)(3))	$135,000

The grantee has some choices about how it invests its HOME and/or NSP funds:

1. Since NSP does not have a maximum subsidy limit, the grantee can fund this project in its entirety with NSP funds. If it does so, it must comply with the NPS purchase price discount requirement. It can pay no more than $99,000 (1% of $100,000) in acquisition costs. Therefore, the grantee can invest a maximum of $164,000 in NSP funds.
2. Since the HOME maximum per unit subsidy is $135,000, and the total development cost is $165,000, the grantee cannot use HOME funds to fund this project in its entirety. It can maximize its HOME investment and use $135,000 in HOME funds and use NSP funds for gap financing. It can invest up to $30,000 in NSP funds if NSP does not fund any acquisition costs, or $29,000 if NSP funds are used for acquisition costs.
3. The grantee can distribute the project costs between the two programs in a number of other ways, provided that it does not invest more than $135,000 in HOME funds and does not pay more than $99,000 in acquisition costs if NSP funds are invested in the acquisition.

Cost Reasonableness

HOME and NSP grantees must ensure that costs are reasonable, regardless of which entity or program is developing a property, in accordance with OMB Circulars A-87 (for public agencies) and A-122 (for nonprofit organizations). This means that the grantee must have solid underwriting standards and practices for its development activities, to justify its investments. HUD auditors periodically conduct reviews of this issue, and where grantees allow “undue enrichment” to the developer or borrower, the grantee could face expensive findings. These OMB Circulars are discussed in more detail in Chapter 5.

Match

HERA specifically states that there are no matching funds required under NSP. This statutory directive supersedes the State CDBG match requirement for program administration at 24 CFR 570.489(a)(i).

The HOME Program, however, requires that PJs contribute an amount equal to no less than 25 percent of the total HOME funds drawn down for project costs as a permanent contribution to affordable housing. Note, NSP funds are not eligible to be used as match for HOME.

PJs incur a match obligation only for project funds, not for administrative, operating, or capacity building expenditures. Although the obligation is incurred based on per dollar expended in a HOME project, match "credit" can be invested in any HOME-eligible project, whether the project receives HOME funds or not. Match can be contributed in many different forms, including cash; value of waived taxes or fees; value of donated land or property; or donated goods, services, materials, or equipment.

When HOME funds are expended in a project that uses both HOME and NSP funds, the PJ must make a match contribution for the HOME funds expended.

Program Income

Both HOME and NSP have rules governing the use of program income. The following sections define program income and explain its eligible uses.

Definition of Program Income

The definition of program income is any gross revenue received by the PJ or grantee, State recipient (HOME), or subrecipient that is directly generated from the use of program funds (HOME or NSP) or matching contributions (for HOME). If program income is generated by housing that is only partially assisted with HOME or NSP funds or HOME matching funds, the income is prorated to reflect the percentage of program funds used.

Under both HOME and NSP, program income includes, but is not limited to:

- Proceeds from the sale or long-term lease of real property acquired, rehabilitated, or constructed with HOME or NSP funds or HOME matching contributions
- Income from the use or rental of real property owned by a PJ, State recipient, or subrecipient that was acquired, rehabilitated, or constructed with HOME or NSP funds or HOME matching contributions, minus the costs incidental to generating that income
- Under NSP only, the amounts recaptured from the resale of assisted units during the affordability period. Under HOME these amounts are considered to be "recaptured funds," not program income.
- Payments of principal and interest on loans made with HOME, NSP, or HOME matching funds, and proceeds from the sale of loans or obligations secured by loans made with NSP, HOME, or matching contributions.

> Note that program income is received only by PJs, subrecipients, or State recipients. Revenues received by for-profit or nonprofit developers, beyond any negotiated repayments of principal and interest to the grantee, are ***not*** program income and thus not subject to HOME or NSP program income limitations.

Use of Program Income for HOME and NSP

The following requirements guide the use of HOME and NSP program income:

- All program income on hand must be used prior to drawing additional funds from the U.S. Treasury.
- HOME and NSP grantees must use program income for program-eligible activities. This means that NSP program income must be used for NSP-eligible activities that meet a national objective in accordance with NSP requirements, and HOME program income must be used for HOME-eligible activities in accordance with HOME requirements.
- NSP program income is subject to the NSP low-income set-aside requirement.
- Grantees have the option of permitting subrecipients or State recipients to retain program income, for use in program-eligible activities.
- Grantees must have written agreements in place with subrecipients and State recipients that specify whether that entity can retain the program income, and if so, to convey the program income requirements to ensure compliance.
- Grantees are obligated to track their receipt and expenditure of program income.

Tracking Program Income for NSP and HOME

Both HOME and NSP require grantees to track their receipt and expenditure of program income, although how this is done varies somewhat for each program.

Under NSP, program income is tracked in DRGR. The grantee records program income received in the Quarterly Progress Report (QPR) module in the quarter it was received, under the activity in which it was received. Once the QPR is saved (even as a draft QPR), the amount of program income entered is made available to the grantee to draw and it will show in the Drawdown module the next time the grantee creates a voucher. The QPR does not need to be submitted to or approved by HUD for the program income to be made available.

Under HOME, the HOME PJ tracks the receipt and use of program income in the IDIS system. PJs use the IDIS receipt module to show the receipt of program income. Any income on hand should be receipted into IDIS before drawing funds. To report the use of program income, the PJ must first fund the IDIS activity with program income using the Activity Funding module, then use the Drawdown module to create and approve a program income drawdown voucher.

Financial Management Systems

For both HOME and NSP, grantees should ensure that their financial management systems adhere to several key principles:

- Protect funds, property, and other assets against loss or misuse.
- Record receipt and use of funds in order to account for where all funds come from and how all funds are used.
- Record assets and liabilities to account for what is owned and what is owed.
- Retain source documentation to support receipt and use of funds.
- Ensure that fund expenditures are consistent with the budget, as it may have been amended, and are not in violation of any of the restrictions or prohibitions that apply to the Federal assistance.

- Manage cash effectively to avoid unnecessary borrowing costs and to take proper advantage of opportunities to earn interest.
- Ensure that costs are reasonable and properly allocated.
- Report complete and current financial results to permit an accurate assessment of financial results.
- Use audits to strengthen financial management systems.

In addition, grantees should be sure that their subrecipients' and State subrecipients' financial management systems have the following capabilities:

- Accurate, current, and complete disclosure of the financial results of each Federally- sponsored program, including sources and application of funds
- Comparisons of outlays with budgeted amounts for each award
- Sound internal controls over purchases, cash disbursements, and cash receipts, including segregation of duties and proper authorization and approvals of transactions
- Periodic internal and external audits or evaluations
- Record retention policies
- Documentation of accounting policies, particularly those pertaining to cost charging, timesheet preparation, and procurement
- An accounting system that meets the following requirements:
    - Segregation of unallowable costs from allowable costs
    - Segregation of direct from indirect costs
    - Proper assignment and allocation of costs to functional classifications
    - Matching of income and applicable credits with associated expenditures
    - Timely reconciliation of accounts and subsidiary ledgers
    - Time-charging systems that allocate labor costs among program activities and comply with OMB Circular A-87 (public agencies) or A-122 (nonprofit organizations), as applicable
    - Consistency in accounting treatment over time and from one function or award to another
    - Timely and accurate financial reporting
    - Maintenance of proper supporting documentation for all transactions, estimates, and calculations.

Reporting

HOME PJs are required to report on HOME program activities in IDIS. NSP grantees are required to report on NSP program activities in DRGR.

Both IDIS and the DRGR systems allow grantees to request their grant funding from HUD and report on what is accomplished with these funds. In order to obtain funding, each system requires the grantee to provide HUD information about use of funds, funding commitments and disbursements, activity progress, performance goals, program outcomes, and program beneficiaries. Using this information, HUD is able to monitor program progress. Specifically, HUD monitors for anomalies or performance problems that suggest fraud, waste, and abuse of funds; reconciles budgets, obligations, fund draws, and expenditures; calculates applicable administrative limitations and CHDO reservations (HOME);

assesses compliance with income targeting and affordability requirements; and conducts risk analyses to determine its monitoring plan.

To ensure transparency, HUD posts HOME production reports on the HOME Program website at www.hud.gov/homeprogram/ and requires the grantee to post its NSP report on its website for its citizens when it submits the report to HUD.

HUD has imposed key changes to the CDBG reporting requirements for NSP:

- NSP grantees are not required to submit the annual CAPER report on their consolidated plans. Upon approval of their DRGR action plans, grantees can set up specific projects and activities in DRGR and then draw against those approved activities.
- NSP grantees must submit Quarterly Progress Reports (QPRs) in DRGR within 30 days (10 days for NSP2) of each quarter end, throughout the life of the grant. The DRGR requires the grantee to report on each activity for which it has drawn funds.
- The grantee must download its QPR in HTML and post it on its website for citizen review and comment.
- Under NSP2 only, grantees must also report on progress and accomplishments at www.federalreporting.gov/, a centralized government-wide reporting system for all recipients of ARRA funds.
- The regular CDBG performance measurement requirements do not apply to NSP funds. DRGR performance measures fit the NSP activities.

For more information on DRGR, see HUD's DRGR website at www.hud.gov/offices/cpd/communitydevelopment/programs/drsi/drgrs.cfm.

Recordkeeping Systems

Both the HOME and NSP programs have specific requirements regarding records retention. Generally, for both programs, grantees must establish and maintain sufficient records to document that program requirements are met. These records must be retained for the most recent five year period and for five years following the completion or closeout of the program activity. Records may need to be retained for a longer period if there are any unresolved audit findings.

For HOME, certain records that document compliance with requirements that apply throughout an affordability period need to be retained beyond the five years after completion. For instance, general records for a specific rental project should be retained for five years following project completion, but records that document compliance with affordable rents and low-income occupancy requirements must be retained for the most recent five year period, up to five years following the completion of the affordability period.

HOME and NSP grantees should establish their own recordkeeping and record retention policies for their housing partners. These requirements should enable the grantee to meet HUD requirements and maintain complete information about funded projects.

Accurate recordkeeping is crucial to the successful management of HOME- and NSP-funded activities. Insufficient documentation leads to monitoring findings, and these findings are more difficult to resolve if records are missing, inadequate, or inaccurate.

For the HOME Program, the following records must be maintained:

- PJ designation
- Records related to the PJ's administration of the program, including the consolidated plan, action plan, policies and procedures, grant agreement
- Records related to assisted projects such as the agreement, number and type of assisted units, cost allocation analysis (if applicable), subsidy layering (if applicable)
- CHDO records
- Financial records such as draw requests or procurement records
- Beneficiary data (income documentation)
- Records that document compliance with cross-cutting Federal requirements such as equal opportunity and fair housing, and conflict of interest.

For NSP, the following records must be maintained:

- General administrative records
- Appraisal records for all properties
- Address, appraised value, purchase offer amount, discount amount and sale price, if applicable, of each property purchased
- Financial records
- Project/activity records, including documentation on sources and uses of funds for each activity
- Data on demolition and conversion of any low- to moderate-income housing units as required in the alternative requirement to the one-for-one replacement requirement
- Determinations of NSP eligible use determinations, and national objective records
- Income documentation records
- Subrecipient records.

HOME and NSP grantees must provide citizens and other interested parties with reasonable access to records. Access must be consistent with applicable State and local laws regarding privacy and obligations of confidentiality. In addition, HUD and the Comptroller General of the United States, and any of their representatives, have the right to access any records of grantees and subrecipients for auditing, excerpt, or transcript purposes.

Monitoring

HOME and NSP grantees must ensure that program funds are expended in accordance with applicable program requirements. Grantees must review and/or audit their housing partners (subrecipients, procured contractors, and HOME State recipients) to ensure that they also comply with the program requirements, and must take or impose corrective actions as necessary.

For HOME and NSP, the grantee must conduct periodic onsite visits throughout the affordability period to ensure continued compliance with the affordability requirements. For HOME rental projects, property inspections must also be conducted throughout the affordability period to ensure that property standards continue to be met. NSP grantees may impose inspection requirements if desired.

Chapter 3: Homebuyer Activities Using HOME and NSP

Homebuyer housing programs can be an effective means to enhance neighborhood stabilization because they generate decent and safe housing stock for long-term occupancy. Homebuyer assistance programs are an appropriate and eligible use of HOME and/or NSP funds. However, the grantee must reconcile some differences in the requirements for each program when it combines these funding sources.

This chapter discusses how the grantee can combine HOME and NSP to assist homebuyers, including the use of funds for direct assistance to homebuyers and assistance for the development of homebuyer housing. The chapter explains and compares the HOME and NSP rules for methods of assisting buyers (i.e., program design), methods of financing, eligibility of buyers, property eligibility, property standards, and long-term affordability.

Approaches to Creating Homebuyer Housing

Homebuyer programs using HOME and/or NSP funds can be structured in a variety of ways to encourage the acquisition, acquisition and rehabilitation, or the new construction of affordable homes. The two primary approaches to creating homebuyer units are:

- **Homebuyer subsidy approach.** The grantee provides a direct subsidy (typically down payment and closing cost assistance, or a soft second mortgage) to the homebuyer to help him or her afford the new home.
- **Development approach.** The grantee subsidizes the rehabilitation or new construction of affordable homebuyer units. These units are then sold to eligible homebuyers.

Homebuyer Subsidy Approach

HOME Eligible Activity Type: *Homebuyer Housing*

NSP Eligible Uses: *(A) Financing Mechanisms; (B) Purchase and Rehabilitate; or (E) Redevelopment*

The direct homebuyer subsidy approach involves providing funds to a household to enable it to purchase an existing home. Both HOME and NSP can be used to provide direct assistance to homebuyers in a variety of ways:

- Provide down payment and closing cost assistance
- Assist homebuyers to finance the purchase of the home (by providing financing or principal write-downs)
- Use individual development accounts
- Developing lease-purchase programs.

Down Payment and Closing Cost Assistance

One of the most common methods for assisting income-eligible households to purchase a home is to provide the down payment and closing cost assistance. Income-eligible households that are able to afford the monthly cost of homeownership (i.e., mortgage payments, taxes, and insurance) do not always have sufficient funds for the lender's required down payment and/or the various up-front fees and charges that are collectively called "closing costs."

Both HOME and NSP allow for the provision of down payment and closing cost assistance in the form of loan or grant, to eligible homebuyers as follows:

- Under the HOME Program, the provision of down payment and closing cost assistance to qualified low-income buyers is considered an eligible homebuyer activity. This type of assistance is considered direct assistance to acquire a property.
- Under NSP, a grantee can provide direct homebuyer assistance to a LMMI homebuyer for:
  - The purchase of a home or residential property that had been abandoned or foreclosed upon and rehabilitated under Eligible Use B
  - The purchase of a redeveloped or newly constructed property that was vacant or demolished under Eligible Use E. (Note, the property does not need to have been foreclosed or abandoned.)
- The grantee may also use HOME or NSP funds to pay up-front either all or a portion of the mortgage insurance premiums (such as private mortgage insurance, or PMI) for the first year. This lowers the homebuyer's monthly housing costs. Note that subsequent payments of this premium would not be permitted under either program.

Since down payment and closing cost assistance is considered to be "direct homeownership assistance" under the CDBG statute and regulations, the amount of the NSP down payment assistance is capped at 50 percent of what is required by the private lender. Closing cost assistance is not capped.

Additional homebuyer assistance tools – such as principal or interest write-downs – can also be provided under NSP Eligible Use B, as well as under HOME. These forms of assistance are described below.

Homebuyer Financing

There is a wide range of direct and indirect forms of financial assistance to homebuyers to enable them to purchase their homes. The grantee can:

- Act as a lender by providing a first or second mortgage
- Subsidize the financing offered by a private lender, such as an interest or principal write-down
- Create other forms of credit enhancement, such as a loan guarantee or loan loss reserve.

Exhibit 3-1 describes a wide range of homebuyer financing activities, and indicates the HOME and NSP eligibility of the activity.

Exhibit 3-1: Homebuyer Financing Activities and HOME/NSP Eligibility

Homebuyer Financing Activities	Description	HOME-Eligible?	NSP-Eligible?
Direct PJ Lending			
Grants or forgivable loans	Grantee directly lends funds that are not repaid or that are forgiven on a pro-rata or other basis over time. For example, a $20,000 HOME mortgage might be forgiven at $2,000 a year over a 10-year period so long as the low-income household remains in the unit.	Yes	Yes
Amortizing first position loans	Grantee directly lends funds that are typically paid back on a monthly basis, usually with some interest payment. While uncommon, the grantee might provide the first mortgage when no private financing is available. This activity greatly reduces the number of homes that can be assisted, so grantees should use it only as a last resort.	Yes	Yes
Amortizing second or lower position loans	Grantee directly lends funds where there is also non-HOME or non-NSP financing and that other financing has a higher lien position. This typically occurs when there is a private first mortgage and a HOME or NSP second mortgage.	Yes	Yes
Deferred payment loans	Grantee directly lends funds that are not repaid until a specific point in time or activity occurs, such as the subsequent sale of the home.	Yes	Yes
Tools to Make Private Loans More Affordable			
Principal write-downs	Grantee uses HOME or NSP funds to write down the loan amount that a private lender provides. Example: A homebuyer needs $100,000 to buy a home but can only afford the payments on a $60,000 mortgage. The grantee could provide HOME or NSP assistance to the lender to write down the difference. The difference is generally secured by a lien.	Yes	Yes

Homebuyer Financing Activities	Description	HOME-Eligible?	NSP-Eligible?
Interest rate write-downs	Grantee provides assistance to a private lender so that it is able to make a first mortgage to a homebuyer at a lower interest rate. Example: The market interest rate is 7%, but the homebuyer cannot afford the monthly payment at this rate. The grantee provides an interest rate buy-down to the lender so that the effective interest rate is 2% and the buyer can afford the monthly payment. The payment reduction is more typically accomplished using a principal write-down which makes the monthly payment equal to what it would have been with the original principal at a lower interest rate.	Yes	Yes
Loan guarantees	PJ makes a guarantee to the lender establishing that if the homebuyer defaults on the loan, the PJ will repay the lender for a specified portion of the loss. Because the PJ takes on a significant portion of the lender's risk, it is vital that it develop stringent policies and procedures for loan guarantee activities.	Yes	Yes
Private mortgage insurance	Grantee pays insurance premium to a private mortgage insurance company, who makes a loan guarantee to the private lender.	Yes, if paid up-front for first year only	Yes, if paid up-front for first year only
Loan loss reserves	An amount of funds held in a reserve as a percentage of a lender's total loans on the balance sheet. The amount held represents the amount thought to be adequate to cover estimated losses in the loan portfolio.	No	Yes

Under NSP, the homebuyer financing methods described in this subsection can be used for the purchase and redevelopment of foreclosed homes for LMMI homebuyers under Eligible Uses A and B; with abandoned properties under Eligible Use B; and with vacant properties under Eligible Use E.

Individual Development Accounts

Individual development accounts (IDAs) are dedicated savings accounts that provide start-up funds to assist income-eligible residents to purchase a home or start a business.

Both HOME and NSP funds can be used to assist IDAs that are established solely for homeownership assistance purposes to assist income-eligible account holders who are saving to purchase a home.

HOME funds can support IDAs that provide down payment and/or closing cost assistance for low-income buyers. NSP funds can be used in an IDA as Eligible Use A (financing of foreclosed units), Eligible Use B (acquisition and rehabilitation of foreclosed or abandoned properties), or Eligible Use E (redevelopment of vacant properties) as a form of direct homeownership assistance. The activity must meet the LMMH national objective (that is, each assisted household must be low-, moderate-, or middle-income). NSP funds may be deposited in an IDA to capitalize the account or as matching deposits over the course of the household's participation in the program.

IDAs are intended to be an intermediate term approach to saving for homeownership. Given the stringent use and expenditure deadlines of NSP, IDAs may not be the best match with NSP, since it may take two or more years for their value to the buyer to accumulate. However, it may be an effective use of NSP program income earned over time.

For more guidance on using NSP funds to support an IDA, see *Use of Community Development Block Grant (CDBG) Funds to Assist Individual Development Accounts*, HUD Notice CPD 01-12, August 14, 2001. For more guidance on using HOME to support homebuyer IDAs, see *HOMEfires,* Volume 1, Number 8, at www.hud.gov/offices/cpd/affordablehousing/library/homefires/volumes/vol1no8.cfm.

Lease-Purchase Programs

Lease-purchase programs assist income-eligible households to save for the purchase of a rental home during the lease period. Lease-purchase programs are often used in areas with weak sales markets, or where financing for mortgages is limited. The lease period and amount vary by program. Housing counseling and homebuyer education are often an integral part of the lease-purchase program requirements.

Under the HOME Program, lease-purchase is an eligible form of homeownership assistance. HOME requires that the income-eligible tenant purchase the unit within three years of signing a lease-purchase agreement. The household must be income-eligible at the time that the HOME lease-purchase agreement is signed. Tenants can receive HOME TBRA to reside in the lease-purchase unit prior to purchase, and are also eligible to receive HOME-funded homebuyer assistance for the purchase.

In the event that the original tenant-purchaser is unable to purchase the unit, the PJ has a total of 42 months from the date of the project completion to identify and transfer title of the property to another eligible homebuyer. If the property is not transferred to an eligible homebuyer at the end of the 42-month period, it reverts to a HOME rental unit, and is thereafter governed by all applicable HOME rental housing requirements, including the long-term affordability requirements.

Lease-purchase programs are also eligible under NSP:

- To assist a tenant to purchase a foreclosed upon home under Eligible Use A.
- To acquire and/or rehabilitate a foreclosed upon or abandoned property for use in a lease-purchase program under Eligible Use B.
- To operate a land bank and rent/sell the land banked properties to income-eligible households under Eligible Use C.
- To acquire and redevelop vacant property and provide direct homeownership assistance to enable a subsequent income-eligible household to rent/buy the home under Eligible Use E.

NSP uses the same time limits as HOME (three years for the tenant-purchaser to purchase the home, and 42 months for the grantee to transfer the home to another income-eligible buyer if the initial tenant-purchaser is unable to purchase the home. Unlike HOME, NSP funds cannot be used to provide ongoing rental assistance to the tenant-purchaser during the lease period (such as HOME TBRA).

When designing lease-purchase programs, grantees should consider the best ways to use NSP funds, given NSP's tight use and expenditure deadlines. For instance, NSP funds will be spent most quickly if they are invested in the acquisition and/or rehabilitation of the property(ies) that will be leased, rather than as direct homebuyer assistance to the tenant to purchase the unit at the end of the lease period.

When both HOME and NSP are invested in a single lease-purchase project, in the event the initial tenant fails to purchase the property and it reverts to a HOME rental property in accordance with HOME requirements, the rental project continues to be eligible under NSP. The NSP grantee can choose to adopt the HOME requirements to enforce the long-term affordability of the rental unit. Under both programs, it is critical that the tenant be provided a Move In Notice [see 24 CFR 570.606(b)(2)(ii)(B)] that advises him or her that if he or she is unable to meet the eligibility requirements of the lease-purchase program, he or she will not be eligible for relocation assistance under the Uniform Relocation Act or section 104(d).

Buyer-Driven v. Grantee-Driven Homebuyer Program Models

Regardless of whether the grantee provides assistance to the buyer or assistance to the developer, both HOME and NSP can be used to provide homebuyer assistance in a buyer-driven model or a grantee-driven model.

- In a ***buyer-driven model***, administered by the PJ or a subrecipient, the homebuyer is responsible for finding and selecting his or her own home. Under NSP, the homebuyer must find a foreclosed or abandoned unit in the target area and approach the grantee (or its subrecipient) for purchase assistance. The benefits of the buyer-driven model are that the household undertakes the search process itself, which helps ensure that the household buys the type and location of unit that it desires. In addition, this approach may relieve some administrative burden for the grantee. However, it does require a reasonably stable market, with homes and mortgages readily available to buyers.
- In a ***grantee- driven model***, the grantee (or its subrecipient) identifies the home and then offers financing to the selected eligible buyer. The benefit of a grantee-driven model is that it enables to grantee to target specific properties for redevelopment and reuse. Further, it is sometimes easier to administer than the buyer-driven model, given the range of requirements attached to the use of NSP funds such as the location of the property in an area of greatest need, the required URA acquisition notice, the cap on the purchase price, and the need for an appraisal.

Development Approach

HOME Eligible Activity Type: *Homebuyer Housing*

NSP Eligible Uses: *Homeownership Assistance under (B) Purchase and Rehabilitation; or (E) Redevelopment*

Under the development approach to homebuyer assistance, the grantee funds a nonprofit subrecipient or developer or for-profit developer of the housing. The developer purchases sites or units and develops the homes. These units are then sold, often at below market prices, to income-eligible buyers. In some instances the grantee directly develops the housing, but this is not typical. Options for the development of housing include acquisition with rehabilitation or new construction of units. Either option can be carried out on a scattered site basis or in specific neighborhoods or subdivisions.

Acquisition/Rehabilitation

In an acquisition/rehabilitation project, the grantee, a developer, or a subrecipient acquires and renovates an existing property. The home is then sold to an income-eligible homebuyer, typically at a below market price. Both HOME and NSP can be used to acquire existing units, rehabilitate them, and resell them to income-eligible homebuyers. Under NSP, eligible properties must be either foreclosed upon or abandoned (Eligible Use B) or vacant or demolished (Eligible Use E).

Investing in Manufactured Housing Units

Both HOME and NSP funds can be invested in manufactured housing units for homeownership or rental housing; however, slightly different rules apply:

- Under NSP, and in accordance with longstanding CDBG policy, manufactured homes must be defined by State law as real property to be eligible for assistance.
- Under NSP, the grantee can invest in manufactured housing units only if manufactured homes are part of the community's permanent housing stock, in accordance with 24 CFR 570.202.
- Under HOME, at the time of project completion, the manufactured housing must be connected to permanent utility hook-ups.
- HOME requires the manufactured housing to meet the Manufactured Home Construction and Safety Standards established in 24 CFR 3280 and further requires installation to comply with applicable State or local laws or codes (or, in the absence of such laws or codes, it must comply with the manufacturer's written installation instructions). NSP requires the grantee to define and adopt property standards. (NSP property standards are discussed later in this chapter.)
- HOME requires the manufactured housing unit to be located on land that is owned by the owner of the manufactured housing unit, or for which the unit owner has a leasehold interest for at least the duration of the applicable affordability period. NSP imposes no similar requirement; however, the grantee should consider how its affordability requirements will be met if this is not the case.
- Under HOME and NSP, if a grantee acquires a site that has or once had an existing unit, it can replace that unit with a manufactured housing unit as reconstruction, rather than new construction. For HOME, the number of units and tenure type must remain constant.

When HOME and NSP funds are invested in the same manufactured housing project, the most restrictive requirements of the programs must be met.

New Construction

In a new construction project, the developer, grantee, or subrecipient builds new units and then sells these units to low-income homebuyers. The units may be built as scattered sites at infill or other locations or they may be built as a neighborhood (see below). New construction is not typically eligible under CDBG, except in certain limited circumstances. However, NSP allows the new construction of housing under Eligible Use E (redevelopment of demolished or vacant properties). NSP does not require that the grantee work via a community-based development organization (CBDO) to undertake new construction, although it may choose to do so.

For new construction, HOME and NSP can be used to pay for costs that are necessary:

- Acquisition of land
- Construction costs for units

- Demolition of existing structures under HOME or demolition of blighted structures under NSP Eligible Use D (under NSP2 and NSP3 demolition is limited to 10 percent of the grantee's allocation unless part of reconstruction under Eligible Use B or new construction under Eligible Use E, or otherwise approved by HUD)
- Site preparation
- Onsite infrastructure improvements
- Relocation costs
- Making utility connections including off-site utility connections from the property line to the adjacent street.

Neighborhood Development

In a neighborhood development project, the developer purchases a number of properties (for infill development) or a single large parcel and uses that land to develop a number of homes within a neighborhood. The homes that are built in this neighborhood are then sold to income-eligible homebuyers.

NSP, like CDBG, can be used to undertake a wide variety of activities related to targeted neighborhood development in areas of greatest need. Under NSP Eligible Uses B (acquisition and rehabilitation of foreclosed or abandoned units), D (demolition of blighted structures) and E (redevelopment of demolished or vacant properties), the grantee can acquire, demolish, and construct new units in a targeted area or site. In addition, the grantee can use its CDBG funds for related activities such as public services or economic development. The CDBG program provides grantees with regulatory flexibility when using program funds to develop larger-scale neighborhood revitalization activities within areas designated as neighborhood revitalization areas (NRSAs) or community revitalization strategy areas (CRSAs) under the State CDBG Program. Note, however, that this flexibility does not remove the general prohibition on new construction using CDBG funds.

While the HOME Program does not include special provisions for PJs developing new neighborhoods or subdivisions, costs related to the development of newly constructed housing unit(s) are eligible, including onsite infrastructure and off-site utility hook-ups. Note, a subdivision that is developed under common ownership, management, and financing is considered a single project under HOME. Therefore, a substantial amount of infrastructure, including new roads, sidewalks, and utilities, are considered "onsite" in a subdivision that is developed as one project. These costs are eligible, but are subject to the HOME maximum per unit subsidy limits for the PJ. NSP generally views such projects in the same way.

Converting Rental Units to Homeownership Units

In some circumstances, the grantee may want to develop housing units as rental initially, with the intent of converting them to homeownership units in the future. This strategy might make sense in housing markets where homeownership housing demand is low, but is expected to recover in the near future. Under NSP, the grantee is permitted to sell NSP-assisted rental units during the affordability period to income-eligible buyers. (Note, relocation and tenant protection requirements may apply. These are discussed in Chapter 5.) However, HOME-assisted rental units can be sold only to existing tenants during the affordability period, in accordance with 24 CFR 92.255. In either case, if the homebuyer receives additional NSP or HOME assistance, the affordability period would start anew, and would be based on the amount of assistance. If no additional assistance is provided to the buyer, the remaining period of affordability from the initial provision of rental assistance would continue.

Methods of Financing

As discussed above, the grantee generally uses one or more of the following financing methods to support its homebuyer programs:

- Grants
- Deferred-payment loans
- Below market-rate loans
- Loan guarantees
- Loan loss reserves (under NSP/CDBG).

NSP grantees may also draw funds from their NSP letter of credit in a lump sum to establish a rehabilitation fund in one or more private financial institutions for the purpose of financing the rehabilitation of privately-owned properties. The fund may be used in conjunction with various rehabilitation financing techniques, including loans, interest subsidies, loan guarantees, loan reserves, or such other uses as may be approved by HUD consistent with the objectives of NSP. The fund may also be used for making grants, but only for the purpose of leveraging non-CDBG funds for the rehabilitation of the same property. There are specific requirements pertaining to the amount of the lump sum, eligible costs, and terms and conditions that must be in the agreement between the NSP grantee and participating lender. These requirements are found in CDBG regulations at 24 CFR 570.513.

Levels of Investment

The levels of HOME and NSP investment are impacted by a number of rules that include:

- The minimum level of HOME assistance is $1,000 per unit.
- The maximum amount of HOME assistance is capped by the Section 221(d)(3) maximum subsidy limits, as published by HUD.
- NSP does not have minimum or maximum dollar amounts per unit, although other limits apply (below).
- Each project with multiple funding public funding sources is subject to a subsidy layering review in accordance with HOME requirements.
- Projects that contain multiple units (such as in a subdivision) are subject to the NSP and HOME cost allocation rules to ensure that each funding source pays only its fair share of the total eligible development costs.
- When NSP funds are used to acquire a foreclosed property, the purchase price must be at least one percent less than the appraised value of the property.

Chapter 2 reviews each of these rules in detail.

Eligible Properties

Grantees are able to use a number of different housing unit types in their homebuyer programs, under both the HOME and NSP programs. However, there are restrictions on the value of the properties that can be used (HOME) and the purchase price of foreclosed homes (NSP).

Property Types

Eligible property types for HOME and NSP include any property that will serve as the purchaser's principal residence, including:

- One-unit (single family) property
- A condominium unit
- A cooperative unit or a unit in a mutual housing project (if recognized as homeownership by State law)
- A manufactured home (as discussed previously in this chapter)
- Two- to four-unit property, with the following considerations:
  - **Under HOME:**
    - HOME PJs have the option of designating all or some of the units as HOME-assisted and the HOME requirements (including the long-term affordability requirements) apply to all units so designated. A minimum number of units must be designated HOME-assisted, based on the amount of HOME investment, in accordance with the cost allocation methods described in Chapter 2.
    - If only the owner-occupied unit is HOME-assisted, then the assisted unit must be the principal residence of the purchaser and HOME's long-term affordability requirements apply to the assisted ownership unit only. See the discussion *Long-Term Affordability for Homebuyer Housing*, later in this chapter.
    - If any of the additional units are HOME-assisted, the HOME rental affordability requirements apply to the rental units.
  - **Under NSP:**
    - For a property with two units, at least one unit must be designated as an NSP-assisted unit.
    - For a property with three or four units, then the grantee can designate the number of NSP-assisted units in accordance with NSP cost allocation procedures described in Chapter 2 (either 51 percent of the units are designated NSP-assisted, or NSP-assisted units are so designated proportionally, based on the amount of funds invested in the property).
    - If only the owner-occupied unit is NSP-assisted, then long-term affordability requirements adopted by the grantee apply to the assisted ownership unit only. See the discussion *Long-Term Affordability for Homebuyer Housing*, later in this chapter.
    - If any of the additional units are NSP-assisted, the NSP rental affordability requirements adopted by the grantee apply to the rental units.

Property Values, Purchase Price, and Buyer Sales Price

There are several different requirements related to the sales price and value of properties that can be acquired with HOME and NSP funds.

Under HOME, the housing in a homebuyer program must be modest. This means:

- For a property that will be acquired (without rehabilitation) or newly constructed for a homebuyer, the ***sales price*** of the property cannot exceed 95 percent of the median purchase price for that type of single family housing for the area.

- For a property that will be acquired and rehabilitated for a homebuyer, the after-rehabilitation ***property value*** of the property may not exceed 95 percent of the median purchase price for that type of single family housing for the area.
    - An appraisal is not required, but PJs must use a reasonable method to determine property value:
        - An estimate of value performed by a PJ or subrecipient
        - An appraisal performed by a licensed fee appraiser or a staff appraiser of the PJ
        - A tax assessment of a comparable, standard property, if current and computed for 100 percent of the after-rehabilitation value.

PJs can use a HUD-published estimate of 95 percent of median purchase price (available online at www.hud.gov/homeprogram/), or they can conduct a specialized market analysis that meets the requirements outlined in the HOME Final Rule at 24 CFR 92.254 (a)(2)(iii).

NSP imposes two different caps that are related to the purchase price of an abandoned or foreclosed home or property:

- The ***purchase price discount cap*** (discussed in detail in Chapter 2) on foreclosed properties requires the grantee, developer, homebuyer, or other housing partner to acquire a foreclosed property at a discount when it buys a property from a lender who holds title to the foreclosed unit. The discount must be at least one percent (1%) below the current appraised value of the property. Abandoned or vacant properties are not subject to this requirement.
- The ***buyer's sales price cap*** requires that, after a foreclosed property has been rehabilitated or redeveloped, the grantee or its housing partner must sell the property to an individual homebuyer at a sales price that does not exceed the lesser of the total cost to acquire and develop the unit ***or*** the current market value. This sales price cap helps ensure that the price that an individual household pays for an abandoned or foreclosed unit ***after*** it has been rehabilitated or redeveloped is affordable and reasonable, given what the grantee (or housing partner) invested in the unit. It prohibits the grantee (or its partner) from making a profit on the final sale of the property to the individual household.

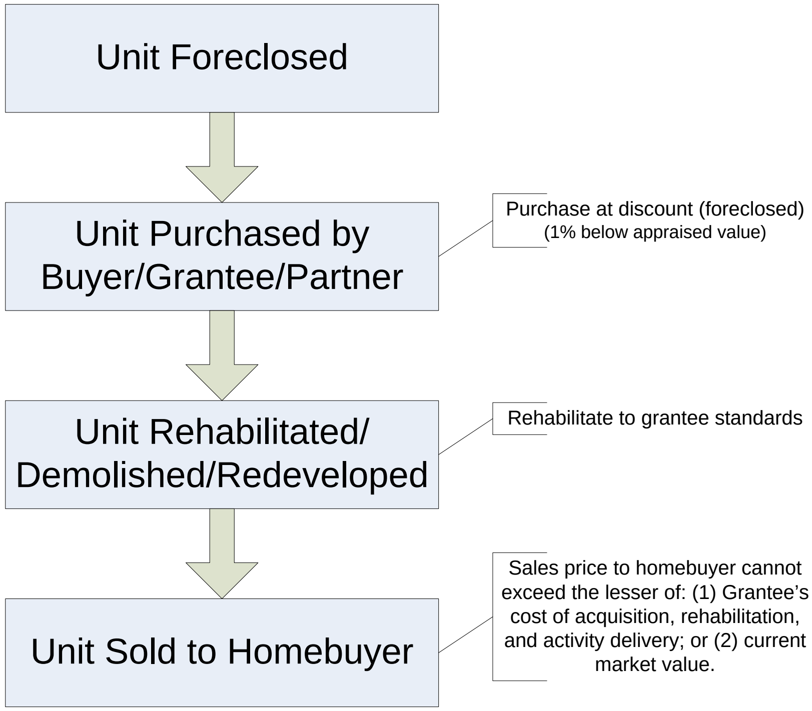
Exhibit 3-2 illustrates the interaction of these two NSP program caps.

When determining the total cost to acquire, redevelop, or rehabilitate the unit for the purpose of applying the sales price cap, the grantee counts all the costs of the project, not just those paid by NSP. In addition, this total cost can include:

- The grantee's (or housing partner's) construction costs
- Activity delivery costs (such as inspections, work write-ups, architects costs)
- A reasonable developer's fee; or, for grantees or subrecipients, activity delivery costs (such as project staff.)

The grantee cannot include in the sales price its costs to maintain the unit pending the sale of the unit to the buyer, such as costs to mow the grass or clean the home. These are NSP-eligible "disposition" expenses under 24 CFR 570.202(b), however. Nonetheless, without conducting rehabilitation on the property, the grantee cannot include these costs in the sales price to the homebuyer.

Exhibit 3-2: NSP Purchase Price and Sales Price Caps



When HOME and NSP are used in the same project, the grantee needs to ensure that:

- A property that is acquired and/or rehabilitated must:
  - Have an after-rehabilitation value of less than the HOME limits (95 percent of area median purchase price)
  - Be acquired from the lender for at least one percent below the current market value, if foreclosed property (NSP)
  - Be sold to an individual homebuyer at or below the total acquisition and development cost to the grantee or its housing partner or current market value, whichever is less (NSP).
- A property that is acquired without rehabilitation or that is newly constructed must:
  - Be acquired from the lender for at least one percent below the current fair market value, if foreclosed property (NSP)
  - Be sold to an individual homebuyer at a price that is:
    - No more than 95 percent of the area median purchase price (HOME)
    - The lower of (1) the total acquisition and development cost to the grantee or its housing partner, or (2) the fair market value, (NSP).

Exhibit 3-3 on the following pages illustrates how to apply the NSP purchase price discount and the HOME and NSP sales price caps to a project.

Exhibit 3-3: Applying the NSP Purchase Price Discount and the HOME and NSP Sales Price Caps

The following two scenarios demonstrate how the NSP purchase price discount and the HOME and NSP sales price caps are applied to a project.

Scenario 1: Assistance for Acquisition and Rehabilitation

In this scenario, the grantee provides a development subsidy to the project because the cost to acquire and rehabilitate the unit is greater than the unit's after-rehabilitation value.

Project Background

A grantee wants to acquire and rehabilitate a foreclosed home. The grantee has determined the following:

Acquisition cost	$ 60,000
Total development cost (includes acquisition, rehabilitation & activity delivery)	$141,000*
After-rehabilitation value	$100,000
95% of jurisdiction's median purchase price	$200,000
HOME maximum per unit subsidy	$120,000

* For purposes of this example, the HOME activity delivery costs are treated as project costs and are therefore included in the per-unit cost calculation.

Applying the HOME and NSP Rules

The table below illustrates the grantee's analysis of the property value and sales price requirements for the two programs.

Scenario 1 Property Analysis

	HOME	NSP	Comments
Maximum purchase price	$60,000 (Current value)	$59,400 (appraised value minus required 1% discount)	Depending on which funding source pays for the acquisition, the applicable limit for that program applies. (That is, if HOME pays for the acquisition, then $60,000 is the applicable limit.)
Maximum after-rehabilitation property value	$200,000 (95% of jurisdiction's median purchase price).	N/A	Property is eligible because the after-rehabilitation value of $100,000 is under this limit.
Per-unit subsidy limit	$120,000 No more than $120,000 in HOME funds can be invested in this project.	No set limit, but underwriting must substantiate that costs are reasonable and subsidy to buyer is appropriate.	The total development cost of $141,000 exceeds the HOME per-unit subsidy limit. Other funds are needed for the project.

	HOME	NSP	Comments
Maximum sales price to buyer	HOME does not establish a maximum sales price, but under typical market conditions it would not exceed the property value ($100,000).	$100,000	NSP maximum sales prices is based on the lesser of either: $141,000 (acquisition plus development plus activity delivery costs) Property value $100,000.

Project Analysis

The grantee can distribute the project costs between HOME and NSP in a number of ways, provided that it meets the following conditions:

- It does not invest more than $120,000 in HOME funds.
- It does not pay more than $59,400 to acquire the property if any NSP funds are invested in acquisition costs.
- The homebuyer does not pay more than $100,000 (fair market value) for the property.

Two possible investment strategies include:

1. The grantee funds up to the maximum per unit subsidy with HOME funds ($120,000) and uses NSP funds for gap financing ($21,000). If any NSP funds are invested in the property acquisition, then the grantee can pay no more than $59,400 to acquire the property. The property is sold to a low-income buyer at fair market value.

2. The grantee uses HOME funds to pay for the property acquisition ($60,000) and uses NSP funds to pay for the rehabilitation and activity delivery costs ($81,000). The property is sold to at fair market value to a low-income homebuyer.

Scenario 2: Assistance for Development and Homeownership Assistance

In this scenario, the grantee uses NSP funds to finance the acquisition and rehabilitation, and uses HOME funds to provide direct downpayment assistance to a low-income homebuyer.

Project Background

The grantee acquires a foreclosed unit with NSP funds for $30,000, and uses $30,000 in NSP funds for rehabilitation, including activity delivery costs. The homebuyer is able to secure a $35,000 mortgage from a private lender. The grantee uses HOME funds to provide the homebuyer with a soft second mortgage in the amount of $15,000 ($50,000 fair market value - $35,000 first mortgage).

Acquisition cost	$ 30,000
Total development cost (includes acquisition, rehabilitation & activity delivery)	$ 60,000
After-rehabilitation value	$ 50,000
95% of jurisdiction's median purchase price	$200,000
HOME maximum per unit subsidy	$ 55,000
Direct subsidy to buyer (homeownership assistance)	$ 15,000

The table below illustrates the grantee's analysis of the property value and sales price requirements for the two programs.

Scenario 2 Property Analysis

	HOME	NSP	Comments
Maximum purchase price	N/A	$29,700 ($30,000 - $300)	Since NSP funds are used for the acquisition of the property, the NSP 1% purchase price discount applies.
Maximum after-rehabilitation property value	$200,000 (95% of jurisdiction's median purchase price).	N/A	Property is eligible because the after-rehabilitation value of $50,000 is under the 95% median purchase price for the area.
Per-unit subsidy limit	$55,000	No set limit, but underwriting must substantiate that costs are reasonable and subsidy to buyer is appropriate.	The HOME investment of $15,000 is below the per-unit subsidy.
Maximum sales price to buyer	HOME does not establish a maximum sales price, but under typical market conditions it would not exceed the property value ($500,000).	$50,000	NSP maximum sales prices is the lesser of either: ▪ $50,000 (current market value) ▪ $50,000 total development costs (acquisition, rehabilitation, and activity delivery)

	HOME	NSP	Comments
Homeownership Assistance (Assistance to the Buyer)	$15,000		Since HOME funds are used to provide the soft second mortgage, and the property is sold at fair market value, the only direct assistance to the buyer is the HOME funds.

Project Analysis

The grantee is able to fund this project in the context of its existing program structure. NSP can fund the acquisition and rehabilitation, provided it complies with the purchase price discount requirement and pays no more than $29,700 for the property acquisition. HOME funds ($15,000) can be provided in the form of direct assistance to the homebuyer.

Property Standards

Properties that are assisted (acquired, rehabilitated, or newly constructed) with HOME funds and properties that are rehabilitated with NSP funds must meet certain property and/or rehabilitation standards. Note that the CDBG program does not impose minimum property standards; these requirements apply only to NSP. Therefore, when HOME and NSP are used together in a homebuyer project, the property must meet the property standards required by both programs.

Under HOME, the property standards requirements are based on the activity type, as follows:

- **Acquisition.** If no rehabilitation or construction is planned, the housing acquired must meet State and local housing quality standards and code requirements. If no such standards or codes apply, the property must meet Housing Choice Voucher Housing Quality Standards.
- **Rehabilitation and new construction.** Housing that is constructed or rehabilitated with HOME funds must meet all applicable State or local codes, rehabilitation standards and ordinances, and zoning ordinances. The PJ must adopt written rehabilitation standards to ensure that assisted housing is decent, safe, and sanitary. If no State or local codes apply, PJs must use a national model code.[3] New construction must also meet the International Energy Conservation Code.[4]
- **Manufactured housing.** Manufactured housing must meet the Manufactured Home Construction and Safety Standards established in 24 CFR Part 3280, which pre-empt State and local codes covering the same aspects of performance for such housing. (To be eligible under NSP, the property must be considered as real property under State law, and cannot be personal property.)
    - PJs providing HOME assistance to install manufactured housing units must comply with applicable State and local laws or codes. In the absence of such laws or codes, the PJ must comply with the manufacturer's written instructions for installation of the manufactured housing units.
    - Manufactured housing that is rehabilitated with HOME funds must meet the requirements outlined above that apply to all housing constructed or rehabilitated with HOME funds.

In addition, the HOME Program further requires (and the NSP Program recommends) that the PJ conduct periodic onsite inspections of rental housing to ensure that the applicable property standards are maintained throughout the affordability period.

Under NSP, any NSP-assisted rehabilitation or new construction of an eligible property must comply with applicable laws, codes, and other requirements relating to housing safety, quality, and habitability, in order to sell, rent, or redevelop such homes and properties. The NSP grantee must describe or reference what rehabilitation standards it will apply in its action plan amendment. The grantee should also specify if these property standards apply throughout the affordability period.

HUD strongly encourages grantees to incorporate modern, green building and energy-efficiency improvements in all NSP activities to provide for long-term affordability and increased sustainability and attractiveness of housing and neighborhoods. For NSP2 and NSP3, HUD requires that grantees meet

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3 The national model codes used by the HOME Program are the Uniform Building Code (issued by CABO), National Building Code (issued by BOCA), and the Standard (Southern) Building Code (issued by SBCCI). Since the promulgation of the HOME Program regulations, these code-issuing agencies have merged to form the International Code Council (ICC). The model codes used for the HOME Program are no longer being updated; in their stead, the ICC has adopted the International Building Code. HUD will consider whether changes to the HOME regulations incorporating the International Building Code are appropriate.

4 Formerly the Model Energy Code.

certain green standards for all gut rehabilitation and new construction of residential buildings. Gut rehabilitation includes replacement of the interior of a building, without or without changes to structural elements.

The NSP2 and NSP3 green standards are:

- For properties up to three stories, the property must meet the standard for Energy Star Qualified New Homes.
- For mid -or high-rise multifamily housing structures (such as a condominium building), the property must meet American Society of Heating, Refrigerating, and Air-Conditioning Engineers (ASHRAE) Standard 90.1–2004, Appendix G plus 20 percent (which is the Energy Star standard for multifamily buildings piloted by the Environmental Protection Agency and the Department of Energy).

For other NSP3-funded rehabilitation (not gut rehabilitation), the property must meet these standards to the extent applicable to the rehabilitation work undertaken. For instance:

- Use Energy-Star products when replacing obsolete products and appliances, such as:
    - Windows
    - Doors
    - Lighting
    - Hot water heaters
    - Furnaces
    - Boilers
    - Air conditioning units
    - Refrigerators
    - Clothes washers
    - Dishwashers.
- Use water efficient plumbing (such as WaterSense products) to replace:
    - Toilets
    - Showers
    - Faucets.
- Improve housing to mitigate the impact of disasters (such as earthquakes, hurricanes, flooding, and fires).

Additional resources related to sustainable and energy-efficient construction are available on the *NSP Resource Exchange* website at www.hud.gov/nspta.

All NSP- and HOME-funded development is also subject to Section 504 of the Rehabilitation Act of 1973 and the Fair Housing Act, including provisions that impose specific accessibility standards to serve persons with disabilities. (See 24 CFR Part 8, 24 CFR 100.205, 24 CFR 92.251, and 24 CFR 570.487 and 570.602.)

When combining HOME and NSP funds in a project:

- For rehabilitation, generally, the HOME property standards are likely to be the same or more stringent then the NSP standards, depending on what rehabilitation standards the grantee has adopted for NSP. Therefore, if a property meets the HOME property standards, it will usually also comply with NSP. Note, however, when NSP2 or NSP3 funds are used for gut rehabilitation or new construction, the project is subject to the additional green standards, which are generally more stringent than the HOME standards.

- For acquisition-only projects (such as providing down payment assistance to a buyer), NSP does not impose property standards, but HOME does. The unit will have to meet the HOME property standard throughout the affordability period.
- For new construction that involves both HOME and NSP2 or NSP3, the project is subject to both the International Energy Conservation Code and the additional green standards imposed by NSP.

Eligible Buyers

HOME and NSP funds must be used to assist income-eligible homebuyers. However, each program has different requirements defining the income-eligibility of beneficiaries, as follows:

- **Beneficiaries of HOME Program funds must be low-income.** This means that the assisted household's annual gross income cannot exceed 80 percent of area median income, as adjusted by household size. Annual income is based on the gross amount of income anticipated by all adults in the household during the 12 months following the effective date of the income determination.
- **Beneficiaries of NSP must be low-, moderate- or middle-income.** This means that the assisted household's annual gross income must not exceed 120 percent of the area median income, as adjusted by household size. Income-eligibility is determined in the same manner as the HOME Program. See Chapter 1 for more information on how to make income determinations.

When using HOME and NSP together in a homebuyer program:

- If HOME and NSP are invested in the same unit, HOME's more restrictive income-eligibility requirements apply and the assisted homebuyer of the unit must have an annual gross income that is at or below 80 percent of the area median income.
- If HOME and NSP are invested in the same project (such as a mixed-income condominium development), but both sources are not invested in the same unit, then the assisted homebuyers must meet the income requirements of the applicable program. This means that the homebuyers of the HOME –assisted units must meet HOME income guidelines, and homebuyers of NSP units must meet NSP income guidelines. If the development serves households with incomes over 120 percent of area median income, neither HOME nor NSP can assist these buyers.

Under both NSP and HOME, grantees can choose one of three definitions of income to determine income-eligibility. These are explained in detail in Chapter 1.

Further guidance on how to calculate a homebuyer's income-eligibility can be found in the HOME Program model guide, *Technical Guide for Determining Income and Allowances for the HOME Program*. This publication is at www.hud.gov/offices/cpd/affordablehousing/library/modelguides.

Housing Counseling

NSP requires that each NSP-assisted homebuyer receive and complete at least eight hours of homebuyer counseling from a HUD-approved housing counseling agency before purchase.

If the household has recently participated in a housing counseling program, HUD may allow the grantee to count this participation; the grantee must secure written HUD approval. The grantee, State recipient, or subrecipient must obtain and file a copy of the counseling completion certificate received by the buyer. If a homebuyer is unable to meet this requirement for good cause (such as the lack of a HUD-approved housing counseling agency in the jurisdiction), then the grantee may submit a request for an exception to this requirement from the HUD Field Office.

Note that housing counseling costs for assisted buyers are eligible NSP activity delivery costs that are not counted as administrative costs and are not subject to the NSP ten percent administrative cap. However, if a counseling program is funded on a citywide or neighborhood basis, these costs are not NSP-eligible and need to be funded by CDBG as a public service. Grantees should note that NSP may pay for housing counseling costs for persons who do not finish the course and progress to a home purchase. In this situation, the counseling costs may be allocated across all project line items and charged as an activity delivery cost. The grantee must ensure that the homebuyer obtains a mortgage loan from a lender who agrees to comply with the bank regulators' guidance for non-traditional mortgages. (See *the Statement on Subprime Mortgage Lending* issued by the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Department of the Treasury, and National Credit Union Administration. This statement is available at www.fdic.gov/regulations/laws/rules/5000-5160.html.)

HOME does not require housing counseling but supports it as a part of program operations. HOME funds can be used to pay for housing counseling as a project cost when tracked to the specific HOME-assisted homebuyer and address, or the PJ can use its administrative funds to provide housing counseling to potential owners, tenants, and homebuyers of HOME-assisted housing.

Long-Term Affordability for Homebuyer Housing

Both HOME and NSP impose requirements to ensure that assisted properties remain affordable to income-eligible occupants for some period of time.

NSP grantees determine how to ensure continued affordability for the long term and describe their requirements in their action plans approved by HUD. NSP permits grantees to use the HOME Program affordability requirements as a safe harbor to meet the NSP affordability requirements, and many grantees use this option. Certainly when a grantee combines HOME and NSP, this option is the easiest to implement. However, if a NSP grantee adopts alternative requirements, it must reconcile its requirements with the HOME requirements when using both sources together in a homebuyer project.

The HOME Program requires that assisted units remain affordable for a period of time known as the affordability period. For homebuyer housing, affordability can be secured in one of two ways—through a resale restriction that restricts the resale of the assisted unit to another income-eligible buyer at an affordable price; or through a recapture provision that enables the HOME PJ to recapture the HOME investment upon resale, in order to reinvest it in another HOME-eligible affordable housing project. The recapture option and the resale restriction respond to different market conditions.

The HOME PJ must state in its consolidated plan whether it will use a resale or recapture provision for each homebuyer program it administers, or if it will determine which option to use on a project-by-project basis. If it chooses the latter option, the PJ must advise the homebuyer about which option will be used before the HOME funds are committed to the project and it must describe these requirements in its agreement with the buyer. The PJ must also define the terms of these provisions in its consolidated plan.

A HOME PJ cannot impose both a resale and a recapture provision on the same unit — the PJ must choose one approach. However, a homebuyer under a resale provision can receive a HOME loan and be required to make periodic mortgage payments. For example, assume that a PJ has chosen to use resale as its means of affordability and provided a) $30,000 in development assistance to a CHDO to build the unit; and b) a $40,000 second mortgage to the homebuyer. In this instance, the PJ can use a resale provision to ensure ongoing affordability, but also require that the homebuyer make monthly payments to the PJ on the HOME loan.

When HOME and NSP funds are combined in a unit, the grantee should choose one approach (either resale or recapture), since the two approaches are not generally compatible. Once the sales price is restricted to affordable in one program (HOME or NSP), there will be limited funds to recapture for subsequent affordable housing under the other program. Further, combining both approaches creates confusion for the homebuyer, who would need to comply with both sets of rules when they sell their home. See Exhibit 3-7 for more information on this topic.

- Some NSP grantees have sought to impose both a resale restriction and a recapture restriction because they were concerned about "windfall" sales profits to homebuyers once local housing markets recover.
- Similar to HOME PJs, NSP grantees may choose to combine a recapture provision with a shared appreciation requirement that enables the grantee to receive some of this "windfall" back if the assisted buyer sells during the affordability period. See the section below on recapture provisions for more information on structuring shared appreciation.

The following sections describe the long-term affordability requirements under the HOME Program and identify any issues that might arise if the NSP grantee adopts the HOME rule to comply with the NSP long-term affordability requirements. As noted above, NSP grantees may adopt these rules as a safe harbor. The NSP grantee may impose more stringent standards, but it may not adopt ***less*** stringent standards. Most NSP grantees have elected to adopt the HOME rules for determining and tracking long-term affordability.

Definitions: Development Subsidies and Direct Subsidies

Direct subsidy: A direct subsidy consists of any financial assistance that reduces the purchase price ***below*** fair market value to an affordable price, or otherwise directly subsidizes the purchase (e.g., downpayment or closing cost assistance, subordinate financing).

Development subsidy: A development subsidy is the cost ***above*** the market price needed to develop housing. For example, the PJ might provide a $50,000 construction loan to a developer. The appraised value after construction will be $45,000 because of neighborhood and market conditions. The $5,000 difference between the $45,000 sale price and $50,000 construction loan is not repaid to the PJ and represents a development subsidy provided to the developer. While the subsidy does not go directly to the homebuyer, it helps make development of an affordable home feasible.

HOME Affordability Period

The PJ determines the affordability period for HOME-assisted homebuyer housing differently for projects using a resale restriction and a recapture option:

- When a resale restriction is used, the affordability period is based on the per-unit amount of HOME investment.
- When a recapture option is used, the affordability period is based on the amount of HOME assistance that enables the homebuyer to purchase the property.

Exhibit 3-4 specifies the duration of the affordability period.

Exhibit 3-4: Duration of the Affordability Period for Homebuyer Projects

HOME Assistance Per Unit (resale) or HOME Total Assistance to the Buyer (recapture)	Minimum Affordability Period
Under $15,000	5 years
$15,000-$40,000	10 years
Over $40,000	15 years

When HOME and NSP funds are combined, the minimum affordability period that HUD requires is determined for each program separately, and the periods runs concurrently for the two programs. However, the grantee has the option to establish a longer affordability period than the minimum required by HUD. When HOME and NSP are combined in a project, HUD recommends that grantees impose an affordability period that is based on the total Federal investment. This approach secures affordable housing in the community for longer periods of time.

For example, assume that a grantee is using the recapture option and it provides $10,000 of HOME down payment assistance and $14,000 of NSP homebuyer financing to the homebuyer. The minimum HOME affordability period is five years, based on the $10,000 HOME investment. The minimum NSP affordability period is also five years, based on the $14,000 NSP investment. These affordability periods can run concurrently for a total of five years. Alternatively, the grantee has the option to impose a longer affordability period of 10 years, based on the total Federal investment ($24,000).

HOME Recapture Provision

Recapture is a mechanism that enables the PJ to recover all or a portion of the direct HOME assistance in the event the initial HOME-assisted buyer voluntarily sells or involuntarily transfers the unit (through a foreclosure) during the affordability period. When a recapture option is used, the homeowner is at liberty to sell the HOME-assisted property to any buyer, at any price the market will bear. Generally, net proceeds from the sale are used to repay the HOME assistance. The PJ must use recaptured funds for other HOME-eligible activities. Net proceeds are the sales price minus loan repayment (other than HOME funds) and any closing costs.

Determining the Affordability Period

The affordability period under recapture is based on the total amount of HOME assistance that enables the homebuyer to purchase the unit. This amount includes:

- Any HOME down payment and closing cost assistance
- Direct assistance to the homebuyer toward the purchase price of the home
- The difference between the fair market value of the property and the sales price, when the property is sold to the buyer at a price below market value (often due to HOME development assistance).

Funds provided to an owner, developer, or sponsor for the unit's development are ***not*** included as assistance to the buyer. Note, NSP grantees that adopt the HOME affordability period and recapture provisions must calculate the amount subject to recapture in the same manner as under the HOME Program.

Structuring the Recapture Provision

HUD permits the PJ to adopt one of the following recapture options. Other options are subject to HUD approval:

- Recapture the entire amount of HOME assistance to the buyer, up to the amount of the net proceeds, before paying the homeowner's investment [24 CFR 92.254(a)(5)(ii)(1)].
- Return the owner's investment first, and then recapture the HOME assistance to the buyer, up to the amount remaining in net proceeds [24 CFR 92.254(a)(5)(ii)(4)].
- Reduce (or forgive) a portion of the amount of HOME assistance to the buyer during the affordability period, on a pro rata basis for the time the owner has owned and occupied the unit [24 CFR 92.254(a)(5)(ii)(2)]. Typically, the PJ prorates the reduction based on the amount of time that the owner occupied the unit in relation to the affordability period. For instance, one-fifth of the amount of HOME assistance is forgiven for each year of occupancy in a five-year affordability period; one-tenth is forgiven for each year of occupancy in a ten-year affordability period; and one-twentieth is forgiven in each year of occupancy in a twenty-year affordability period.
- Share the net proceeds proportionally with the owner [24 CFR 92.254(a)(5)(ii)(3)] when the net proceeds are not sufficient to repay both the HOME assistance to the buyer and the homeowner's investment in the housing. The net proceeds are distributed based on the following formulas:
    - HOME investment/HOME investment plus owner investment X net proceeds = HOME amount to be recaptured
    - Homeowner investment/HOME investment plus owner investment X net proceeds = Amount to homeowner.

The PJ can apply a shared appreciation model to any of these approaches. The PJ would choose one of the four net proceeds approaches outlined above, and in its original agreement with the homebuyer require the PJ and owner to proportionately share in the appreciated value of the unit. For example, assume a unit was originally sold for $100,000, and six years later, the market had appreciated and the homebuyer sold it for $150,000. Also assume the owner originally invested $10,000 (25 percent) in the unit and the PJ invested $30,000 (75 percent). The net proceeds at the time of sale are $60,000. Assume the PJ has chosen the second approach to recapture net proceeds (owner is paid first). In this instance, the owner would be repaid their $10,000 and the PJ would be repaid its $30,000. The remaining $20,000 in net proceeds would be shared in proportionately between the owner and the PJ, with the owner receiving 25 percent or $5,000 and the PJ receiving 75 percent or $15,000.

For the recapture option, if there are no net proceeds or if the net proceeds are insufficient to repay the HOME investment, the PJ must recapture an amount less than or equal to the net proceeds. This means that if there are not enough net proceeds at the resale to repay the PJ the entire amount of the HOME subsidy that is subject to recapture, the homeowner cannot be required to repay more than the amount of net proceeds. In this case, the PJ is also not liable to HUD for the difference between the original investment and amount available at the resale (or foreclosure).

For a more detailed discussion and examples of how to implement these recapture options, see Chapter 5 (Homebuyer Activities) of the training manual *Building HOME*, issued by HUD and available online at: http://www.hud.gov/offices/cpd/affordablehousing/training/materials/building/ch05.pdf

NSP Considerations When Adopting the HOME Recapture Option

If the NSP grantee adopts the HOME recapture option as its long-term affordability approach, it should consider the following:

- The NSP grantee must choose one of the HOME net proceeds recapture options for its homebuyer program, or seek HUD approval of an alternative.
- The grantee must limit the amount subject to recapture to no more than the net proceeds, in the event the net proceeds are insufficient to repay the NSP investment.
- Given that NSP units are often developed in neighborhoods where sale prices are currently depressed but are likely to improve in the coming years, NSP grantees may wish to consider also imposing a shared appreciation clause in their agreements with homebuyers. The shared appreciation would be calculated in the same way as was described for the HOME Program in the previous section.
- Funds that are recaptured through this recapture option are considered program income under NSP (note, they are considered recaptured funds under HOME):
    - Recaptured NSP funds must be used for a NSP-eligible use that meets a national objective.
    - Recaptured funds are not subject to the original income targeting requirements (that is, funds that are recaptured for a home that was targeted to a very low-income household can be used for any NSP-eligible activity and do not need to be used for another very low-income household).

It is important to remember that the HUD Field Office can approve an alternate approach to structuring the recapture provision for NSP if it is deemed at least as stringent as the HOME rules. The grantee must describe its planned affordability approach in its Action Plan for HUD to review. If the grantee wishes to change its current affordability approach, it must make a substantial amendment to its Action Plan and submit the revised plan to HUD for review and approval. Grantees wishing to use alternate approaches are encouraged to contact their local HUD Field Office to discuss their proposed approach.

For both HOME and NSP, once funds have been recaptured, the long-term affordability period of the assisted property terminates and the HOME or NSP requirements no longer apply. Thereafter, the home can be sold to any homebuyer, regardless of income.

For more information on HOME resale and recapture requirements see the HOME regulations at 92.254 and *HOMEfires*, Volume 5, Number 2, at
www.hud.gov/offices/cpd/affordablehousing/library/homefires/index.cfm.

For more information on NSP homeownership programs and program income *see NSP Policy Alert! Guidance on NSP-Supported Homeownership: Affordability, Financial Structure, and Program Income*, March 3, 2009:
http://hudnsphelp.info/index.cfm?do=viewResourceDetailsFacetedSearch&ResourceID=33

HOME Resale Restrictions

A HOME resale restriction ensures that the HOME-assisted unit remains affordable over the entire period of affordability, even in the event of a subsequent sale or transfer of property (i.e., foreclosure). This option is often preferred by PJs in high cost areas or rapidly appreciating housing markets. Using this option, the PJ may either (1) require the homeowner to sell the home to another eligible low-income homebuyer or (2) establish a "presumption of affordability" in neighborhoods where it is likely that the homes will remain affordable to low-income buyers.

The resale option ***must*** be used when:

- HOME assistance is provided ***only*** as a development subsidy and there is no direct HOME assistance to the homebuyer. HOME defines the development subsidy as the amount between the cost of producing the unit and the fair market value of the property. For instance, if a unit's total development cost is $80,000 and the fair market value is $60,000, the development subsidy is $20,000. (See 24 CFR 92.254(a)(5)(ii)(A)(5).)
- The HOME assistance to the buyer is in the form of a grant only and therefore there is no amount subject to recapture. (Note, the grantee can provide the assistance as a forgivable loan that does not require repayment. A forgivable loan functions like a grant, but enables the grantee to recapture HOME funds if the property is transferred during the affordability period.)

Determining the Affordability Period

The affordability period for resale is calculated differently than under recapture. It is based on the ***total*** per-unit HOME investment in the home, regardless of the amount that directly benefits the homebuyer.

The per-unit HOME investment includes:

- The total amount of HOME funds provided directly to the homebuyer, such as:
  - Down payment or closing cost assistance
  - Direct assistance to the homebuyer toward the purchase price
  - Any write-down in the sales price below market value, ***plus***
- The HOME funds provided to an owner, developer, or sponsor for the unit's development.

For example, consider a CHDO that receives $150,000 of HOME funds to develop a homebuyer unit. The CHDO then sells the unit to a buyer for $140,000. The CHDO also provides the buyer with $10,000 in HOME down payment assistance. Using a resale restriction, the PJ determines the affordability period based on the total HOME investment: *$150,000 development funds + $10,000 down payment assistance = $160,000.* The affordability period is 15 years.

Note that if the NSP grantee adopts the HOME resale restrictions to ensure long-term affordability, it must follow the HOME Program requirements for determining the minimum period of affordability.

Restrictions on Resale to a Subsequent Buyer

If the original buyer sells the assisted property during the affordability period, then the following rules apply:

- The new subsequent purchaser must be low-income and must occupy the property as the family's principal residence.
- The sales price must be affordable to a reasonable range of low-income homebuyers, as defined by the PJ. Many PJs choose to establish the maximum sales price by calculating the maximum principal, interest, taxes, and insurance (PITI) that could be paid by a reasonable range of low-income households without exceeding 30 percent of gross income, a widely used standard of housing affordability.
- The original homebuyer, now the home seller, must receive a fair return on his or her investment, as defined by the PJ. The PJ should identify its method for determining a fair return in the written documents that apply to the property. The homeowner's investment includes any down payment, loan principal payments, and capital improvements financed by the homeowner.

- Once an affordable price that offers a fair return to the seller is established, a PJ may choose to require the repayment of all or a portion of the HOME grant or loan upon resale, should net proceeds from the sale allow this. This is most likely to occur in housing markets where prices are appreciating.

NSP Considerations when Adopting HOME Resale Restrictions

When a NSP grantee adopts the HOME resale option, it must remember:

- Income targeting that applies to the initial homebuyer also applies to any subsequent homebuyers during the affordability period.
    - For instance, under NSP if the original buyer has an annual gross income at or below 50 percent of the area median income and is counted toward the grantee's NSP low-income set-aside targeting requirement, then during the period of affordability, any subsequent buyer must also be very low-income. If the original owner is income-eligible with an income of up to 120 percent of the area median income, then the subsequent purchaser can have an annual gross income up to 120 percent of the area median income. (Of course, if NSP and HOME are combined in the project, then HOME's more restrictive income-eligibility requirement would apply.)
- An affordable price must be based on affordability for the targeted income group (up to 50 percent of area median income for the NSP low-income set-aside, up to 80 percent of area median income for HOME, or up to 120 percent of area median income for NSP generally).

Example: How the Investment Strategy Impacts the Affordability Period When Using a Single Source of Funds

HOME funds in project:

- $75,000 development funds to the developer
- $5,000 down payment assistance to the homebuyer

Property's after-rehabilitation fair market value (FMV): $65,000

The affordability period will be different, depending on whether the PJ uses resale or recapture provision, and how the assistance is provided to the buyer:

- **Situation 1: PJ uses recapture provision; sells property at FMV:** Since the property is sold at FMV ($65,000), the direct assistance to the buyer is only $5,000. The period of affordability is five years.
- **Situation 2: PJ uses recapture provision; sells property below FMV:** If the developer sells the property for $50,000, then the assistance to the buyer is $20,000 ($15,000 for price differential between FMV and sales price plus $5,000 in down payment assistance). The affordability period is ten years.
- **Situation 3: PJ uses resale restriction; sells property below FMV:** The HOME investment for the property is $80,000 ($75,000 in subsidy for the development of the unit plus $5,000 in assistance to the buyer). The sales price of the property is not relevant since, with a resale restriction, the affordability period is based on the entire HOME investment. The affordability period is fifteen years.
- **Situation 4: Development subsidy only:** Assume the only HOME funds in the project are provided in the form of a development subsidy, and the property is sold at fair market value. In this situation, there is no direct assistance to the homebuyer. The PJ must use a resale restriction to enforce the affordability requirements. The affordability period is 15 years, based on the HOME investment of $75,000.

Presumption of Affordability

Under HOME, when the PJ determines that a specific neighborhood in its entirety is affordable and that it is likely to remain affordable for the foreseeable future, HUD permits the PJ to presume that any sale within that neighborhood will be affordable for the purposes of the resale restriction. In other words, the PJ can rely on the market forces to ensure the continued affordability of HOME-assisted properties, and the PJ can presume the property will be sold at an affordable price to another low-income household. To use a presumption of affordability, the PJ must undertake a market analysis and must document the affordability of the neighborhood in accordance with specialized procedures established by HUD and outlined at 24 CFR 92.254 (a)(5)(i)(B), in order to demonstrate that the neighborhood is, and is likely to remain, affordable. The PJ's analysis is subject to HUD approval, and must be periodically updated by the PJ if the PJ continues to invest HOME funds in the neighborhood.

Under NSP, the grantee can follow the HOME protocol for a presumption of affordability and it will be accepted as a safe harbor under NSP. Therefore, if the grantee wants to establish a presumption of affordability in a neighborhood, it must undertake a market analysis that is consistent with the evaluation outlined in the HOME regulation cited above, and submit it to HUD for approval. Note, if the grantee plans to invest NSP funds in the neighborhood for housing that will satisfy its low-income set-aside requirement, HUD will expect the market data to support the grantee's conclusion that the neighborhood is likely to remain affordable to very low-income buyers.

Providing HOME Assistance to the Second Buyer

When a unit is sold during the affordability period, the grantee may choose to provide purchase assistance to the second buyer if the buyer is qualified for the program. When a new buyer is assisted with HOME or NSP, the old period of affordability is terminated and a new affordability period begins. The new period of affordability may be either a resale or a recapture provision, since direct assistance is provided to the buyer. Whichever option is chosen by the grantee must be spelled out in its written agreement with the second buyer. The following sections describe how the affordability period is treated if the unit is originally under a resale or a recapture restriction and the second buyer is assisted with HOME or NSP.

Assistance to a Second Buyer When the Unit has a Resale Restriction

If the grantee assists the second buyer and chooses the resale option for this buyer of a resale unit, the grantee may establish the new affordability period based on the amount of direct HOME or NSP assistance provided to the new homebuyer. This is true regardless of when during the initial period of affordability the property is sold. The grantee also always has the option of establishing a longer affordability period, such as one that continues the balance of the existing resale affordability period or one that is based on the sum of the original assistance plus the assistance to the new buyer.

If no new HOME or NSP assistance is provided to the second buyer, that buyer must assume the remaining term of the original affordability period. A second buyer during the original resale affordability period must always be to an income-eligible household at an affordable price with a fair return to the seller. If the grantee elects to impose recapture requirements on the second buyer of a resale unit, the period of affordability is based on the amount of direct NSP or HOME assistance to the buyer. This period may be longer or shorter than the remaining balance of the original resale provision.

The example below compares the affordability period options when the second buyer of a resale unit is assisted.

Example: How the Investment Strategy Impacts the Affordability Period When Using a Single Source of Funds

A unit is constructed with HOME funds and has a 15-year resale affordability period. The original owner chooses to sell at the end of Year 7. The new buyer receives $5,000 in HOME down payment assistance.

- If the PJ chooses to impose a resale restriction on the second buyer, the new affordability period the term can be based on the $5,000 of assistance (five years) or, at the PJ's discretion, longer [e.g., the balance of the affordability period (8 years)].
- If the PJ chooses to require recapture for the second buyer, the original affordability period is terminated and the new affordability period is based on the $5,000 direct assistance. In this example, the new affordability period would be five years.

Assistance to a Second Buyer When the Unit has a Recapture Provision

When a unit has a recapture agreement, the affordability restriction on that unit is complete once the recaptured funds are paid by the original owner at closing with the new buyer. If the second buyer is assisted, a new affordability period begins, based on the level of HOME or NSP assistance provided to the new buyer.

For example, assume that the original buyer received $16,000 in down payment and closing cost assistance and thus had a 10-year affordability period. In Year 2, the buyer sells the unit, and the net proceeds are recaptured. At that point, the affordability period on this unit is complete, and the terms of the original buyer's assistance are satisfied. If the new buyer receives $5,000 in HOME closing cost assistance, then the grantee establishes a new five-year affordability period, based on the $5,000 investment. Exhibit 3-5 below summarizes the differences across the resale and recapture options.

Exhibit 3-5: Establishing Affordability Periods for Second Buyers

Type of Assistance to Second Buyer	Original Affordability Period: Resale	Original Affordability Period: Recapture
No NSP or HOME assistance to the second buyer	Affordability period is based on the remaining balance of the original resale period	Original affordability period is terminated -- no affordability period for the second buyer
HOME or NSP assistance to second buyer and grantee chooses ***resale*** for the second buyer	Affordability period can be based on the level of investment for the second buyer or the grantee can elect to impose a longer period, such as the balance of the original resale term	Affordability period is based on the level of investment to assist the second buyer
HOME or NSP assistance to second buyer and grantee chooses ***recapture*** for the second buyer	Affordability period is based on the level of investment for the second buyer	Affordability period is based on the level of investment for the second buyer

Preserving Affordability

Under both the resale and recapture options, the HOME regulations now allow for the investment of additional HOME funds when it is needed to preserve homebuyer housing for which HOME funds were initially invested. Specifically, PJs may use additional HOME funds to acquire housing through a purchase option, right of first refusal, or other preemptive right before foreclosure, to acquire the housing at foreclosure sale, to undertake any necessary rehabilitation, and to provide assistance to another eligible homebuyer. This provision does not apply if the PJ forecloses on its own HOME loan. The per unit subsidy limit applies to the ***total*** HOME funds used for the housing (the original amount plus any additional amount that is provided). However, administrative funds may be used for the acquisition and reimbursed upon sale of the property to a subsequent eligible homebuyer.

NSP funds can be reinvested in the same property before the affordability period has expired; however, given the stringent use and expenditure deadlines under NSP, this may be an unlikely situation. Note, if additional NSP funds are invested in the property before the completion of the affordability period, then the affordability period would start anew.

How to Choose a Resale or Recapture Provision in a HOME- and NSP-Funded Project

When the grantee invests HOME and/or NSP funds in a project, it must determine whether it will impose a resale or recapture provision, and determine the length of the affordability period for the project consistent with the funding source(s). Exhibit 3-6 compares the two options.

Exhibit 3-6: Comparison of Resale Restriction and Recapture Provision

Tool to Ensure Affordability	How It Works	Considerations
Resale restriction	Specific unit must remain affordable throughout affordability period. If unit is sold during affordability period: ▪ Initial owner must receive a fair return on investment ▪ Subsequent buyer must be income-eligible Unit must be sold at affordable price.	Grantee must define and determine "affordable price" and "fair return." Effective in housing markets with: ▪ Appreciating values ▪ Limited supply of affordable units. In some markets where housing values are not appreciating, meeting both "affordable price" and "fair return" requirements may be difficult.
Recapture Provision	Homebuyer can sell to any willing buyer, regardless of income. Grantee must define type of recapture provision (amount subject to recapture) up-front. If property is sold during affordability period: ▪ Amount subject to recapture depends on the grantee's program design, but is limited to what is available from net proceeds of sale Recaptured funds must be returned to the grantee and reinvested for HOME/NSP eligible uses.	Net proceeds of sale are used to repay grantee and initial homeowner investments. ▪ Grantee determines who is repaid first (grantee or homeowner), and whether insufficient proceeds (or equity) will be shared. ▪ Grantee may "forgive" part or all of subsidy subject to recapture by reducing amount to be recaptured during the affordability period. Use of recapture provisions can be effective in stable housing markets. In weak or declining markets, grantee may not recover full subsidy amount. Recapture with shared equity approach is effective in strong markets with appreciating values where prices are currently depressed.

In a project funded with both NSP and HOME, HUD recommends that the grantee impose the same affordability requirements (resale or recapture) for both programs, to avoid unnecessary complexity. Exhibit 3-7 on the following pages illustrates these options.

Exhibit 3-7: Using Resale and Recapture Requirements in HOME- and NSP-funded Projects

The following two scenarios demonstrate how resale and recapture requirements can be applied in jointly funded projects.

Scenario 1: HOME and NSP Invested in Acquisition and Rehabilitation of a Homebuyer Unit (Direct Subsidy)

The Project

- $25,000 of HOME funds for acquisition
- $25,000 of NSP funds for rehabilitation
- Property fair market value is $50,000
- Grantee sells the property for $40,000 to a low-income buyer to make it affordable. This is financed with a private mortgage.
- The initial homebuyer funds a downpayment of three percent, or $1,200.
- The owner (original homebuyer) sells the property in year four of the affordability period.

The Grantee's Options

In this scenario, the grantee has the option to impose a resale restriction or a recapture provision for both programs:

- **Use a Resale Restriction for Both Programs**
  The grantee must consider:
  - **Affordability period.** To ensure affordability for the longest period of time, HUD recommends that the grantee establish an affordability period of at least fifteen years, based on the total Federal investment of $50,000. (Note: the grantee has the option to establish an affordability period of ten years based on the $25,000 investment amount for each program. In this case, the affordability period for the two programs runs concurrently.)
  - **"Affordable price."** The grantee must define "affordable price" to a subsequent buyer. A typical approach is to define affordability in terms of a percentage of a low-income buyer's principal, interest, taxes, and insurance (PITI). For this example, the grantee defines affordable price as 30 percent of a low-income buyer's PITI.
  - **"Fair return."** The grantee must define "fair return" on investment. Often, the grantee defines this as a percentage return on the homebuyer's total initial investment plus any subsequent investments, or simply as the repayment of the homebuyer's initial investment plus any investments made for capital improvements during the affordability period. For this example, the grantee defines fair return as the repayment of the homebuyer's initial investment plus investments for capital improvements.
  - **Upon Resale of the Property.** In this scenario, from the sale, given the grantee's definitions of affordable price and fair return on investment, the following must occur:
    - If there are sufficient net proceeds of sale, the homeowner must be repaid their initial $1,200 investment. In stagnant housing markets, there may not be sufficient proceeds to repay the owner's investment. It is also possible that if the value of the property has depreciated, the owner's fair return may be $0.

        - The property must be sold at a price that is affordable to a low-income buyer and the buyer cannot pay more than 30 percent of annual gross income for housing costs (PITI).

- **Use a Recapture Provision for Both Programs**
  The grantee must consider and/or determine:
    - **Assistance to the buyer.** In this project, the assistance to the homebuyer is $10,000. This is the difference between the fair market value of the property and the sales price to the initial buyer.
    - **Terms of recapture.** The grantee chooses how to structure the recapture provision, deciding how net proceeds will be distributed, who is paid first, and whether insufficient net proceeds (or equity) will be shared. In this scenario, the grantee chooses a recapture provision that requires recapture of the entire $10,000 prior to repayment to the homeowner.
    - **Distribution of net proceeds upon resale of the property.** Assume in this scenario that the property is sold for $45,000, closing costs are $2,000, and the outstanding balance on the first mortgage is $38,000. Upon resale of the property, closing costs and the first mortgage must be repaid first. This leaves net proceeds in the amount of $5,000 ($45,000 - $2,000 - $38,000). Since the grantee opted to recover the Federal subsidy first (prior to repaying the owner its investment of $1,200), the grantee recaptures the full amount of net proceeds ($5,000). It distributes the recaptured funds in proportional amounts for each program (50 percent of the recaptured funds are reinvested in NSP; 50 percent are reinvested in HOME). In this scenario, the homeowner does not recover its initial investment.

- **Use a Resale Restriction for One Program and a Recapture Provision for the Other**
  The grantee may not use a resale restriction for one program and a recapture provision for the other. This is because in most housing markets, if the property sale is restricted to a low-income household at an affordable price, with a fair return to the initial buyer, it is unlikely there will be sufficient funds for the grantee to recapture.

Scenario 2: NSP Development Subsidy and HOME Assistance to Buyer

The Project

- $40,000 in NSP funds for rehabilitation
- $5,000 in HOME funds for down payment and closing cost assistance
- Private financing to purchase the property for $50,000; this is the fair market value

The Grantee's Options

In this scenario, the grantee must use a resale restriction under NSP since there is no NSP assistance to the buyer. This means that the resale of the property must be to a low-income buyer and the sale price must be affordable. To maximize the longest possible affordability for the unit and to minimize administrative complexity, the grantee should restrict the resale of the property for both programs.

To do this, the grantee follows the steps outlined in the scenario above: it must identify the affordability period for both programs, and define what it means to sell the property at an affordable price, and provide a fair return on investment to the initial homebuyer. In this scenario, the grantee has the option to impose either: (1) a ten-year affordability period for NSP and a five-year affordability period for

HOME, and have those years run concurrently, or (2) a 15-year affordability period for both HOME and NSP, based on the combined Federal investment of $45,000.

Enforcing Resale and Recapture Provisions

Under HOME, the PJ is responsible for enforcing the resale and/or recapture provisions it imposes.

Enforcing Resale Restrictions under HOME

When using a resale restriction, the PJ must execute and record a deed restriction, covenant running with the land, or similar legal mechanism approved by HUD (unless affordability is secured through a presumption of affordability). Such a restriction on the land ensures that the HOME requirements are passed on to any subsequent owners, in the event the property is transferred during the affordability period.

In addition, the PJ must execute a written agreement with each owner, developer, or sponsor of HOME-assisted housing that conveys the HOME requirements and specifies the PJ's right to enforce the terms of the resale restriction. Further, the PJ must execute a written agreement with each homebuyer to establish the PJ's legal right to enforce the restrictions. This agreement must clearly state the homebuyer's obligations to occupy the unit as its principal residence and to meet the specific terms of the resale restriction.

Upon foreclosure of a property with a resale restriction, when affordability restrictions are suspended in order to clear title to a property, the PJ is still held responsible for ensuring that the property is transferred to another income-eligible buyer, or the PJ must repay the HOME funds.

Enforcing Recapture Provisions under HOME

For PJs using a recapture provision, the PJ must execute a deed of trust, note, or mortgage that specifies the amount of HOME funds that are subject to recapture, at a minimum. Ideally, however, the PJ should secure the recapture provisions with a deed restriction or covenant running with the land.

As with a resale restriction, the PJ must execute a written agreement with each owner, developer, or sponsor of HOME-assisted housing that specifies the PJ's right to enforce the terms of the recapture provisions; and it must execute a written agreement with each homebuyer to establish the PJ's legal right to enforce the recapture provisions. The agreement must clearly state the homebuyer's obligations to occupy the unit as its principal residence and must specify the amount of HOME funds that are subject to recapture, and under what circumstances those funds will be recaptured.

Upon foreclosure of a property with a recapture provision, HOME funds must be recaptured in accordance with the PJ's recapture provisions. This means, at foreclosure, when there are no net proceeds, or the net proceeds are insufficient to repay the HOME investment due, the grantee may recapture an amount less than the net proceeds, in accordance with its provisions. Once this is done, the long-term affordability requirements are terminated and the PJ's obligation is satisfied.

Considerations for Enforcing Affordability Requirements under NSP

Under NSP, the grantee must adopt a means to enforce the resale restriction or recapture provision. The HOME enforcement mechanisms can be adopted as minimum level of enforcement. In its action plan, the grantee's description of how it will ensure continued affordability for NSP properties should specify how these requirements will be enforced.

When HOME and NSP are used together, it is recommended that the grantee adopt the HOME enforcement mechanisms; if the grantee adopts its own enforcement mechanisms, the requirements of both must be met.

Chapter 4: Opportunities for Rental Development with HOME and NSP

While many communities may think of NSP as primarily a single family homebuyer program, in fact the program presents unique opportunities for addressing rental housing needs as well. In addition, the HOME Program continues to be a major resource for creating rental housing nationwide. This chapter:

- *Summarizes how HOME and NSP can be used together to create affordable rental housing*
- *Describes the range of approaches for creating rental housing*
- *Discusses the rules for financing and developing rental housing when combining NSP and HOME funds in a project*
- *Identifies ongoing rules for managing the rental properties over time.*

Approaches to Creating Rental Housing

There are many possible approaches to using HOME and NSP to develop affordable rental housing:

- **Acquisition of existing rental housing.** The grantee or its housing partner can acquire standard rental housing and rent it out at affordable rents. Under NSP, this can be done under Eligible Use B, using property that is foreclosed or abandoned. Rental property can also be acquired under Eligible Use E, but the property must be vacant, making it far less likely to be in standard condition.
- **Rehabilitation.** Grantees may use HOME or NSP to rehabilitate existing housing. Under NSP, the housing must be foreclosed or abandoned (under Eligible Use B) or vacant (under Eligible Use E). Note that rehabilitation can be combined with acquisition.
- **Reconstruction and conversion.** Reconstruction is the rebuilding of an existing unit on the same site. Conversion is developing a non-residential structure into a residential one. Both reconstruction and conversion are allowed under HOME and are treated as forms of rehabilitation. NSP permits reconstruction as a rehabilitation activity under Eligible Use B (for foreclosed or abandoned property) or under Eligible Use E (for vacant property), as above. NSP allows the conversion of any type of vacant structure into housing.
- **New construction.** This involves building new rental units, which is permitted under HOME. Unlike CDBG, NSP also allows new construction but only under Eligible Use E.
- **Tenant-based rental assistance.** In communities with a sufficient supply of standard housing, rental assistance is provided directly to the tenants. This is known as "tenant-based rental assistance," or TBRA. It is allowed under HOME but not under NSP.

For NSP3, the grantee must establish procedures that create a preference for the development of affordable NSP-assisted rental housing. Grantees must describe such procedures in their action plan substantial amendments or abbreviated plans.

Acquisition

HOME Eligible Activity Type: *Rental Housing*

NSP Eligible Uses: *(B) Purchase and Rehabilitation; (C) Land Bank; or (E) Redevelopment*

Both HOME and NSP funds can be used to support housing acquisition. An acquisition program involves purchasing existing standard rental units within the community and then lowering their rents to make them affordable to income-eligible households. Usually, this is accomplished by directly subsidizing the purchase of the units so that the owner's ongoing financing costs are reasonable, making it possible for to offer lower rents.

There are several benefits of using an acquisition approach to developing affordable rental housing:

- It can be very cost effective since no construction is needed.
- It can be successful in communities that have ample rental housing stock in standard condition.
  - In many communities, there are not a sufficient number of units in standard condition that are also reasonably priced for purchase. In this type of community, it may not be financially feasible to purchase existing units and offer them at an affordable rent.
- It can be used to promote mixed-income housing goals.
  - For example, a PJ can use HOME funds to assist a developer who is purchasing a 50-unit building. The HOME funds are invested in five of the total units. (Note, the HOME investment is capped at the maximum per unit subsidy limits.) These five units carry the HOME restrictions related to affordability, income, and unit quality. The developer is able to rent the remaining 45 units to moderate- or upper-income people.
  - NSP can also be used to fund this type of project, assuming that its level of investment pays for its fair share, consistent with the percent of units that are occupied by persons who are low-, moderate-, and middle-income (LMMI). (See Chapter 2 for more information on HOME and NSP cost allocation and fair share.)
- If scattered site, single family units are acquired for rental housing, it can support deconcentration of lower income people. Note, however, that scattered site rental housing can be more expensive when the units are geographically spread.

While a grantee can fund acquisition with either HOME or NSP funds, or both, it should note the following rules:

- For HOME, the units must meet the applicable local code or national model codes and standards. If the units are not in standard condition, HOME can also assist with rehabilitation costs (discussed below).
- Under NSP, acquisition is an eligible activity under Eligible Use A (financing mechanisms), B (purchase and rehabilitation), C (land banking), or E (redevelopment).
  - If Eligible Use A is used, the grantee provides a loan, grant, interest rate subsidy, or other financing to assist the purchaser to buy a ***foreclosed*** property.
  - If Eligible Use B is used, the grantee can directly acquire ***abandoned*** or ***foreclosed*** units and then re-sell them to developers, or it can provide assistance to nonprofit or public developers to buy and then rent units.

For an acquisition-only activity under NSP, only the grantee, a public agency, or a nonprofit subrecipient can make the rental housing purchase because CDBG prohibits developers from undertaking acquisition-only housing activities. Note, however, that NSP permits for-profit and nonprofit developers to undertake acquisition with rehabilitation because that is classified as a rehabilitation activity rather than as an acquisition activity. Under rehabilitation in the CDBG regulations, an end-user (such as a homeowner or a developer) is not required to administer funds as a public agency would.

Eligible Use C allows public agencies and nonprofits to acquire foreclosed properties and hold those properties in a land bank for up to ten years. In many communities, the units held in a land bank will be blighted and may be demolished and held as vacant land. Land banking is intended only as an intermediate activity; the end use for the property must be eligible under Eligible Use A, B, or E as described in this guide.

The CDBG change of use rules apply to property that is acquired with NSP funds. This means that when an entitlement community invests $25,000 or more in NSP funds (or $100,000 in NSP funds for States), the property must be used for the original approved purpose in perpetuity, unless the grantee undertakes certain steps, including a citizen participation process, to approve the new, eligible use. (See 24 CFR 570.505 for more information on this issue.) Note that a subrecipient can change the property use any time after five years from its closing out its subrecipient agreement with the grantee.

Rehabilitation, Conversion, and Reconstruction

HOME Eligible Activity Type: *Rental Housing*

NSP Eligible Uses: *(B) Purchase and Rehabilitation; or (E) Redevelopment*

Rehabilitation of existing housing is another way of creating affordable, standard rental housing. Under this model, a jurisdiction provides low-cost assistance to help an owner bring his or her units up to a quality standard. In return, the owner agrees to rent units at reduced rents to income-qualified households. This model can be combined with acquisition so that the developer is acquiring and rehabilitating the property. Rehabilitation can be minimal, or it can be very extensive, including reconstruction.

There are two obvious benefits to this approach — it helps to house low-income families and it reduces the number of existing dilapidated housing units in the community. This approach to developing affordable rental housing can be quite expensive, however. In some communities, and given some project situations, it may be more expensive to renovate units than to undertake new construction. Also, when rehabilitating occupied units, extensive renovations might cause displacement and trigger requirements and related costs under the Uniform Relocation Act and/or Section 104(d) relocation.

Both HOME and NSP can be used for rehabilitation only or for acquisition with rehabilitation. Both programs can also finance historic preservation as a part of rehabilitation. In these instances, jurisdictions work with their State's Historic Preservation Office (SHPO) to determine the appropriate scope of work. Under either program, any rental housing can be rehabilitated so long as the resulting units are standard and rented to income-eligible tenants.

Under NSP, rehabilitation is primarily undertaken under Eligible Uses B and E. Under Eligible Use B, the grantee itself, a subrecipient, or a developer buys and rehabilitates foreclosed or abandoned units; under Eligible Use E properties that are acquired and rehabilitated (or constructed) must be demolished or vacant. In some cases, the existing units on a site are sufficiently substandard that traditional rehabilitation is not cost effective. In these cases, the grantee or developer may demolish the existing units and rebuild units of the same size on the same lot. This reconstruction activity is allowed as a form of rehabilitation under both HOME and NSP. The reconstructed units do not need to be on the same foundation as the original units but do need to have the same number of dwelling units. For example, assume that a grantee demolishes a 10-unit rental complex. It can rebuild a new 10-unit rental complex on the site as a rehabilitation activity. Note, however, that if the number of dwelling units is increased or decreased then the activity is "new construction."

For NSP, reconstruction is usually done under Eligible Uses B or E. Eligible Use E also supports new housing construction.

A jurisdiction might also choose to rehabilitate an existing commercial or industrial building and convert it into affordable units. Generally, conversion of an existing structure to affordable housing is eligible as rehabilitation under both the HOME Program and NSP. Conversion projects are treated as new construction only when adding one or more units beyond the existing walls.

New Construction

HOME Eligible Activity Type: *Rental Housing*

NSP Eligible Uses: *(E) Redevelopment*

Grantees can provide affordable rental housing by building new units. Under this approach, the grantee typically works with a nonprofit or for-profit developer who identifies the site, develops the plans and specifications, and works with a general contractor to build the units.

The benefit of new construction is that it generates new affordable units for the community. In addition to creating housing, new units can help spur other development or services in the neighborhood. New construction can also be very expensive, and delivery of new units can take a long time. Depending on local market conditions, new housing may also exacerbate an oversupply of units.

HOME can be used for new construction of rental units. It can finance all or a portion of the costs, including the acquisition of the site, hard construction costs, soft costs, or an 18-month project operating reserve. As with other forms of rental development, the amount of HOME funds invested will dictate how many HOME units must be provided. (See Chapter 2 for a more detailed discussion of cost allocation.)

Unlike CDBG, NSP can be used for new construction of housing, regardless of whether a community-based development organization (CBDO) is involved. However, NSP funds can only be used for new construction under Eligible Use E. This means that the new construction must be related to the redevelopment of a vacant or demolished site; the site need not have been foreclosed or abandoned, although it could have been. With NSP funds, the grantee can also finance the cost of infrastructure to support new housing development.

Tenant-Based Rental Assistance

HOME Eligible Activity Type: *TBRA*

Another method of making existing rental housing affordable is to offer assistance to help tenants pay their rent. The most common tenant-based rental assistance (TBRA) model is the Housing Choice Voucher Program that is run by housing authorities across the country.

HOME can be used to create a TBRA program. The program options are highly flexible—from a voucher model to a security deposit only program. NSP cannot be used for TBRA because the CDBG program considers rental assistance as a type of income payment (i.e., payments directly to or on behalf of households) which is expressly prohibited, unless it is conducted as a part of a CBDO-eligible activity.

Tenants can use HOME TBRA to pay rent in a HOME- or NSP-assisted unit. Tenants can also choose to use HOME TBRA in a private or other assisted unit within the jurisdiction since HOME TBRA is provided to the tenant, and is not provided to the project or unit. Neither HOME nor NSP grant funds can be used for project-based assistance to pay for ongoing project operating costs.

Converting Rental Units to Homeownership Units

NSP funds can be used to develop rental housing units, with the intent of converting them to homeownership before the end of the affordability period. Under HOME, rental units can only be sold to existing tenants during the affordability period. This strategy is discussed in more detail in Chapter 3, subsection "Converting Rental Units to Homeownership Units."

Methods of Financing

The grantee may provide assistance to rental housing in a number of different forms, each with its own risks, as described below:

- **Refinancing.** HOME funds may be used to refinance existing debt if the HOME funds are used to rehabilitate the property and the refinancing is necessary to permit or continue affordability. Certain restrictions apply. NSP funds may not be used only for refinancing but can be done in concert with rehabilitation or construction activities on the property.

- **Predevelopment loans or grants to pay for project planning and pre-construction activities.** Predevelopment expenses include staff costs of the developer, options to purchase land or a building, legal fees, architectural and engineering fees, appraisals, and possibly loan application fees. These expenses are the highest risk because money is spent before the developer can determine whether the project is feasible and there is security for loan. Forgivable predevelopment loans are available under HOME at the PJ's discretion for CHDOs only. If the project does not go forward, the HOME PJ can forgive the CHDO predevelopment loan and it remains an eligible cost. NSP can be used to pay predevelopment costs for any developer; in the event the project does not move forward, these costs are forgiven and are treated as activity delivery costs or may be charged as general administrative expenses, subject to the administrative cap. Note that HOME and NSP predevelopment funds cannot be used before completion of the environmental review and approval of the Request for Release of Funds.

- **Construction loans.** These short-term or interim loans cover the cost of constructing or rehabilitating a project, with one or more long-term, permanent loans taking out (paying off) the construction loan at project completion. Construction funds from traditional private lenders are typically loaned at a higher interest rate than permanent loans due to the high risk involved. Construction loans are allowed under both HOME and NSP. Because of the high risk, the grantee should verify that permanent financing is available before making a construction loan (to make sure it can be repaid). If not, the grantee may inherit a partly finished building if anything happens during construction to create a significant budget shortfall, or if the developer abandons the project. In such an event, it is unlikely the grantee could sell the building for what it has invested.

- **Permanent mortgage loans.** Permanent loans provide long-term financing and are repaid from the operating income from a rental or cooperative housing project. Permanent loans are used to repay construction, bridge, and predevelopment loans. If the HOME or NSP permanent financing replaces other loans, the original loans must have been used for eligible costs in compliance with all applicable Federal requirements, such as Davis-Bacon wage rates. Grantees may choose to finance part or all of the total development costs. If there is a high vacancy rate, an unexpected increase in operating costs, or a need to deplete reserves earlier than expected, the grantee may not get repaid. If not combined with private financing, this method also ties up large amounts of HOME or NSP funds in a few projects and, therefore, risks are concentrated.

    - **Bridge loans.** Often provided by the construction lender, these short-term loans finance the project if upon construction completion, the project does not yet meet the requirements of permanent financing. Bridge loans are used when the project will not be ready for permanent financing when construction is complete, such as with multi-stage projects or projects awaiting low-income housing tax credit equity payments. They may also be used when the permanent mortgage lender wants a project to establish a track record before making a loan. Significant changes in the project's projected income or expenses could affect the availability of permanent financing, even if a loan commitment is in place. Bridge loans are allowed under both HOME and NSP, assuming that the project is eligible and followed all applicable rules.
    - **Credit enhancements.** Credit enhancements such as loan guarantees, mortgage insurance, and loan loss reserves, are used to enhance the credit-worthiness of a project to attract private lenders who would not otherwise participate. Default requires a cash pay-off of the lender. Loan guarantees are allowed under HOME for any rental activity and are eligible under NSP under Eligible Use A, B, and E, since rehabilitation in CDBG includes financing.

Levels of Investment

The levels of HOME and NSP investment are impacted by a number of requirements, reviewed in detail in Chapter 2, that include:

- The minimum level of HOME assistance is $1,000 per unit and the maximum amount of HOME assistance is capped by the Section 221(d)(3) maximum subsidy limits, as published by HUD.
- Each project with multiple funding public funding sources is subject to a subsidy layering review as required by HOME, and underwriting as required by NSP.
- If the project contains multiple units, both NSP and HOME pay only their fair share of the total eligible development costs, in accordance with applicable cost allocation methods.
- When NSP funds are used to acquire a foreclosed property, the purchase price must be at least one percent less than the appraised value of the property.

Eligible Rental Projects

Both HOME and NSP define rental projects as one or more buildings on a single or multiple site(s) that are under common ownership, management, and financing. Both programs offer a wide range of options in the design and selection of rental projects. Grantees are free to choose projects that meet their local preferences for project size, unit style, or unit amenities, so long as all costs are eligible, reasonable, and necessary. Specifically, there is flexibility in:

- Property and unit types
- Targeting for special needs populations.

Property and Unit Types

Under HOME and NSP, eligible properties that can be used to develop rental housing include:

- **Publicly- or privately-owned.** Properties may be owned by nonprofits, private developers, housing authorities, or other public agencies. However, HOME funds may not be used for development, operations, or modernization of public housing projects financed under the Housing Act of 1937. HOME funds can be used in combination with HOPE VI funds. NSP funds can be used to modernize public housing units but NSP cannot be used to operate public housing.
- **Wholly residential or mixed-use.** Mixed-use properties are those that contain both a commercial and a residential element. For example, a property might have commercial space on the ground floor street level and residential unit(s) on the upper floors. HOME can pay only for the residential portion of the building. NSP can also be used to pay for residential development. Under Eligible Use E, NSP1 funds (but not NSP2 or NSP3) can also be used for commercial rehabilitation on the building if the property is vacant. However, the grantee must consult with its local HUD Field Office representative before funding this type of activity. CDBG can be used for the commercial portion of the project if the project is eligible and meets a CDBG national objective.

For both the NSP and HOME programs, there are no preferences for project or unit size or style. Rental housing is often developed in multi-unit, multifamily buildings. These buildings may be of any style from high-rise elevator buildings to garden style walk-up units. Rental projects may also include small duplex, triplex, or quad buildings where the owner may live in one of the units, as well as single family detached units.

While these types of multi-unit buildings are certainly allowed under both NSP and HOME, other property styles are also possible. For example, single family units may be held under common ownership, management, and financing and operated as a scattered site rental project. This may be particularly common under NSP, where many of the foreclosed or abandoned units are single family structures. It is important to note, however, that scattered site rental projects can be difficult and expensive to operate and grantees should encourage developers of these properties to seek technical assistance from experienced property managers.

In addition, a range of rental ownership styles are possible under both HOME and NSP. In addition to the traditional nonprofit, public, or for-profit ownership models, properties may be owned by the tenants under a resident management corporation. Similarly, some States consider mutual or cooperative housing as a form of rental housing. As described in Chapter 3, units may also be developed under a lease-purchase approach, whereby the tenants are saving to buy the unit within a specified timeframe. Finally, as noted above, under NSP, units may be owned by a land bank and temporarily rented out pending the final use of the site.

Special Needs Housing

There are some significant differences between the HOME and NSP programs when it comes to special needs housing and facilities.

HOME can be used only to fund permanent housing; temporary housing is ineligible, including shelters that have a residential component, such as homeless shelters or orphanages. Transitional housing is eligible under the HOME Program, provided it meets the definition of transitional housing at 24 CFR 92.2. Under HOME, transitional housing, single room occupancy units (SROs), and group housing units are considered to be rental housing activities and they must comply with the HOME rental housing rules. (The HOME rents are calculated differently for these types of units, however; for guidance on how to determine HOME rents for these units, see HUD's publication *Compliance in HOME Rental Projects: A Guide for PJs*, (HUD-2009 HOME Rental PJ), issued March 2009.)

Under NSP, group homes and SRO units are temporary housing; and these and other types of temporary special needs housing are defined as ***public facilities***. Therefore, under NSP, these facilities can only be developed only with NSP1 funds (not with NSP2 or NSP3) under Eligible Use E. This has several important implications:

- If developed with NSP1 funds, these units qualify under the limited clientele national objective rather than under the housing national objective. If the facility exclusively serves a clientele that is presumed to be LMMI, the grantee is not required to document household income.
- Public facilities must be owned by the grantee, a nonprofit, or another public agency. Therefore, for-profit firms cannot develop and own a facility for persons with special needs under NSP.
- Since these units are public facilities and not housing, expenditures for these projects do not count toward the grantee's 25 percent low-income set-aside requirement.

Certain types of transitional housing may be eligible as housing under NSP, provided the tenant has a lease for the housing and the grantee defines the housing type as permanent housing.

Unit Mix and Income Targeting

HOME and NSP's different income targeting requirements impact the rental property management of these properties.   Effective and compliant property management requires up-front designation of assisted units, and identification of unit-specific income targeting for HOME- and NSP-assisted units.

Designating Assisted Units

A HOME-assisted unit is a unit that has been purchased, rehabilitated, or constructed using HOME funds. In order to manage compliance with rent and occupancy requirements throughout the affordability period, the PJ must determine whether its HOME-assisted units are "fixed" or "floating."

- **Fixed.** When HOME-assisted units are "fixed," the specific units that are HOME-assisted (and, therefore, subject to HOME rent and occupancy requirements) are designated and do not change during the affordability period. For example, Unit 101 is designated as HOME-assisted and Unit 101 remains HOME-assisted for the duration of the affordability period. When units in a project are not comparable (in terms of size, number of bedrooms, and amenities) they must be designated as fixed.
- **Floating.** When HOME-assisted units are "floating," the units that are designated HOME-assisted may change over time as long as the total number of HOME-assisted units in the project remains constant. For example, initially, Unit 101 is designated HOME-assisted and Unit 201 is designated non-assisted. If the household that occupies Unit 101 becomes over-income, then when Unit 201 vacates, it can be redesignated as the HOME-assisted unit and Unit 101 can be redesignated as non-assisted.
    - The floating designation gives the owner some flexibility in assigning units and can help avoid stigmatizing the HOME-assisted units.
    - If the floating designation is used, the owner must ensure that the HOME-assisted units remain comparable to the non-assisted units over the affordability period in terms of size, features, and number of bedrooms.

The NSP rules do not directly use the term "NSP-assisted unit" but do incorporate this concept when considering the rents, unit quality restrictions, and ongoing affordability requirements. Grantees need to provide guidance to owners about how to meet these ongoing NSP requirements during the affordability period, and will need to designate units as fixed or floating in order to do so. This designation should be included in a written agreement with the property owner. When HOME and NSP funding is combined in the same project, the grantee should be sure that fixed or floating designation is the same for each of the two programs, to facilitate property management.

Income Targeting

Under HOME, all tenants must have annual gross incomes that are at or below 80 percent of the area median income at move-in and throughout the affordability period. In addition, the HOME "program rule" dictates that for all of the PJ's rental and TBRA projects combined, 90 percent of initial occupants must have incomes that are at or below 60 percent of area median income. Further, for projects with five or more HOME-assisted units, the HOME "project rule" requires that 20 percent of the units be rented to persons with incomes that are at or below 50 percent of area median income. The project rule is imposed throughout the affordability period. HOME requires the project owner to verify tenant income on an annual basis. If a tenant's income has increased and the tenant is no longer income-eligible, the owner must take certain steps to restore compliance with the HOME income requirements.

Under NSP, in order to meet the LMMH national objective, all tenants in an NSP-assisted unit must have annual gross incomes that are at or below 120 percent of area median income. In addition, across the entire NSP grant, 25 percent of funds must assist very low-income households (with annual gross incomes at or below 50 percent of area median income). These requirements last throughout the entire affordability period. This means that the income targeting requirements that are imposed on the unit upon initial occupancy are also imposed on a subsequent tenant during the affordability period. For instance, when a unit is occupied by a very low-income household, in order to meet the low-income targeting requirement, then any subsequent tenant of that unit must also be very low-income during the affordability period.

NSP grantees must verify the household's income-eligibility prior to initial occupancy. If the occupant moves out during the affordability period, the grantee (or the project owner) must verify the subsequent household's income-eligibility as well. Unlike HOME, however, NSP grantees are not required to certify the income-eligibility of occupants on an annual basis. For example, if an NSP-assisted rental unit is designated as a very low-income unit and its tenant vacates the building during the affordability period, the new tenant moving into the unit must also be very low-income.

There are two possible approaches to combining HOME and NSP in rental projects:

- When HOME and NSP funds are used together in a single assisted unit, then that unit is designated as both a HOME- and NSP-assisted unit. The more restrictive rules (mostly HOME) apply to that unit. This means that:
    - Occupancy would be restricted to households with annual gross incomes that are at or below 80 percent of area median income.
    - For any unit that the grantee designates as a Low HOME Rent unit under HOME, in order to meet the HOME "project rule," that unit must be restricted to very low-income occupants throughout the affordability period.
    - For any unit that the grantee designates as a very low-income unit under NSP, in order to meet the low-income targeting requirement, occupancy in that unit must be restricted to a very low-income household throughout the affordability period.
    - The project owner must charge the lesser of the HOME or NSP affordable rents for the unit. HUD issues High HOME Rents and Low HOME Rents, and the grantee defines the NSP affordable rents for its rental programs. When combining HOME and NSP, most grantees will adopt the HOME rent limits to simplify administration; however, if the NSP grantee adopts a different rent structure, the lowest rents will apply. Affordable rents are described in more detail later in this chapter.
- Using appropriate cost allocation methods (described in Chapter 2), the grantee can designate some units as HOME-assisted and other units as NSP-assisted. When this approach is used the HOME rules apply to the HOME units and the NSP rules apply to the NSP units.

Mixed-Income Housing

Both HOME and NSP allow jurisdictions to develop mixed-income housing (housing that combines both market-rate and assisted housing units). In developing mixed-income housing, the grantee must be sure that HOME and NSP funds are used to pay only for HOME- or NSP-eligible costs. HOME and NSP funds cannot be invested in units that will be occupied by households that are not income-eligible for that funding source. The grantee can pay for a proportionate share of the HOME- or NSP-eligible costs, including a share of the common costs, in accordance with the subsidy limitations and cost allocation methods for each program. If the units in the project are not comparable, actual development costs must be allocated to the units that are HOME- or NSP-assisted. Chapter 2 discusses cost allocation in detail.

The HOME and NSP programs can be readily combined for mixed-income housing so long as units that count as both HOME- and NSP-assisted meet the more stringent requirements.

Property and Neighborhood Standards

There is a difference between HOME and NSP when it comes to property standards.

HOME property standards are based on the HOME activity type, and are the same for rental housing and homeowner housing. In addition to these property standards, under HOME newly constructed rental housing is subject to site and neighborhood standards found at 24 CFR 983.6(b).

> The property standard requirements of each program are described in detail in Chapter 3. The requirements are substantially the same for rental and homeownership programs.

For rental housing, HOME requires the PJ to conduct periodic onsite monitoring and site inspections to ensure that the properties comply with applicable property standards throughout the affordability period.

Under NSP, there is no one set of established rules regarding property quality or habitability. NSP encourages regular inspections of the units. NSP2 and NSP3 impose a green standard to ensure a minimum level of energy efficiency in new construction and gut rehabilitation projects. The NSP grantee is required to establish rehabilitation standards for its rehabilitation programs and describe its adopted standards in its action plan. These rehabilitation standards must require compliance with applicable laws, codes, and other requirements related to housing safety, quality, and habitability. As part of its action plan description, the grantee should address whether these standards apply for the duration of the affordability period.

Long-Term Affordability for Rental Housing

Unlike CDBG, the NSP program imposes ongoing affordability restrictions. HUD allows NSP grantees to use the HOME rules as a “safe harbor,” or the grantee may establish more stringent rules. This section highlights the HOME affordability requirements and responsibilities after project completion. These rules apply to any project where the NSP grantee has adopted the HOME standards. If the NSP grantee adopts different requirements, it must ensure that the requirements of both programs are met.

Affordability Period

HOME- assisted rental units carry rent and occupancy restrictions for varying lengths of time. The duration of the affordability period depends upon the average amount of HOME funds invested per unit, as described in Exhibit 4-1.

Exhibit 4-1: Determining the Affordability Period for Rental Housing under the HOME Program

Activity	Average Per-Unit HOME or NSP $	Minimum Affordability Period
Rehabilitation or acquisition of existing housing	<$15,000/unit $15,000–$40,000/unit >$40,000	5 years 10 years 15 years
Refinance of rehabilitation project	Any $ amount	15 years
New construction or acquisition of new housing	Any $ amount	20 years

When HOME and NSP funds are combined in the same project, HUD encourages grantees to impose an affordability period that is based on the total Federal investment. This approach secures affordable housing in the community for longer periods of time, and is particularly important when the total Federal investment is substantial. The ***minimum*** affordability period that HUD requires, however, is determined for each program separately and the affordability periods run concurrently.

For example, assume a grantee invests $200,000 in HOME funds and $300,000 in NSP funds in a 10-unit rehabilitation project, where the PJ designates all the units as HOME- and NSP-assisted:

- If the affordability period is based on the total Federal investment:
  - Per unit subsidy of $50,000/unit ($500,000 total Federal investment / 10 units)
  - Affordability period is 15 years.
- If the affordability period is based on each program separately:
  - HOME affordability period is 10 years based on $20,000 HOME per unit subsidy ($200,000 HOME investment / 10 units)
  - NSP affordability period is 10 years based on $30,000 NSP per unit subsidy ($300,000 NSP investment / 10 units)
  - The two affordability periods run concurrently, so the total affordability period is 10 years.

Rent Requirements

Every HOME- or NSP-assisted unit is subject to rent limits designed to make rents more affordable throughout the applicable period of affordability.

Under the HOME Program, these rent limits are referred to as "HOME Rents," and represent the maximum rent that can be charged for a HOME-assisted unit. There are two types of HOME rents—High HOME Rents and Low HOME Rents:

- **High HOME Rents.** Maximum High HOME rents are the ***lesser of***:
  - The Fair Market Rents (FMRs) for existing housing
  - Thirty percent (30%) of the adjusted income of a household whose annual gross income equals 65 percent of area median income.
- **Low HOME Rents.** For properties with five or more HOME-assisted units, at least 20 percent of HOME-assisted units must have Low HOME rents which are no greater than the ***lesser of***:
  - Thirty percent (30%) of the tenant's monthly adjusted income

- Thirty percent (30%) of the annual gross income of a household whose income equals 50 percent of area median income
- If a project has a Federal or State project-based rental subsidy and the tenant pays no more than 30 percent of his or her adjusted income toward rent, the maximum rent may be the rent allowable under the project-based rental subsidy program.

HOME rents include utility costs. This means that if tenants pay for some or all utilities, the HUD-published HOME rent limit must be reduced by a utility allowance (determined by the PJ) in order to determine the maximum rent that can be charged for a unit. Exhibit 4-2 illustrates how this is done.

Exhibit 4-2: Using Utility Allowances

High HOME Rent Units		Low HOME Rent Units	
High HOME Rent	$728	Low HOME Rent	$577
Utility allowance	- $50	Utility allowance	-$50
Maximum HOME rent for 80% of units	**$678**	**Maximum HOME rent for at least 20% of units**	**$527**

Annually, the PJ must establish utility allowances and provide them to owners. The PJ may use either the utility allowance prepared by the local public housing authority (PHA), or it may prepare its own utility allowances. The owner must use the PJ-adopted utility allowance to adjust the HOME rent limits.

Project owners can propose utility allowances that differ from the PHA or PJ-established utility allowance on a project-specific basis when they can show that the actual utility costs of their property differs from the PJ's adopted utility allowances (such as in a building with energy efficiency features). The PJ must review and approve in writing any alternative utility allowance.

Based on changes in area income levels or market conditions, HOME rents, as calculated by HUD annually, may increase or decrease:

- New rents are effective upon receipt of the new HUD-published rent limits. Tenants must be given at least 30 days written notice before rent increases are implemented. Increases can only be made in accordance with the lease provisions. For example, rents may not increase until the tenant's lease expires.
- HOME rents may decrease due to changing market conditions or increasing utility costs. Owners are not required to decrease rents below the HOME rent limits in effect at the time of project commitment. However, if decreasing HOME rents reflect a change in market conditions for the area, owners may have to reduce rents in order to maintain occupancy.
- HUD may permit adjustments to the rent structure if the financial feasibility of the project is threatened. This is may be important to lenders providing financing to HOME-assisted projects. Note, however, that property owners cannot raise rents above the current HOME limits without a written waiver from HUD Headquarters. HUD is unlikely to grant this waiver unless the owner can demonstrate that the rent increase will not have a significant and detrimental effect on the existing tenants. That said, HUD rarely grants rent exceptions. Further, the ability to obtain a rent exception is based on market rents in the area — not on the operating expenses of the housing.

HOME program administrators must enforce rent and occupancy agreements through one of the following:

- Covenants running with the property
- Deed restrictions
- Other mechanisms approved by HUD.

Under the housing national objective, NSP units must initially be rented at an “affordable rent.” However, NSP does not define what “affordable “means; jurisdictions must adopt standards for what will be deemed “affordable” under their NSP programs and must make these standards public in their action plans. The grantee must consider what rent limits will be imposed to ensure affordability, and how those rents will remain affordable throughout the designated affordability period. Many grantees have adopted the HOME rent limits as a safe harbor to meet this requirement. Other options might include the Low Income Housing Tax Credit (LIHTC) rents or the HUD-published Fair Market Rents for the Section 8 Program.

If the grantee has elected to use the HOME or LIHTC rents as its standard, it must also follow the HOME or LIHTC rules regarding subtraction of tenant-paid utilities.

Income Targeting

Both NSP and HOME impose income-eligibility requirements for tenants in assisted rental projects.

HOME rental housing has two constraints on occupancy, discussed previously:

- **Program targeting rule** that specifies that 90 percent of the total families assisted through the PJ’s rental development and TBRA programs (counted together) have incomes that do not exceed 60 percent of the area median income. The balance of rental units and TBRA assistance must assist tenants with incomes that do not exceed 80 percent of the area median income. This rule applies to all funds expended from each fiscal year allocation; it is not project specific. It applies to initial occupancy only.
- **Project rule** that specifies that in projects with five or more HOME-assisted units, at least 20 percent of the HOME-assisted rental units must be occupied by families who have annual incomes that are at or below 50 percent of area median income. These very low-income tenants must occupy units with rents that are at or below the Low HOME Rent level. This rule applies throughout the affordability period.
    - Projects with fewer than five HOME-assisted units do not have to restrict the rents of any units to the Low HOME Rents or limit occupancy to tenants at 50 percent or below of the area median income.

> In practice, most PJs require that all HOME-assisted rental units be initially occupied by tenants with annual incomes at 60 percent of median or less, in order to meet the program targeting rule.

Under NSP, all NSP units must be initially rented to households with annual gross incomes that are at or below 120 percent of area median income. In addition, 25 percent of the grantee’s NSP funds must be targeted to households with annual gross incomes at or below 50 percent of area median income. Many NSP grantees find it easier to serve people below 50 percent of area median income with rental housing. This low-income targeting rule applies to the NSP program overall, not necessarily to each project. If a unit has been designated as part of the low-income set-aside, its occupants must continue to meet the very low-income criteria throughout the affordability period.

Note that if the rental housing is a single unit structure, its tenant must be LMMI. If the property is a duplex, one of the two occupant households must be LMMI. If the property has three or more units, the grantee must designate the number of NSP-assisted units based on the NSP cost allocation methods described in Chapter 2, and the occupants of the NSP-assisted units must be LMMI.

Both HOME and NSP:

- Use the same definitions of income to determine household income-eligibility. Chapter 1 provides guidance on income-eligibility determinations.
- Require that units remain affordable and occupied by income-eligible households throughout the affordability period.
- Require the grantee to verify a household's income prior to occupancy to determine income-eligibility.

HOME also requires that the PJ determine tenant household income-eligibility on an annual basis throughout the affordability period to ensure continued income-eligibility. If a tenant's income increases and the tenant is no longer income-eligible, the PJ must take certain steps to restore compliance in the property. When a tenant vacates a unit, the PJ is required to determine the income-eligibility of the subsequent tenant.

Unlike HOME, NSP grantees are ***not*** required to recertify income on an annual basis during the affordability period. The NSP grantee must verify the tenant's income prior to occupancy. When a tenant vacates a unit during the affordability period, the grantee must determine the income-eligibility of the subsequent tenant.

Ongoing Property Quality

Under HOME, properties must remain in standard condition throughout the affordability period. To verify this, HOME requires that the PJ monitor property quality after project completion and on a periodic basis throughout the affordability period. In order to verify compliance with property standards and to verify the information submitted by owners on tenants' incomes, rents, and other HOME rental requirements during a project's period of affordability, HOME rules require the PJ to conduct onsite inspections of HOME properties. The frequency of these inspections is based on the total number of units in a project as shown in Exhibit 4-3:

Exhibit 4-3: Frequency of Inspections Under HOME

Total Number of Units	Frequency of Inspections
1-4	Every 3 years
5-25	Every 2 years
26 or more	Annually

NSP does not require that grantees conduct periodic inspections of properties during the affordability period, but does recommend this practice. In addition, grantees may wish to impose inspection requirements as a part of their program design and their agreements with property owners.

When HOME and NSP funds are invested in the same project, the HOME ongoing inspection requirements apply.

Chapter 5: Applicability of Other Federal Requirements to HOME and NSP

There are a number of requirements that cut across most Federal programs, known as "cross-cutting" or "other" Federal requirements, including:

- *Environmental review*
- *Lead-based paint*
- *Fair housing and nondiscrimination*
- *Accessibility in housing*
- *Employment and contracting*
- *Tenant protections*
- *Acquisition and relocation*
- *Site and neighborhood standards*
- *Federal labor standards, including Davis-Bacon Act requirements*
- *Debarred contractors*
- *Conflict of interest*
- *Affirmative marketing*
- *Uniform administrative requirements and financial management.*

This chapter summarizes these other Federal requirements that apply to HOME and NSP, identifies any differences that may exist for the two programs, and describes what rules must be followed when the two sources of funds are combined.

Other Federal Requirements Applicable to HOME and NSP

Other Federal requirements that differ for HOME and NSP:

- Relocation and acquisition
- Site and neighborhood standards
- Davis-Bacon (Federal labor standards)
- Employment and contracting
- Conflict of interest
- Affirmative marketing
- Uniform administrative requirements and financial management

Other Federal requirements that are the same for HOME and NSP:

- Environmental review
- Lead-based paint
- Fair housing and nondiscrimination

Environmental Review Requirements

HOME and NSP are subject to the same environmental laws and regulations and, in general, these laws are implemented in the same way for both programs. The local government or the State must conduct what is commonly referred to as a "Part 58 environmental review" ***prior*** to investing either source of funds. Depending on the activity, the level of environmental review and related requirements will vary, as follows:

- **Exempt activities**
  - Includes planning, inspections, administration
  - Document the exemption, but no additional review is required.
- **Categorically excluded activities that are not subject to Part 58.5**
  - Includes tenant-based rental assistance, downpayment assistance, housing counseling, and predevelopment activities, among other things
  - Document the categorical exclusion not subject to Part 58.5; no additional review is required. Note, the Part 58.5 review addresses compliance with laws regarding historic properties, floodplains, or wetlands, etc.
- **Categorically excluded activities that are subject to Part 58.5**
  - Includes acquisition or disposition of land or real property; rehabilitation of one- to four-unit properties where density is not increased above four units, the footprint is not in floodplain or wetland, and the project does not involve land use change; and multifamily rehabilitation where density is not increased by more than 20 percent, there is no land use change, and the cost is less than 75 percent of replacement cost
  - Part 58.5 review is needed to determine if certain additional laws apply (e.g., historic properties, floodplains, wetlands, etc.). This type of review requires a notice of intent to request release of funds.
- **Any activity that is not exempt or categorically excluded**
  - Includes new construction of more than five units
  - A full environmental assessment is required to determine the project's impact on the environment. An environmental assessment requires additional information and analysis in addition to the information required in a review of categorically excluded subject to 58.5 activities. This level of review requires a notice of intent to request release of funds as well as a finding of no significant impact.

Due to the time constraints imposed by NSP, the grantee should use tiering if possible. Tiering can be used for categorically excluded activities that are subject to Part 58.5 and activities requiring a full environmental assessment. Tiering permits a general assessment of the impacts of an activity on the environment and allows the grantee to obtain the release of funds from conditions prior to the identification of a specific site. Site-specific impacts are analyzed once sites are known.

Unlike the regular CDBG program, NSP permits States to carry out activities directly, or to use a unit of general local government to carry out activities. How the State chooses to carry out its program activities impacts who has the authority to issue the Request for Release of Funds (RROF).

For both HOME and NSP, when the State uses a local government to carry out activities, the local government submits the RROF to the State, not to HUD. Alternatively, when the State carries out NSP activities directly, it must submit the RROF to HUD.

Using Conditional Contracts and Option Agreements to Secure Site Prior to Environmental Review

Prior to receiving environmental approval, a grantee can enter into either a "conditional contract" with a seller for the purchase of existing single family units (1-4 dwelling units) only, or an "option agreement" with the seller of a multifamily site or property that signifies the seller's willingness to remove the property from the market for an agreed period of time. The conditional contract or option agreement must stipulate that a grantee's willingness to proceed with acquisition of the property is contingent upon the completion of the environmental review.

Guidance on environmental review for nonprofits is available at the *NSP Resource Exchange* at http://hudnsphelp.info/index.cfm?do=viewFindaResourceDetails&resourceID=504.

Applicable Laws and Regulations

- 24 CFR 92.352 (HOME)
- 24 CFR 570.604 and 570.605 (CDBG)
- 24 CFR Part 58
- National Environmental Policy Act (NEPA) of 1969 and related laws and authorities and implementing regulations at 42 CFR 1500

Resources

NSP Environmental Clearance Requirements:
www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/nspenvironmentalreq.cfm

Environmental Review and the HOME Investment Partnerships Program. HUD Notice CPD 01-11, July 17, 2001: www.hud.gov/utilities/intercept.cfm?/offices/cpd/lawsregs/notices/2001/01-11.pdf

Tenant Protections

Two recently enacted laws aimed at protecting bona fide tenants in foreclosed dwellings and residential real property have set out new requirements of which an initial successor in interest (the successful purchaser at foreclosure; usually, the lender) to foreclosed property will need to be aware. ARRA provides tenant protection provisions that apply to NSP-funded acquisitions of foreclosed properties. Additionally, the Protecting Tenants at Foreclosure Act (PTFA) provides tenant protection provisions that apply broadly to foreclosed property.

The tenant protection requirements for both laws are similar, though separate and distinct.

NSP Tenant Protection Requirements under ARRA

With respect to the acquisition of a dwelling or residential real property foreclosed after February 17, 2009, the use of NSP funds to acquire such property is eligible only if the grantee can determine that the initial successor in interest has complied with the following requirements:

- Any bona fide tenant occupying the property under a lease in effect on or before the date of notice of foreclosure is entitled to remain through the end of his/her lease term and must be provided a minimum of 90 days' notice to vacate (Note: if the initial successor in interest (ISII) sells the unit to a buyer that will occupy the property as a primary place of residence, the ISII may terminate the lease effective on the date of sale, provided that a minimum of 90 days' notice to vacate is provided).

- Any bona fide tenant occupying the property without a lease or with a lease terminable at will under State law at the time of foreclosure must be provided with a minimum of 90 days' notice to vacate.
- In the case of any recipient of Section 8 assistance residing in qualified foreclosed housing at the time of foreclosure, the ISII shall be subject to the lease and housing assistance payments contract for the occupied unit.

For purposes of NSP, a dwelling or residential real property is "foreclosed" if any one of the following apply:

(a) The property's current delinquency status is at least 60 days delinquent under the Mortgage Bankers of America delinquency calculation and the owner has been notified of this delinquency.

(b) The property owner is 90 days or more delinquent on tax payments'.

(c) Under State, local, or tribal law, foreclosure proceedings have been initiated or completed.

(d) Foreclosure proceedings have been completed and title has been transferred to an intermediary aggregator or servicer that is not an NSP grantee, subrecipient, contractor, developer, or end user.

Defining a "Bona Fide Lease or Tenancy"

Both ARRA and PTFA protect the rights of bona fide tenants. A bona fide lease or tenancy is defined as:

- The mortgagor under the contract is not the tenant.

  NOTE: PTFA also requires that the child, spouse, or parent of the mortgagor under the contract is not the tenant.
- The lease or tenancy was the result of an arms' length transaction.
- The lease or tenancy required the receipt of rent that is not substantially less than fair market rent for the property.

  NOTE: PTFA states alternatively that the receipt of rent is not substantially less than fair market rent for the property, or that the unit's rent is reduced or subsidized due to a Federal, State, or local subsidy.

Prior to using NSP funds to acquire residential property, a grantee is required to perform due diligence to determine whether the ISII complied with ARRA's tenant protection requirements, if applicable. The grantee should keep adequate documentation of such compliance or the inapplicability of the requirements.

If the grantee finds that the requirements are applicable, but determines that the ISII did not or will not comply with the tenant protection requirements in ARRA:

- If the property is still occupied and no bona fide tenant has vacated the property, then the grantee can either:
  - Assume the obligations of the ISII and provide the required tenant protections. If the grantee assumes these obligations with respect to an occupied property, the grantee may

be required to provide relocation assistance in accordance with the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (URA), if a tenant will be displaced for the NSP-funded project.
  - Abandon the transaction. If compliance cannot be determined, NSP funds are not eligible for the acquisition of the property.

- If the property has been vacated contrary to the tenant protection requirements, then the grantee cannot assume those requirements and cannot acquire the property with NSP funds.

Tenant Protections and Relocation

If any tenant will be displaced for a HOME-funded or NSP-funded project, the grantee must be prepared to provide relocation assistance pursuant to the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970, as applicable. The tenant protection requirements described in this section are separate and apart from the requirements imposed by the URA.

Tenant Protections Arising Under the Protecting Tenants at Foreclosure Act

The PTFA applies to any federally-related mortgage loan, dwelling, or residential real property in the U.S. that is foreclosed upon after May 20, 2009, including projects funded under HOME, CDBG, and other federally-assisted programs. The PTFA will sunset on December 31, 2014, due to an extension in the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Under PTFA, the immediate successor in interest to residential property that was ***foreclosed after May 20, 2009*** **must:**

- Permit any bona fide tenant occupying the property under a lease in effect on or before the date of notice of foreclosure to remain through the end of his/her lease term and provide a minimum of 90 days' notice to vacate. (Note: If the ISII sells the unit to a buyer that will occupy the property as a primary place of residence, the ISII may terminate the lease effective on the date of sale, provided that a minimum of 90 days' notice to vacate is provided).
- Provide any bona fide tenant occupying the property without a lease or with a lease terminable at will under State law at the time of foreclosure with a minimum of 90 days' notice to vacate.

However, these requirements shall not affect the requirements for termination of any Federal- or State-subsidized tenancy or any State or local requirement that provides longer time periods or other additional tenant protections.

As with NSP, the HOME PJ must perform due diligence to determine whether foreclosed residential property which will be used in a HOME-funded project is in compliance with the PTFA tenant protections. The protections are not applicable when using properties that were foreclosed upon prior to May 20, 2009, or which are occupied by a person who is not a bona fide tenant (that is, the former mortgagor or the child, spouse, or parent of the former mortgagor).

Unlike NSP, if the PJ finds that the ISSI has not complied with the tenant protection requirements, the PJ should consult with its program counsel and HUD to determine whether the property could be used for a HOME-funded project.

Applicable Laws and Regulations

- American Recovery and Reinvestment Act of 2009 (Pub. L. 111–5, approved February 17, 2009)
- Protecting Tenants at Foreclosure Act of 2009 (PTFA) (Pub. L. 111-22, approved May 20, 2009)

Resources

Protecting Tenants at Foreclosure: Notice of Responsibilities Placed on Immediate Successors in Interest Pursuant to Foreclosure of Residential Property: http://portal.hud.gov/hudportal/documents/huddoc?id=09-17pihn.pdf

NSP Policy Alert! Guidance on NSP Tenant Protection Requirements Under the Recovery Act, August 2010: http://hudnsphelp.info/index.cfm?do=viewResourceDetailsFacetedSearch&ResourceID=30

Acquisition and Relocation

Federal acquisition and relocation laws are designed to provide uniform, fair, and equitable treatment of persons whose real property is acquired or who are displaced in connection with Federal and federally-assisted programs or projects, and to lessen the impact of displacement. These laws are:

- Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (generally known as the Uniform Relocation Act, or URA), as amended (42 U.S.C. 4601-4655) and implementing regulations at 49 CFR Part 24, 24 CFR 92.353 [HOME] and 24 CFR 570.606 [CDBG]. Note: NSP-specific URA guidance is available in the *Federal Register* notices cited at the end of this section.
- Section 104(d) of the Housing and Community Development Act of 1974 (HCD Act), as amended(42 U.S.C. 5304(d)), and implementing regulations at 24 CFR part 42, Subpart C, applicable to CDBG/NSP, HOME, UDAG, and Section 108 loans.

Residential Anti-Displacement and Relocation Assistance Plan

Section 104(d) of the HCD Act requires CDBG grantees and HOME PJs to adopt and follow a residential anti-displacement and relocation assistance plan. Implementing regulations at 24 CFR 42.325 provide further instructions. This requirement has been extended to NSP grantees via the *Federal Register* notice cited below.

Acquisition

As discussed, Section 2301(d)(1) of HERA requires the NSP grantee to acquire any foreclosed-upon home or residential property at a discount from the current market-appraised value of the home or property. Under URA, only voluntary acquisitions [those that meet the requirements at 49 CFR 24.101(b)(1) through (5)] can be made at less than fair market value.

Voluntary acquisitions meet the requirements that the acquiring agency must meet. These vary based upon the characteristics of the agency, including whether the agency has eminent domain authority. In any case, the owner of record must be notified in writing that Federal financial assistance will be used in the acquisition, the Agency's estimate of fair market value, and that the acquisition is not subject to eminent domain (in other words, if agreement cannot be reached through negotiation, the acquisition will not take place).

The URA does not require the Agency's estimate of fair market value to be based on an appraisal for voluntary acquisitions. However, under NSP, an appraisal of the foreclosed property is required in order to determine the current market-appraised value within 60 days of making the final offer. The owner must also be advised that, under NSP, the acquisition price must be at a discount from the current market-appraised value (the offer price should reflect the discount proposed by the buyer).

HOME funds, however, can be used to finance the acquisition cost of a jointly funded project, without triggering the NSP purchase price discount requirement. Further, HOME funds can be used for a voluntary or involuntary acquisition. All relevant URA requirements apply.

HUD has developed a number of sample guideforms to assist NSP grantees in meeting the acquisition notification requirements. These are available on the *NSP Resource Exchange* at www.hud.gov/nspta.

Relocation Assistance

HOME PJs and NSP grantees are required to minimize displacement that may result from assisted activities/projects. However, whenever a person (including a business or nonprofit organization) is permanently displaced due to acquisition, demolition, or rehabilitation of real property for a federally-assisted program or project, those persons may be eligible for relocation assistance under the URA. Alternatively, a lower-income person who is displaced from real property as a result of demolition or conversion of lower-income housing in connection with an activity assisted with NSP, HOME, CDBG, UDAG, or Section 108 funds may be eligible for relocation assistance and payments under section 104(d) of the HCD Act.

The grantee must determine the displaced person's occupancy in the affected property to assess the relocation assistance and payments, if any, the person is eligible for. An unlawful occupant who is displaced [as defined at 49 CFR 24.2 (a)(29)] is not entitled to relocation assistance and payments under the URA. The URA relocation assistance to be made available to residential occupants displaced by a HOME- or NSP-funded project may include any or all of the following:

- Specific written notices describing the project, its impact on the person, and eligibility or ineligibility for relocation assistance at various stages of the acquisition, rehabilitation, or demolition process
- Moving expense payments
- Advisory services
- Replacement housing payments.

Grantees and program participants are strongly encouraged to consult with their relocation specialists in the HUD regional offices when dealing with any potential relocation due to the complexity of the rules.

One-for-One Replacement

Under section 104(d) of the HCD Act, all occupied and vacant occupiable lower-income housing units that are demolished or converted to a use other than lower-income housing must be replaced one-for-one with comparable lower-income housing units. This requirement has been waived for NSP and HUD has implemented alternative requirements. For NSP, each grantee planning to demolish or convert any low- and moderate-income dwelling units as a result of NSP-assisted activities must submit certain information related to its demolition and conversion activities in its NSP action plan substantial amendment and report on actual accomplishments under the plan. Since this alternative requirement applies only to NSP, if NSP is combined with HOME or CDBG funds, the one-for-one replacement rules apply.

Applicable Laws, Regulations, and Program Requirements

- Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (generally known as the Uniform Relocation Act, or URA), as amended (42 U.S.C. 4601) and implementing regulations at 49 CFR Part 24
- Section 104(d) of the Housing and Community Development Act of 1974(HCD Act), as amended (42 U.S.C. 5304(d))
- 24 CFR 92.353 (HOME)
- 24 CFR 570.606 (CDBG) and 570.488 (State CDBG)
- 73 *Federal Register* 58330, at K-L (Oct. 6, 2008) (NSP1)
- NSP2 Notice of Funding Availability (May 4, 2009), http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/pdf/nsp2_nofa.pdf, at Appendices I, K-L
- 75 *Federal Register* 64322, at K-L (Oct. 19, 2010) (NSP3)

Resources

Real Estate Acquisition and Relocation in HUD Programs, online training module: www.hud.gov/offices/cpd/affordablehousing/training/web/relocation

NSP – Acquisition and Relocation Resources: www.hud.gov/offices/cpd/library/relocation/nsp/index.cfm

NSP Policy Alert! Guidance on NSP Appraisals -- Voluntary Acquisitions:
http://hudnsphelp.info/ index.cfm?do=viewResourceDetailsFacetedSearch&ResourceID=35

Site and Neighborhood Standards

Housing provided through the HOME Program must promote greater choice of housing opportunities. Newly constructed rental housing must meet site and neighborhood standards in accordance with 24 CFR 983.6(b), to ensure that the site is in an adequate location for assisted housing. Among other things, these site and neighborhood standards limit construction in areas that have a "minority concentration" or a "concentration of assisted housing" unless the housing construction is part of a comprehensive neighborhood revitalization effort. The PJ is responsible for conducting this site and neighborhood standards review.

NSP does not impose site and neighborhood standards. However, when HOME and NSP funds are used together for new construction of rental housing, the project is subject to the HOME site and neighborhood standards review.

Applicable Laws and Regulations

- 24 CFR 983.6(b) and 92.202 (HOME)

Davis-Bacon Act and Other Labor Requirements

A number of labor requirements apply to HOME and NSP projects. Most notably, the Davis-Bacon Act ensures that mechanics and laborers employed in construction work under federally-assisted contracts are paid wages and fringe benefits equal to the prevailing rates in the locality where the work is performed. It also provides for the withholding of funds to ensure compliance, and excludes from the wage requirement apprentices enrolled in a bona fide apprenticeship program, volunteers, and those contributing sweat equity. Prevailing wage rates are published by the U.S. Department of Labor.

The Davis-Bacon Act applies to both HOME and NSP, although there are some differences in how and when the law applies, summarized in Exhibit 5-1.

- **NSP.** Davis-Bacon applies when NSP funds are used to finance the construction or rehabilitation of housing structures with eight or more units.
- **HOME.** Davis-Bacon applies to every contract for the rehabilitation or new construction of housing that contains twelve or more HOME-assisted units.

Exhibit 5-1: Differences in the Applicability of Davis-Bacon under NSP and HOME

NSP	HOME
Eight or more total units	Twelve or more HOME-assisted units
NSP pays the new construction or rehabilitation costs	Project is for new construction or rehabilitation, but HOME funds can pay any eligible cost
Units must be located in a single ***structure*** (not in scattered sites)	Units must be part of a single project and covered in a single ***contract***, even if they are not in a single structure (e.g., scattered sites)

Once Davis-Bacon is triggered, the requirements apply to the entire project, not just the assisted units.

For both programs, the labor standards provisions and prevailing wage requirements must be included in all bid documents, contracts, and subcontracts.

The grantee is responsible to distribute current wage rates to its development partners.

The following labor law requirements also apply to HOME and NSP projects and must be cited included in all bid documents, contracts, and subcontracts:

- Contract Work Hours and Safety Standards Act, as amended (40 USC 327-333), which addresses safe and healthy working conditions for those employed on federally-assisted construction projects, including provisions for time and half for work in excess of 40 hours.
- Copeland (Anti-Kickback) Act (40 USC 276c), which governs the allowability of certain deductions from paychecks and requires all contractors to submit weekly payrolls and statements of compliance.
- Fair Labor Standards Act of 1938, as amended (29 USC 201, et. seq.), which establishes the basic minimum wage for all work, requires the payment of overtime at the rate of at least time and one-half, and establishes child labor standards.

Applicable Laws and Regulations

- Davis-Bacon Act (40 U.S.C. 276a - 276a-5)
- 24 CFR Part 70 (volunteers)
- Copeland Anti-Kickback Act (40 U.S.C. 276c)
- Contract Work Hours and Safety Standards At, as amended (40 U.S.C. 327-333)

- Fair Labor Standards Act of 1938, as amended (29 USC 201, et. seq.)
- 24 CFR 92.354 (HOME)
- 24 CFR 570.603 (CDBG)

Resources

HOME Cross-Cutting Federal Requirements (search "Labor"): www.hud.gov/offices/cpd/affordablehousing/lawsandregs/fedreq

Debarred Contractors

Regardless of the housing activity, HOME and NSP funds may not be used to directly or indirectly employ, award contracts to, or otherwise engage the services of any contractor or subrecipient during any period of Federal debarment, suspension, or placement of ineligibility status.

HOME PJs and NSP grantees are required to check the eligibility status of all contractors, subcontractors, and subrecipients against the Federal publication that lists debarred and ineligible contractors. This list can be found on the *Excluded Parties Listing System* at https://www.epls.gov

Applicable Laws and Regulations

- 24 CFR Part 24
- 24 CFR 92.350 (HOME)
- 24 CFR 570.609 (CDBG)

Resources

Excluded Parties Listing System: https://www.epls.gov

Conflict of Interest

Regardless of the activity undertaken, HOME PJs and NSP grantees must comply with certain conflict of interest provisions. These require jurisdictions to follow a written code of conduct that eliminates any real or perceived conflicts of interest in the procurement of goods and services, acquisition/disposition of real property, and contracting/awarding of funds. No employee, agent, consultant, officer, or elected official or appointed official of the grantee (or any of its State recipients or subrecipients), who is in a decision-making position related to the administration of program activities, may gain a financial interest or benefit from his or her participation in the affordable housing program.

The HOME Program also imposes conflict of interest requirements on nonprofit and for-profit owners, developers, and sponsors of HOME-assisted housing and prohibits their officers, employees, agents, consultants, or elected or appointed officials from occupying a HOME-assisted unit (excluding persons receiving funds to rehabilitate or acquire their principal residence, and onsite staff of rental housing).

Applicable Laws and Regulations

- 24 CFR 92.356 (HOME)
- 24 CFR 570.611 (CDBG)
- 24 CFR 85.36
- 24 CFR 84.42

Resources

HOME Program Conflict of Interest Provisions, HUD Notice CPD-98-09, July 14, 1998:
www.hud.gov/utilities/intercept.cfm?/offices/cpd/lawsregs/notices/1998/98-9.pdf

Lead-Based Paint Requirements

All housing that is assisted with HOME or NSP funds is subject to the lead-based paint requirements, found at 24 CFR Part 35. These rules apply to properties that were constructed prior to 1978, and require:

- Certain disclosures (in the form of notices) to occupants and applicants about any known or potential lead-based paint hazards
- Testing, assessing, and stabilization or reduction of lead-based paint hazards in accordance with established procedures, based on activity type and level of Federal assistance (for rehabilitation)
- Use of safe work practices
- Certain provisions included in all contracts and subcontracts related to lead-based paint
- Ongoing maintenance to monitor controls put in place to limit the hazards associated with the presence of lead-based paint.

Applicable Laws and Regulations

- 24 CFR 92.355 (HOME)
- 24 CFR 570.608 (CDBG) and 24 CFR 570.487(c) (State CDBG)
- Lead-Based Paint Poisoning Prevention Act of 1971 (42 U.S.C. 4821 et. seq.)
- Residential Lead-Based Paint Hazard Reduction Act of 1992 (42 U.S.C. 4851-4856) and implementing regulations at 24 CFR Part 35
- 24 CFR 982.401(j), except paragraph 982.401(j)(1)(i)

Resources

Lead Safe Housing Rule, online training:
www.hud.gov/offices/cpd/affordablehousing/training/web/leadsafe

HUD's Office of Healthy Homes and Lead Hazard Control: www.hud.gov/offices/lead

Requirements: NSP, Lead Hazard Control, and Healthy Homes Interventions:
www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/requirements/index.cfm

Employment and Contracting

The cross-cutting Federal employment- and contracting-related requirements fall into the following areas: equal employment opportunity, Section 3 and economic opportunity, prevailing wage, and minority and women business opportunity. In addition, NSP3 imposes a vicinity hiring preference.

Equal Employment Opportunity

HOME PJs and NSP grantees must comply with Executive Order 11246 (E.O. 11246). This Executive Order prohibits Federal contractors and subcontractors and federally-assisted construction contractors and subcontractors with contracts over $10,000 from discriminating in employment decisions on the basis of race, color, religion, sex, or national origin. Contracts and subcontracts over $10,000 must include language prohibiting said discrimination.

Section 3 and Economic Opportunity

HOME PJs and NSP grantees are subject to Section 3 of the Housing and Urban Development Act of 1968 ("Section 3"). This means that they (and any entity acting on their behalf) must provide opportunities for training and employment arising from the expenditure of Federal funds to low-income persons residing in the program service area, to the greatest extent feasible. They must also make available all opportunities to bid on contracting work to be performed in connection with the expenditure of Federal funds to Section 3 business concerns that are located in or owned by persons residing in the program service area.

Section 3 requirements apply to construction or rehabilitation projects where the amount of assistance[5] in the project exceeds $200,000 and for each contract or subcontract that exceeds $100,000. For projects with a combination of HOME and NSP funds (and no other Federal funding), this means when the total of the two sources of funds combined is $200,000 or more, then Section 3 applies. All contracts subject to the requirements of Section 3 must include the Section 3 clause verbatim that is contained at 24 CFR 135.38.

NSP3 Vicinity Hiring Requirement

The Dodd-Frank Act requires NSP3 grantees to hire employees who reside in the vicinity of NSP3-funded projects, and provide contracting opportunities to small businesses that are owned and operated by residents in this vicinity.

- The "vicinity" is each neighborhood identified by the NSP3 grantee as being an area of greatest need.
- A small business is one that meets the criteria set forth in Section 3(a) of the Small Business Act (see 42 U.S.C. 5302(a)(23).

HUD has adopted the Section 3 applicability thresholds to implement this requirement, described above. This means that the NSP3 vicinity requirement applies to any project to which the Section 3 requirements apply.

Should the vicinity hiring preference requirements conflict with the Section 3 requirements, the NSP3 requirements prevail.

In a project that combines both HOME and NSP3 funds, the vicinity hiring requirement applies. The vicinity hiring requirement does not apply to projects funded with NSP1 or NSP2 funds.

Outreach to Minority / Women Business Enterprises

HOME PJs and NSP grantees must comply with procurement requirements [found at 24 CFR 85.36(e)] that require them to undertake specific outreach activities to notify minority and women business enterprises (MBE/WBE) of contracting opportunities. In addition, the HOME regulation requires PJs to establish procedures to oversee a minority outreach program to ensure the inclusion of minorities and

5 Assistance refers to all Section 3 covered assistance, which includes most Federal funding sources. The specific list of what constitutes "Section 3 covered assistance" is found at 24 CFR 135.

women, and entities owned by minorities and women, in the participation of contracting opportunities with the PJ.

When HOME and NSP funds are combined, both sets of requirements apply. These requirements and procedures should be prescribed in all contracts and subcontracts.

Applicable Laws and Regulations

- Executive Order 11246 and implementing regulations at 41 CFR Part 60
- 24 CFR 105(a) and (b)
- Section 3 of the Housing and Urban Development Act of 1968 (12 U.S.C. 1701u) and implementing regulations at 24 CFR Part 135
- 24 CFR 607 (CDBG) and 24 CFR 570.487(d) (State CDBG)
- Executive Orders 11625, 12432, and 12138
- 24 CFR 85.36(e)
- 24 CFR 92.350, 92.351(b), and 92.508(a)(7)(1)(B) (HOME)
- Section 1497 of the Wall Street Reform and Consumer Protection Act of 2010 (Pub. L. 111–203, approved July 21, 2010)

Uniform Administrative Requirements

HOME PJs, NSP grantees, their subrecipients, HOME State recipients, NSP recipients, and other governmental entities to which grantees provide Federal funds must comply with certain uniform administrative requirements. The requirements differ slightly for governmental entities and nonprofit organizations. In general, these requirements include:

- **Cost Principles.** OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* and OMB Circular A-122, *Cost Principles for Nonprofit Organizations* establish the principles and standards to provide a uniform approach for determining allowable costs under Federal grants. As their names suggest, Circular A-87 applies to governmental entities, and Circular A-122 applies to nonprofit organizations.
- **Financial management systems and procurement.** Certain provisions in 24 CFR Part 85 (for governmental entities) and 24 CFR Part 84 (for nonprofit organizations) set forth uniform requirements for financial management systems, procurement, reports and records, and grant close-outs for recipients of Federal grant funding.
- **Audit requirements.** HOME PJs, NSP grantees, their subrecipients, HOME State recipients, and NSP recipients are required to have audits. Audit thresholds and requirements are outlined in OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*.

Note, these administrative requirements do not apply to all nonprofit organizations; they apply only to those nonprofit organizations that are subrecipients. However, the requirements at 24 CFR 84.21, “Standards for Financial Management Systems” apply to HOME CHDOs who are acting as an owner, developer, or sponsor of HOME-assisted housing.

When combining HOME and NSP funds, the uniform administrative requirements apply to those nonprofits that qualify as subrecipients under either program. Chapter 2 reviews when a nonprofit organization is a subrecipient under HOME and NSP.

Applicable Laws and Regulations

- Certain provisions of 24 CFR Part 85, as listed at 24 CFR 92.505(a) for HOME and 24 CFR 570. 502(a) for CDBG
- Certain provisions of 24 CFR Part 84, as listed at 24 CFR 92.505(b) for HOME and 24 CFR 570. 502(b) for CDBG
- OMB Circulars A-87, A-110, A-122, and A-133

Appendices

Appendix 1: Comparison of Key HOME and NSP Requirements

	HOME	NSP
Organizational Issues		
Recipient	PJ (States, counties, localities, consortia).	Designated NSP grantee (State and local governments; and, for NSP2 only, nonprofit organizations or consortia of nonprofit organizations).
Key Partners	CHDOs, nonprofit and for-profit housing developers, private lenders.	CBDOs, nonprofit and public organizations, nonprofit and for-profit housing developers, nonprofit organizations serving the development needs of non-entitlement areas, private lenders.
Projects Under State Programs	States can directly undertake projects or they can work through local governments or nonprofits. States can fund projects anywhere in the State, including in PJs.	Unlike regular CDBG, States can directly undertake projects or they can work through local governments or nonprofits. States can fund projects anywhere in the State, including in entitlement areas. (*Federal Register*, 10/6/08, p. 58336, Item F)
Special Nonprofits	Community Housing Development Organizations (CHDOs): nonprofit development organizations with a board that is at least 1/3 representative of low-income residents. (24 CFR 92.2, definition of CHDO)	Community Based Development Organizations (CBDOs) and nonprofit organizations serving the development needs of non-entitlement areas. These organizations undertake community economic development, neighborhood revitalization, and/or energy conservation. (24 CFR 570.204)
Nonprofit Set-Aside	PJs must spend at least 15% of their annual allocations on development projects undertaken by CHDOs. (24 CFR 92.300(a))	None.
Subrecipients *Chapter 2 discusses the differences in the definition of subrecipient in detail.*	Any public agency or nonprofit organization selected by the PJ to administer all or part of a HOME activity on the PJ's behalf. (24 CFR 92.2, definition of subrecipient)	A nonprofit or public agency that assists a grantee or another subrecipient to administer all or a portion of the NSP program, including any nonprofit organization or unit of general local government that is awarded funds by a State; and including any land bank that receives NSP funds from a grantee or another subrecipient. A subrecipient is defined at 24 CFR 570.500(c), as follows: "*Subrecipient* means a public or private nonprofit agency, authority, or organization, or a for-profit entity authorized under 570.201(o), receiving CDBG funds from the recipient or another subrecipient to undertake activities eligible for such assistance under subpart C of this part."

	HOME	NSP
Funding Issues		
Timelines	2-year commitment, 5-year expenditure deadlines. (24 CFR 92.500(d))	NSP1: 18-month use (obligation), 4-year expenditure deadlines. (*Federal Register*, 10/6/08, p. 58340, Item M) NSP2 and NSP3: 50% expenditure of allocated funds within two years, and 100% within three years. (*Federal Register*, 10/19/09, Section II.M.)
Match	HOME PJs must contribute at least 25¢ for every $1 of HOME funds expended per program year. (24 CFR 92.218-92.222)	None.
Eligible Activities		
Eligible Activities	HOME funds can only be used to support affordable housing activities and projects. (24 CFR 92.1 and 92.2). Acquisition, rehabilitation and new construction of rental and homeownership housing, direct homebuyer assistance (loans, grants, down payment and closing cost assistance), tenant-based rental assistance. (24 CFR 92.205 through 92.212) No non-housing related activities. No assistance to public housing. (24 CFR 92.214)	**(A)** Establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties; **(B)** Purchase and rehabilitation of homes and residential properties that have been abandoned or foreclosed upon, in order to sell, rent or redevelop such homes and properties; **(C)** Establish and operate land banks for homes that have been foreclosed upon; **(D)** Demolish blighted structures; and **(E)** Redevelop demolished or vacant properties. (*Federal Register*, 10/6/08, p. 58337, Item H, as amended by *Federal Register*, 6/19/09, p. 29224) Under NSP2 and NSP3 grantees can: ▪ Undertake redevelopment for housing only ▪ Use up to 10% of its funds for demolition, unless a greater amount is approved by HUD. (*Federal Register*, 10/19/10, Section II.H.3f.)
Refunding of Assisted Projects	No assistance to projects already funded with HOME during the affordability period after the first year. (24 CFR 92.214(a)(6))	Can provide assistance to project already assisted with NSP, as long as new activity is NSP-eligible; new affordability period may apply
Administrative Costs	Eligible under 24 CFR 92.207. Capped at 10%.	General administration and planning costs may not exceed 10% of the NSP grant plus program income. (*Federal Register*, 10/6/08, p.58337, Item H(4))

	HOME	NSP
Low-Income Targeting		
Income Definition	Can choose from among three definitions of income: Part 5; IRS; Census long form. (24 CFR 92.203(b))	Same as HOME except that State grantees can choose one of these three or their own definition. (24 CFR 570.3, definition of income and 24 CFR 570.481)
Income Targeting—Households Served	HOME funds exclusively serve low-income households (<80% area median income). (24 CFR 92.1)	100% of funds must meet a low-, moderate-, and middle-income (LMMI) national objective. LMMI for NSP is up to 120% of area median income. Three national objectives are possible: low/mod housing; low/mod limited clientele; and low/mod area. The CDBG slums/blight and urgent needs objectives cannot be used. 25% of NSP funds must be used to house individuals or families households at 50% of area median income and below. (*Federal Register*, 10/6/08, p. 58335, as amended by *Federal Register*, 6/19/09, p. 29227; *and Federal Register*, 10/19/09, Section II.E.)
Income Targeting -- Rental Units	HOME allows assistance to be targeted toward specific units. Thus the HOME units could be a small percentage of the entire units within a project. Rental projects with five or more HOME-assisted units must rent 20% of the units to very low-income households. Initially, 90% of the households assisted with rental or TBRA funds must have annual incomes that are at 60% of area median income or below. (24 CFR 92.216).	Single unit structures must be occupied by a LMMI household. In a two unit structure, one of the two units must be occupied by a LMMI household, although NSP funds could only be used to support the unit occupied by a LMMI household. In a structure with three or more units, the grantee can choose one rule: (1) 51% of the units occupied by income-eligible; (2) HOME cost allocation approach at 24 CFR 92.205(b); or (3) NSP “unit approach” where the proportion of units occupied by LMMI to the total number of units is equal to or greater than the proportion of NSP costs paid to the total development costs. If the grantee assists only a single unit in multi-unit structure (such as one condominium), only the assisted unit must meet national objective (i.e., be occupied by a LMMI household).
Affordability		
Affordability Period	Applies to homebuyer and rental projects. 5–20 years depending on activity type and funding amount. (24 CFR 92.252, 92.254)	NSP grantee is required to determine how it will ensure continued affordability for NSP-assisted housing in substantial amendment to its action plan. (*Federal Register*, 10/6/08, p. 58334, Item B(3)) Grantee can adopt own definition or adopt HOME affordability period, considered to be minimal compliance. (*Federal Register*, 10/6/08, p. 58334, Item B(3)(a))

Rents	High and Low HOME Rents are specified for low-and very low-income tenants. (24 CFR 92.252(a) and (b))	NSP grantee must define "affordable rents" in its substantial amendments to its action plan. HOME rent standards are considered to be minimal compliance. (*Federal Register*, 10/6/08, p. 58334, Item 3(a))
Unit Requirements		
Unit Quality	HOME property standards: Local rehabilitation standards (for rehabilitation), and State/local codes or standards or, if none exist, the national model code, and Model Energy Code (for new construction). (24 CFR 92.251)	NSP grantee must describe the housing rehabilitation standards that apply to NSP-assisted activities in substantial amendments to its action plan. Grantee also determines what rehabilitation standards apply during the affordability period, if any. NSP2 and NSP3-funded gut rehabilitation and new construction must also meet green building standards. [Energy Star Qualified New Homes for buildings with up to three stories, and the American Society of Heating, Refrigerating, and Air-Conditioning Engineers (ASHRAE) Standard 90.1–2004, Appendix G plus 20 percent, for mid- and high-rise buildings]. (*Federal Register*, 10/19/09, Section II.I.)
Minimum Investment	Minimum HOME investment is an average of $1,000 per unit for project. (24 CFR 92.205(c))	No minimum required.
Subsidy Limit	Capped at the 221(d)(3) limits. Costs must be reasonable. (24 CFR 92.250(a))	No maximum subsidy. Costs must be reasonable and subsidy level must be appropriate, as determined by a thorough underwriting analysis.
Maximum Property Value	Applies to homebuyer homes and is typically based on 203(b) limits. (24 CFR 92.254(a)(2))	No maximum property value but NSP grantees must adhere to property discount requirements when acquiring foreclosed upon properties. Foreclosed upon properties must be purchased at a discount of at least 1% below current fair market value. (*Federal Register*, 6/19/09, p. 29225, Item Q)
Ongoing Compliance		
Ongoing Monitoring	Must monitor compliance with program rules and terms of written agreement. Must also monitor rental properties during the affordability period. Must ensure that homebuyer properties meet resale or recapture provisions. (24 CFR 92.504 and 92.508)	Must document compliance with eligible activity, national objective, and terms of written agreement. Must ensure and enforce the affordability period. (*Federal Register*, 10/6/08, p. 58341, Item O)

Reexaminations of Income	Incomes need to be reexamined for HOME-assisted units annually, and re-verified with source documentation every five years—all new tenants in HOME units must be low-income (80 percent or lower of the area median income). (24 CFR 92.252(h))	Must examine income of any new tenant during the affordability period to document continued income-eligibility. Not required to recertify income of existing tenants on an annual basis.
Unit Inspections	Rental units must be inspected during the affordability period; inspection schedule is based on size of the project. Units occupied by persons using HOME tenant-based rental assistance must be inspected annually. (24 CFR 92.504(d))	None specified, but should maintain unit during affordability period. NSP recommends regular inspections as well.
Program Income	Gross income received by PJ, State recipient, or subrecipient directly generated by: ▪ Use of HOME funds ▪ HOME matching contributions. Funds generated through the use of HOME funds that return to these entities are PI in perpetuity. Applies even if the funds are received after the end of the affordability period. Does not include HOME funds that are recaptured from home sales during the affordability period, pursuant to the PJ's recapture provisions. (24 CFR 92.2, definition of program income)	Gross income received by grantee, unit of general local government, or subrecipient directly generated by the use of NSP funds, including: ▪ Proceeds from the sale/lease of property acquired, rehabilitated, redeveloped with NSP ▪ Principal and interest on NSP loans ▪ Revenue returned by non-subrecipients ▪ Net operating income from rental properties if a subrecipient or grantee. (NOI is not considered program income if owner is classified by grantee as a developer) Includes NSP funds that are recaptured from home sales during the affordability period, pursuant to the grantee's recapture provisions. Note, program income received after 7/30/13 is not required to be returned to HUD as originally required by HERA, and may continue to be used for NSP-eligible activities. (24 CFR 570.500(a), definition of program income; and *Federal Register*, 6/19/09, p. 29224, Substantial Revision B)

Appendix 2: HOME Cost Allocation Methodology

The approach to determine HOME cost allocation depends on whether or not the project units are comparable, meaning similar in size, quality, number of bedrooms, and amenities. If units are comparable, a pro-rata method of cost allocation can be used or the actual cost method can be used. If units are not comparable, the actual cost method must be used.

In order to determine cost allocation, the PJ must determine at least one of two facts about the project--either the number of HOME units and the total number units in the project ***or*** the intended level of HOME investment and the total eligible development costs for the project. Once either the number of HOME units or the planned HOME investment is known, the PJ may use that information to determine the cost allocation.

Cost Allocation Methodology to Determine Maximum HOME Subsidy (Number of HOME-Assisted Units is Known)

Pro-Rata Share Cost Allocation Method: Comparable HOME Units

If all the units in a multi-unit project are comparable, the PJ may determine the HOME "fair share" of costs based on the portion of units that are to be HOME-assisted. (In rental housing, often these HOME units are floating but this is not always the case.) The percentage of the total HOME-eligible costs that may be paid by HOME is equal to the percentage of units that are HOME-assisted. In general, the cost allocation equation may be described as:

$$\frac{HOME\ UNITS}{TOTAL\ UNITS} = \frac{HOME\ INVESTMENT}{TOTAL\ ELIGIBLE\ DEVELOPMENT\ COSTS}$$

It is important to note that this equation is based on total ***eligible*** costs, not all costs. If the project's development budget includes items that are not eligible under HOME, such as swimming pools or luxury amenities, these costs must be subtracted before the percentage can be determined. Once the PJ determines the HOME fair share, it must compare that amount to the Section 221(d)(3) maximum subsidy limit in order to ensure that the HOME investment is within those limits. The example below

Pro-Rata Share Cost Allocation Example – Comparable Units

Total development costs	$1,500,000
Ineligible costs (pool repair)	$50,000
Total eligible costs ($1,500,000 - $50,000)	$1,450,000
Total number of units	8
HOME-assisted units	3
Section 221(d)(3) limit	$160,000
HOME share % (3 HOME units/8 total units)	37.5%
% of HOME share of costs $1,450,000 X 37.5% =	$543,750
$160,000 (maximum subsidy) X 3 units =	$480,000

Maximum investment is $480,000, assuming that the subsidy layering analysis supports this.

illustrates this approach.

Actual Cost Method of Cost Allocation: Non-Comparable HOME Units

If all the units in a rental project are ***not*** comparable, the cost allocation must be determined by assessing the actual unit construction costs for the HOME-assisted units. The mathematical approach to determining fair share cannot be used. The PJ or the architect/engineer must determine the specific and actual costs for the HOME units, based upon the work write-ups for these units. Once these unit costs are known, HOME can then pay for its "fair share" of the common costs such as the acquisition, eligible soft costs, or common areas such as lobbies, elevators, or roof. The PJ must always ensure that the HOME investment does not exceed the Section 221(d)(3) maximum subsidy limit. (In rental housing, these non-comparable units must always be fixed rather than floating units.)

In general, the cost allocation equation for non-comparable units may be described as:

$$Total\ eligible\ costs\ for\ HOME\ units + \left[\frac{HOME\ unit\ square\ foot}{Total\ unit\ square\ foot}\right] \times Eligible\ common\ costs$$

The example below illustrates this non-comparable approach.

Actual Cost Method of Cost Allocation Example – Not Comparable Units

Total development costs	$1,500,000
Cost of the HOME units	$400,000
Total common costs	$300,000
Ineligible costs (pool repair)	$50,000
Total eligible common costs ($300,000 - $50,000)	$250,000
Total number of units	8
HOME assisted units	3
Square footage of all units	12,000 S.F.
Square footage of HOME units	2,700 S.F.
221(d)(3) limit (max per unit subsidy)	$160,000
HOME share of common costs % (2,700 /12,000)	22.5%
Eligible common costs X % of HOME share ($250,000 X 22.5%)	$56,250
Total HOME costs ($56,250 in common costs + $400,000 in total HOME unit costs) =	$456,250
$160,000 (221(d)(3) limit) X 3 units =	$480,000

Maximum investment is $456,250, assuming that the subsidy layering supports this.

Cost Allocation Methodology to Determine the Number of HOME-Assisted Units (HOME Investment Is Known)

When the amount of the HOME investment and the total development costs are known, the same cost allocation formula can also be used to determine the minimum number of HOME-assisted units the PJ must designate. The number of HOME-assisted units in a given project must be specified at project commitment. HOME rules create a floor for the number of HOME-assisted units a project must have. This floor is based on the proportional share of total eligible costs to be paid with HOME funds. Obviously, the PJ may designate more HOME units than the minimum required; some projects may consist of only HOME-assisted units. The fair share calculation of the minimum number of HOME units is only relevant when evaluating comparable projects. When evaluating non-comparable projects, the specific HOME-assisted units must be known and identified because these will be fixed (rather than floating) HOME units.

The formula for calculating the minimum number of comparable HOME-assisted units is the same as above. However, in this instance the PJ is solving for the minimum number of HOME units, not the minimum HOME investment:

$$\frac{HOME\ UNITS}{TOTAL\ UNITS} = \frac{HOME\ INVESTMENT}{TOTAL\ ELIGIBLE\ DEVELOPMENT\ COSTS}$$

As was previously the case, the PJ must ensure that it also does not invest more than the maximum per unit subsidy (Section 221(d)(3) limit). The case below provides an example of this calculation.

Determining Minimum Number of HOME-Assisted Units Example – Comparable Units

Total development costs	$1,500,000
Ineligible costs (pool repair)	$50,000
Total eligible development costs ($1,500,000 - $50,000)	$1,450,000
HOME investment	$700,000
Total number of units	8
221(d)(3) limit (max per unit subsidy)	$270,000
HOME share of costs % ($700,000 /$1,450,000)	48.2%
HOME share of units (8 units X 48.2%)	3.86, or 4 units (round up)
HOME share of units based on max per unit subsidy	
$700,000 (HOME $)/$270,000 maximum per unit subsidy=	2.59, or 3 (round up)

The minimum HOME units are 4, assuming that this level of investment is supported by the subsidy layering analysis.

For more information on cost allocation, see *Allocating Costs and Identifying HOME-Assisted Units in Multifamily Projects*, see HUD Notice CPD-98-02, March 18, 1998 at www.hud.gov/offices/cpd/affordablehousing/lawsandregs/notices.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT