

# DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

## 24 CFR Parts 5 and 200

[Docket No. FR-4452-F-02]

RIN 2501-AC45

### Uniform Physical Condition Standards and Physical Inspection Requirements for Certain HUD Housing; Administrative Process for Assessment of Insured and Assisted Properties

**AGENCY:** Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

**ACTION:** Final rule.

**SUMMARY:** This rule establishes for multifamily housing certain administrative processes by which HUD will notify owners of HUD's assessment of the physical condition of their multifamily housing; the owners, under certain circumstances, will be provided an opportunity to seek technical review of HUD's physical condition assessment of the multifamily housing; and HUD may take action in certain cases where the housing is found not to be in compliance with the physical condition standards. This rule follows publication of a November 26, 1999 proposed rule and takes into consideration public comment received on the proposed rule.

**DATES:** *Effective Date:* January 8, 2001.

**FOR FURTHER INFORMATION CONTACT:** For further information about multifamily issues covered by this rule, contact: Kenneth Hannon, Office of Housing, Department of Housing and Urban Development, 451 Seventh Street, SW, Room 6274, Washington, DC 20410; telephone (202) 708-0547, ext. 2599 (this is not a toll-free number).

For further information about the scoring methodology or the technical review process, contact: Wanda Funk, Real Estate Assessment Center, Department of Housing and Urban Development, 1280 Maryland Avenue, SW, Suite 800, Washington, DC, 20024; telephone Technical Assistance Center at 1-888-245-4860 (this is a toll-free number).

For both offices, persons with hearing or speech impairments may access that number via TTY by calling the Federal Information Relay Service at 1-800-877-8339.

#### SUPPLEMENTARY INFORMATION:

#### I. Uniform Physical Conditions Standards and Uniform Physical Inspection Protocol

This final rule follows publication of a November 26, 1999, proposed rule (65

FR 66539) and builds on the rule issued by HUD on September 1, 1998 (63 FR 46566), that established uniform physical condition standards for public housing, and housing that is insured and/or assisted under certain HUD programs (collectively, HUD properties). The September 1, 1998, final rule also established a uniform physical inspection protocol, based on computerized software developed by HUD, that allows HUD to determine compliance with these standards. The uniform physical condition standards are intended to ensure that HUD program participants carry out their legal obligations to maintain HUD properties in a condition that is decent, safe, sanitary and in good repair. The uniform inspection protocol is intended to assure that, to the greatest extent possible, there is uniformity and objectivity in the evaluation of the physical condition of HUD properties.

The preamble to the November 26, 1999, proposed rule provided a detailed overview of HUD's proposal for the administrative process for the assessment of insured and assisted housing, and the basis for HUD's proposal. The preamble to this rule does not repeat that information.

#### II. Significant Changes Made at This Final Rule Stage

The following highlights significant changes made to the proposed regulations at this final rule stage.

- HUD amends § 5.705 to remove paragraph (b). Paragraph (b) of this section provides that HUD will notify the public when the inspection software for HUD's physical inspection protocols and the accompanying guidebook are issued and available. This section further provides that HUD will publish a notice in the **Federal Register** to inform the public when the software and guidebook are available, and the notice will provide 30 days within which covered entities must prepare to conduct inspections in accordance with part 5, subpart G. The notice described by § 5.705 was published earlier in the **Federal Register**. Since HUD has published the notice in accordance with § 5.705(b), paragraph (b) is no longer relevant and is removed by this rule.

- HUD amends § 200.853, which lists the HUD multifamily programs to which HUD's physical condition standards and physical inspection protocols are applicable. For the Section 241 Program (Section 241 of the National Housing Act—Supplemental Loans for Multifamily Projects), HUD clarifies that Section 241 properties are subject to inspection, except where the primary (first or senior) loan is insured or

assisted by HUD under another program listed in § 200.853. Without this clarification, the regulatory language would subject Section 241 properties to two inspections—one inspection under the Section 241 program, and one inspection under another program covered by this subpart.

- HUD amends § 200.855 to add a new paragraph (b) to clarify that for a property with more than one HUD insured loan, only the first mortgage lender is required to conduct the physical inspection. The second mortgage lender, however, must be provided a copy of the physical inspection report by the first mortgage lender.

- HUD also amends § 200.855 to add a new paragraph (c) that specifies when the responsible entity must perform the required physical inspection. For example, all annual inspections must be performed in the following calendar year and no earlier than 9 months and no later than 15 months from the date of the last inspection. Comparable time periods are provided for inspections that must occur every two years and those that must occur every three years.

This new paragraph (c) also provides that a newly endorsed multifamily property will receive its first physical inspection no earlier than 21 months but not later than 27 months from the date of final endorsement, but in no event shall the inspection be performed after the end of the calendar year following the two year anniversary date of final endorsement.

HUD is aware that linking the timing of the inspection to the calendar year may constrain the flexibility to schedule some inspections, but HUD believes that coordinating the timing of the inspection with the end of a calendar year is important to ensuring that information required to be reported by the end of a calendar year is reported by such deadline and properties are scheduled for inspection at their appropriate cycle.

On the subject of when the responsible entity must conduct its physical inspection, HUD advises in this preamble and in the notice published elsewhere in today's edition of the **Federal Register** that HUD will complete all annual inspections required of properties covered by this part through December 31, 2000. Responsible entities should begin preparations for either one year and two year cycle inspections in accordance with this rule.

- HUD amends § 200.857 to provide for designation of properties as either standard 1, standard 2, or standard 3, on the basis of fixed points, not percentile

groupings as provided by the proposed rule. Properties receiving scores of 90 points or higher on a physical inspection will be designated as standard 1. Properties receiving scores of 80 points or higher but less than 90 on a physical inspection will be designated as standard 2. Properties receiving scores of less than 80 will be designated as standard 3. Because scores can include fractions (e.g. 89.3), a score that includes a fraction below one half point will be rounded down, and a score that includes a fraction of one half point or higher will be rounded up. For example, a property score of 89.5 or 89.6 will be rounded to 90 and the property will be designated as standard 1. A property score of 89.4 will be rounded down to 89 and the property will be designated as standard 2.

HUD received considerable comment on the method provided in the proposed rule by which properties are designated as standard 1, 2 or 3. The commenters opposed designation on the basis of percentile groupings and recommended that designation be made on the basis of fixed points. HUD agreed with the recommendations of the commenters and has made this change at this final rule stage. HUD recognizes that fixed points provide a clear standard, understandable by those being rated at the time they are rated. HUD also recognizes that fixed point scores provide additional incentive for improvement since with a fixed score, owners know that improvement to a cut point will result in a less burdensome inspection schedule. HUD welcomes any additional comments on the change from a percentile approach to a fixed point approach in the designation of properties as standard 1, 2, or 3, and may make adjustments on the basis of comments received.

- HUD amends paragraph (a) of § 200.857 to remove reference to REAC's baseline physical inspection of properties. The baseline review has been completed.

- HUD amends paragraph (c) of § 200.857 to clarify that the 72 hours to report correction of exigent health and safety violations refers to 3 business days from the date of the physical inspection.

- HUD amends paragraph (d)(4) of § 200.857 to revise the definition of "significant improvement" to mean the correction of a material error, asserted by the owner, which causes the score for the owner's property to cross an administratively significant threshold (for example, the property would be redesignated from standard 3 performing to standard 2 performing or from standard 2 performing to standard

1 performing), or result in an increase of 10 points or more (new language is highlighted).

- HUD amends paragraph (e) of § 200.857 to provide that if an owner requests an adjustment of the physical condition score based on considerations other than those for technical review after the physical inspection report has been submitted to the owner (either electronically through the internet or by mail), the owner must make a request for adjustment to REAC within 45 days following submission of the report to the owner by REAC. HUD may, but is not required to consider requests made after that period. However, since the items that may be requested as a basis for score adjustment are unique and not subject to addition and change from period to period, owners are strongly encouraged to request database corrections prior to inspections. In this way, the inspection results can fully consider approved corrections, eliminating score deductions for approved database corrections and the need for post report adjustments. HUD also amends this paragraph to provide that requests for database adjustments are to be directed to REAC. The proposed rule provided for requests to be submitted to the applicable HUD Field Office. Since REAC, however, is the point of contact for requests for technical review, HUD determined that REAC is also the appropriate point of contact for requests for database adjustments.

- HUD adds a new paragraph (f) to § 200.857 to clarify when an owner's physical condition score becomes final. This new paragraph also notes that final physical condition scores will be made public by HUD, and the owner must make its physical inspection information (the physical inspection report, scores) available to residents to review upon request during business hours. Paragraph (f), (g) and (h) in the proposed rule are redesignated (h), (i) and (j), respectively.

- HUD adds a new paragraph (g) to § 200.857 to require an owner to notify its residents of upcoming physical inspections of the owner's property and to clarify the documents related to the physical condition scoring process that the owner must make available to its residents and when these documents must be made available. HUD also welcomes any additional comments on new paragraph (g).

- HUD amends newly designated paragraph (h) of § 200.857 to provide that a multifamily property that receives a score of 30 points or less on its physical condition inspection will be

referred to HUD's Departmental Enforcement Center for evaluation.

In addition to these changes, HUD has made certain editorial and technical changes throughout the rule for the purposes of clarity.

### III. Discussion of Public Comments

At the close of the public comment period on the November 26, 1999, proposed rule, HUD received 53 public comments. The commenters included residents, resident organizations and resident advocates, two housing authorities, nonprofit housing providers and housing industry organizations and associations.

In the discussion of public comments that follows, the heading "Comment" states the issue, opinion, recommendation or question raised by the commenter or commenters, and the heading "Response" presents HUD's response to the issue, question or recommendation raised by the commenters.

#### *Resident Involvement in the Physical Inspection Process*

Many of the resident commenters on the rule stated that the rule should provide for more resident involvement in the physical inspection process. The comments on resident involvement are as follows.

**Comment.** The proposed rule omits almost completely resident involvement in the physical inspection process. The rule should provide for resident involvement in the physical inspection process and specifically, provide for residents to be notified of the physical inspection results, as well as be provided with copies of the inspection report, any related documents, any owner appeals, and compliance plans. The rule also should provide for the issuance of quality control reports that include the input of residents. These recommended provisions should be placed in a new regulatory section that will address how residents will participate in the physical inspection process.

**Response.** HUD recognizes the importance of involving residents in the physical inspection process to ensure that their housing is decent, safe, sanitary and in good repair. HUD declines, however, to adopt the suggestion that the rule require resident involvement in the physical inspection of the housing as recommended by the commenters. HUD has had many discussions with resident groups on this topic and has explained that the inspection process itself does not lend itself to conversational input. Instead,

the process relies on objective observation.

To ensure that there is sufficient opportunity for the residents to participate in seeing that all necessary repairs are made in a timely, efficient and comprehensive manner, HUD is making several changes to the rule at this final rule stage. As noted earlier in this preamble, HUD is requiring owners to notify their residents of upcoming physical inspections of their units and the housing development, generally. HUD is also requiring owners to make the physical inspection information (the physical inspection report, scores) available to residents to review upon request during regular business hours. With respect to the results of a property's physical condition, HUD will make public the results of the physical inspection scores of the properties similar to the manner in which HUD makes public the results of physical inspection scores of public housing under the Public Housing Assessment System.

*Comment.* Residents should have the same right of appeal of physical inspection scores that is provided to owners. Residents should have the right to appeal any and all aspects of the physical inspection finding, and appeals should not be limited to material errors.

*Response.* The responsibility for the physical condition of the property rests with the owner. It is the owner's responsibility to review the physical inspection report, and to submit information clearly describing the errors and omissions that have a significant impact on the physical inspection score in accordance with the conditions and requirements of the rule. However, as discussed earlier in this preamble, HUD has added a new paragraph at this final rule stage that requires owners to notify residents of upcoming physical inspections of the properties and to make documents related to the physical inspection available to the residents, and that also invites residents to submit comments directly to HUD on the condition of the housing in which they reside.

*Comment.* A resident representative should be present for the on-site physical inspections.

*Response.* HUD declines to impose this requirement in its rule. The intent of the physical inspection process is to limit the inconvenience to the owner and the residents of the property being inspected. HUD believes that increasing the number of participants in the physical inspection process could slow down the inspection (thereby increasing inconvenience) and also jeopardize the objectivity of the inspection process.

*Comment.* The rule should provide for residents, rather than owners and managers, to verify that any exigent health and safety violations have been corrected by the managers and owners.

*Response.* Again, the physical condition of the property is the owner's responsibility and correction of exigent health and safety violations (as well as other deficiencies) is the owner's responsibility, as is the verification that these violations have been corrected. The sanctions can be severe if an owner falsely certifies exigent health and safety violations have been corrected.

*Comment.* The rule should provide that the property inspector is required to meet with the residents of the property. The rule also should provide that the inspectors are to leave a resident a notice if a unit was inspected and no one was at home.

*Response.* HUD declines to adopt these suggestions. The duties of the inspector are limited to conducting the physical inspection of the property. Notification to absent residents is the owner's responsibility. This is one reason an owner's representative is required to accompany the inspector.

HUD notes that several resident commenters made suggestions about how a resident survey should be conducted. Although resident surveys were part of the rulemaking for HUD's Public Housing Assessment System (PHAS) regulations, they are not part of this rulemaking, but HUD is further considering this issue.

#### *Physical Inspection Coverage*

*Comment.* HUD's physical inspection software should address tenant malfeasance or nonfeasance and the owner should not be penalized for tenant noncompliance. The physical inspection needs to be limited to habitability issues, not tenant housekeeping/tenant caused conditions, unless these conditions are a direct threat to structural soundness or a safety issue.

*Response.* HUD's physical inspection system is objective and does not distinguish between those defects that are the fault of a resident and those that are the fault of the owner. The physical inspection system is simply a tool for observing and transmitting data regarding the physical condition of the property at the time of the inspection. An owner of HUD assisted or insured housing is contractually responsible for maintaining the physical condition of the property. HUD anticipates that owners of such assisted or insured rental properties, like all landlords, will rely on lease provisions regarding the resident maintenance or destruction of

the units, and HUD encourages owner to do so in compliance with the physical condition standards. Good property management, which includes regular housekeeping and preventative maintenance inspections through the year, coupled with strict lease enforcement will result in well-maintained housing that meets the standard.

*Comment.* The rule should view as health and safety issues the basic accessibility design features which are required in federally funded housing units to assure all people can safely utilize the dwellings. Proper and required accessible design features contribute to the overall well being, both physically and financially of the housing. The rule also should clarify that deficiencies with any physical accessibility features of the units (or the housing, generally, will be classified as Exigent Health and Safety Deficiencies and shall require resolution.

*Response.* Housing design, including accessibility design, is not a feature of HUD's Uniform Physical Condition Standards. HUD's Uniform Physical Condition Standards focus on whether the housing is habitable, is decent, safe, sanitary and in good repair. HUD's Office of Fair Housing and Equal Opportunity is charged with determining compliance with accessibility requirements under the Fair Housing Act or Section 504 of the Rehabilitation Act of 1973 where complaints of violation of these statutory requirements have been alleged. (This office, however, is not responsible for ongoing inspections of maintenance of accessibility features in a unit or building.) To assist HUD's Office of Fair Housing and Equal Opportunity in its task, the inspection collects specific information related to general accessibility. This information is provided to the Office of Fair Housing and Equal Opportunity in the event such information reveals a absence of accessible features where these features should exist.

#### *Ranking and Thresholds for Designation*

The overwhelming majority of commenters who commented on the proposed performance designations (*i.e.*, Standard 1, Standard 2, Standard 3), which were based on percentile groupings, were opposed to the percentage groupings and requested that performance categorizations be based on fixed scores. The comments on this issue included the following.

*Comments.* The ranking classification in the proposed rule fails to provide guidance as to the numeric cut-off for each performance designation (*i.e.*,

standard 1, standard 2, standard 3.). The rule should only use numeric classifications.

The issuance of grades by curving results will not work. The numeric scoring has in fact become the standard in the past 1½ years and should not be changed. A curved ranking is at odds with the possibility of a meaningful appeal.

HUD needs to explain the rationale in holding public housing to an absolute standard (under PHAS) and private HUD assisted housing to a relative standard based on an absolute grade.

HUD should not use percentages, but set a score to objectively rank properties and then conduct annual inspection only for the marginal properties in the bottom 17% or so.

With baseline results completed, to distinguish between properties that all are deemed to be satisfactory based on the percentages in the proposed rule is arbitrary and it increases lender inspection costs with no apparent benefit.

An absolute score is preferable to the standards in the proposed rule.

*Response.* As noted earlier in this preamble, this final rule sets the numeric standards for all three categories. As noted earlier in this preamble, HUD recognizes the need by owners for a clear standard, understandable by those being rated at the time they are rated, and fixed points provide this standard. HUD recognizes that the percentile approach was obscure in this regard.

*Comment.* The rule did not advise how HUD will make known the numeric thresholds for the three tiers and how often the thresholds will be evaluated. If numerical thresholds are to be applied based on national numerical thresholds or will regions have their own discrete numerical assignments on the administrative significant thresholds.

*Response.* All thresholds will be national. Any changes to the thresholds will be made only as needed to maintain the health of HUD's portfolio, and HUD will provide appropriate notification of any changes to the numerical thresholds.

#### *Frequency of Inspection and Post-Inspection Processes*

*Comment.* Physical inspections of properties should be mandatory when requested by 10% or more of the residents of a property, or when requested by a resident organization that meets HUD's standards.

*Response.* HUD declines to adopt this suggestion as a regulatory requirement. If there are concerns by residents of the property in which they reside, they are

encouraged to contact their local HUD Field Office and relay these concerns, and HUD will make the appropriate inquiries to follow-up on these concerns.

*Comment.* The frequency of inspections should be determined by the property's score on the 100 point scale, rather than its score relative to other properties. It is the condition of the building that is of concern and it is only the building's condition that is within the owner's power to control—not the score relative to other projects.

*Response.* As noted earlier in this matter, the rule has been revised to provide for fixed point scores and the frequency of inspections is based on these fixed point scores.

#### *Verification That Repairs Have Been Made*

*Comment.* Owners should not be allowed to self-certify that repairs have been made. This self-certification is at odds with HUD's emphasis on strict, objective, and professional inspections. When an inspector finds violations, management is not concerned about correction of these violations because no one comes back for two or three years, and when HUD returns, it is a different inspector who does not review the previous report. The rule should require reinspections by the same inspector to confirm that repairs have been made.

*Response.* HUD does not agree that it is practical or necessary to require that subsequent inspections be conducted by the same person, year after year. HUD and mortgagees will generally use contract inspectors, and it is not unusual for contractors or personnel employed by contractors to change from year to year. In addition, the design of HUD's physical inspection system focuses on an inspection of the property that will produce objective, consistent results. Therefore, the person who undertakes the inspection, provided the person is trained and certified to use HUD's inspection system, is not a determining factor in the outcome of the inspection. Additionally, those properties for which there are serious physical concerns are inspected annually, not every two or three years as the comment suggests. Given how the inspection process is conducted, the certification required of owners is not at odds with HUD's inspection system. The owners' certification that repairs have been completed is part of an ongoing monitoring plan which will assist HUD in determining if conditions have improved.

*Comment.* HUD should take strong action against owners with seriously substandard buildings—that is the

owners who fail to comply with the physical condition standards. The owner's properties should be transferred to a non-profit or to resident owners who will maintain the properties as decent, safe and affordable housing.

*Response.* HUD has no authority to require the transfer of owners' properties that have been found substandard, to a non-profit organization or residents or resident organization but, if these organizations have the resources to correct the problems, they may be eligible purchasers of the properties. The rule, however, provides for the full range of enforcement actions available to HUD to initiate against owners who refuse or fail to comply with HUD's physical condition standards.

*Comment.* With respect to administrative review of properties and enforcement actions, the rule should provide that reinspection of properties is mandatory where there is a Departmental Enforcement Center (DEC) Compliance Plan in place.

*Response.* HUD declines to adopt this recommendation as a regulatory requirement, but HUD notes that the DEC has the option to take this action under the rule. Properties under evaluation by the DEC as a result of physical condition deficiencies would be reinspected annually.

#### *Properties Covered by the Rule*

*Comment.* Nursing homes, intermediate care facilities, assisted living facilities, and board and care homes should be excluded from the rule's coverage.

*Response.* HUD requires inspection of these properties to determine if Federal Housing Administration (FHA) funds are at risk and if the physical condition meets the needs of the resident population. Since these properties are insured or HUD-held, a physical inspection is appropriate.

*Comment.* Reference to coverage of Section 241 of the National Housing Act (NHA) projects (Supplemental Loans for Multifamily Projects) in the rule should be modified to provide that these projects are to be inspected except where the underlying mortgage is insured or assisted by HUD under a program covered in this part. Without this qualification, there may be duplication of inspection.

*Response.* As noted earlier in the preamble (see Section II), HUD has made this clarification in this final rule.

*Comment.* The proposed rule does not address new construction properties. New properties in conformance with HUD's final cost certification should be

given a 3 year waiver before inspection begins.

*Response.* As discussed earlier in this preamble (under Section II), the final rule addresses newly endorsed properties and provides for a physical inspection to be conducted within approximately two years from final endorsement.

#### *The Training and Qualifications of the Physical Inspectors*

*Comment.* The training provided to inspectors is still not sufficient to ensure proper application of the physical condition standards consistently between properties. While HUD's physical condition and inspection system is clearly more objective in its design, it is still subject to wide variations in its implementation which is attributable, in part, to minimally trained inspectors looking at similar conditions and reporting them with varying degrees of severity. HUD should implement a uniform method of training and certification.

*Response.* The training of inspectors who are certified in the use of the HUD inspection protocol is standardized. To ensure appropriate and adequate training of inspectors, HUD sought experts in the field who would take the lead in actually presenting the materials developed by HUD and training the inspectors. In addition to selecting experts in the field to perform the training, every inspector candidate must meet the minimum qualification requirements determined by HUD. The inspector candidates also must take the required course and then take and pass a test. HUD monitors and controls all aspects of this training process through REAC.

Since the inspection under HUD's new standards and physical condition protocols began in approximately October 1998, the initial start-up involved some refining as one would expect given the size and magnitude of the portfolio to be inspected. In certain cases, problems were encountered and HUD responded to these problems. HUD believes that the process overall, however, is now running smoothly. HUD is striving to constantly improve and refine the process and will continue to do so in the future. In this regard, HUD also provides for periodic retraining of the inspectors, to ensure that the inspectors are up-to-date and familiar with any changes made to the physical condition protocol and software.

HUD acknowledges that even with qualification and training requirements imposed on inspectors, some inspectors, as is the case in any profession, perform

better than others. REAC monitors the inspectors, and HUD invites owners that have concerns about an inspector's ability to contact REAC through its Technical Assistance Center (1-888-245-4860).

*Comment.* Inspectors need to have knowledge of local building and fire codes in order to conduct an accurate and informed inspection.

*Response.* HUD disagrees with this suggestion. HUD's physical inspection protocol have some basis in a national codes (e.g., fire safety) but there is too much variation among local and state codes to make the use of local code an efficient and effective alternative to HUD's physical inspection protocols. Additionally, the responsibility of HUD contract inspectors is to determine whether HUD assisted and assured housing meets HUD's Uniform Physical Condition Standards, not to ensure enforcement of local building codes.

It is the responsibility of the owner to be cognizant of and abide by all local codes. HUD notes, however, that there are allowances built into HUD's physical inspection protocols, as noted in the November 26, 1999 proposed rule, that provide for an owner to notify HUD of significant conflicts between HUD's Uniform Physical Condition Standards and local code requirements or other local requirements applicable to the property.

*Comment.* HUD requires the use of qualified and trained inspectors but gives no information on this process so that a lender's inspector can benefit from this training and meet HUD's qualifications.

*Response.* The response to an earlier comment described the requirements that individuals must meet to become HUD contract inspectors. Persons and firms that are required to comply with HUD's Uniform Physical Condition Standards may seek to have their own employees trained and certified. The common element is that the party that actually performs an inspection (to conform with HUD requirements) must complete and pass HUD's qualification training and testing for property inspectors. Each successful candidate will be issued identification from REAC as evidence that the candidate has met all requirements. It is important to note that parties that wish to better understand the REAC protocol, may participate in REAC monitored training. However, only inspectors who are working for HUD contractors, multifamily lenders or who perform inspections under independent third party contracts will be issued final identification. The information about how to become a HUD contract

inspector is (and has been) available from REAC's Internet site at <http://www.hud.gov/reac>. Additionally, interested parties are welcome to call REAC's Technical Assistance Center at 1-888-245-4860.

#### *Simplifying and Improving the Scoring Process*

*Comment.* The rule should provide a simpler and abbreviated physical inspection protocol for smaller properties where property facilities are less complicated and the loan balance is small. Smaller loan balances mean lenders have less money for inspections. These properties do not have need for a complicated, multi-tiered inspection on amenities and facilities that do not exist. For smaller properties, inspections should not be more than every two years.

*Response.* HUD is charged with assuring all housing is decent, safe, sanitary and in good repair, not just larger properties or properties with large loan balances. HUD's physical inspection protocols are structured in a manner to adjust for size and properties that have amenities and facilities and those that do not. Additionally, HUD's rule provides for cost savings through less frequent inspections for properties that are well-maintained. HUD's obligation to ensure that its assisted and insured housing is decent, safe, sanitary and in good repair does not permit HUD to exempt a property from an annual inspection, simply because the property is a small property.

*Comment.* The physical inspection process would be improved if HUD requires the inspector to clearly communicate each observable deficiency and ensures that a detailed written report of deficiencies is left with the owner.

*Response.* HUD agrees with this comment and all inspectors have been trained to communicate the defects that the inspector records to the owner's representative during the inspection. While HUD acknowledges that the owner's representative may have differing views regarding the deficiency definitions and may express those views to the inspector, the inspectors are trained not to engage in a discussion of the merits of the deficiency definitions. Inspectors have no authority or discretion to alter the definitions of deficiencies or the severity level assigned. Inspectors must record the deficiencies in accordance with the inspection protocol. At this time, technology that would allow HUD to leave a copy of the inspection report immediately following the inspection remains too expensive. Therefore, a

copy is provided to the owner within a few days of the inspection.

*Comment.* HUD's inspection report should show the score of each observable deficiency.

*Response.* HUD has revised the inspection report to show the points deducted for each observed deficiency.

*Comment.* HUD's physical inspection protocol should take into consideration minor routine repairs in assessment. The weighting that minor repairs receive can be as much as deferred maintenance or major repairs. Therefore, the inspection protocol software should provide a category of noted, routine repairs without a point loss and should note the difference between minor, routine repairs and deferred maintenance of capital needs, and showing the scoring effect should clarify this.

*Response.* HUD's protocol already takes into consideration minor defects and repair requirements by way of the scoring process. The inspection summary report notes the difference on a summary basis between routine repairs and capital needs.

*Comment.* The rule should define the meaning and application of "health and safety." It is unclear what HUD means when it refers to health and safety or how health and safety is scored. Clarification is important because failure to correct such a deficiency could result in demotion from standard 1 or standard 2 to standard 3.

*Response.* Health and safety concerns are clarified in 24 CFR 5.703(f), which this rule cross-references. Exigent health and safety deficiencies are a distinct subset of health and safety standards and are considered a risk to life. A standard 1 property for which extreme hazardous conditions are not corrected would be subject to further inspection and may change designation as a result of that reinspection.

#### *Appeal, Technical Review, Burden of Documentation and Reinspection*

*Comment.* It is unrealistic to require owners to use the "Items, Weights and Criticality" document to make the determination, within 15 days, that an error has occurred that if corrected would result in a significant improvement in the scoring process. The scoring process is very intricate and complicated and point values change dramatically depending on elements at each specific property.

*Response.* To address this concern, HUD has revised the inspection summary reports so that they will show the point value for each cited deficiency.

*Comment.* The requirement in § 200.857(c) to report to HUD within 72 hours of the inspection that exigent health and safety items have been mitigated is neither practical nor reasonable. HUD should allow a response of 10 working days. The rule should clarify that the 72 hour limit in § 200.857(c) means 3 business days.

*Response.* The final rule makes the clarification that 72 hours refers to 3 business days from the date of the physical inspection, the date the owner receives the notice of exigent health and safety deficiencies. HUD, however, declines to extend this period beyond 3 business days. This time period mirrors the critical need for the owner to repair or mitigate the most serious health and safety conditions immediately.

*Comment.* The 15 day time period for response and appeals is unrealistic. HUD should allow at least 30 days. The time to evaluate the complex score and report is the same in order to prepare a detailed and adequate response and appeal. HUD should provide owners with a reasonable time to challenge inspection results because they have the burden of proof and must provide substantial evidence.

*Response.* HUD declines to expand the response time. HUD believes 15 days is sufficient time to prepare a response and submit a request for technical review. As noted earlier, HUD requires inspectors to point out defects as they are observed on the day of the inspection to the owner's representative. The score impact of every item observed is known at the time the inspection report is issued to the owner.

*Comment.* Because the rule relies on owner responses in prescribed time periods following HUD's notification, the rule should state that time periods begin after the owner receives notice from HUD. HUD correspondence is received/postmarked considerably later than it is dated.

*Response.* To avoid delays between submission of the report to the owner and the owner's response to HUD, HUD is planning to have all inspection reports available to the owners through the Internet. For those owners without Internet capability, HUD will consider mailing the results. However, HUD allows, as an allowable project expense, the reasonable cost of an internet service provider so that over time we expect that virtually all properties will have access either on site, through the agent's off site office or a sharing arrangement with other providers.

*Comment.* HUD should revise communications with owners in a way that the final report presents a more realistic picture on the property. The

current report focuses on what is wrong and when it is read in a vacuum, regardless of the property's score, the report presents an out-of-line picture.

*Response.* The report shows the potential score of all inspectable items, not just those items identified as deficiencies. HUD believes that the report which now shows the potential score for all inspectable items combined with the score for items identified as deficiencies allows a balanced view.

*Comment.* The rule takes the right approach in providing that reinspections are HUD's responsibility. If a mortgagee uses a HUD certified inspector and HUD's physical inspection protocols and the inspection is technically acceptable then the mortgagee has fulfilled its obligations. If the owner challenges the results, the owner will request HUD, not the mortgagee, for a reinspection.

*Response.* The mortgagee is responsible for performance by its employees or contractors in a manner to assess that the product transmitted to HUD is of good quality. REAC reviews all inspections and, in the event the inspection is not acceptable, the mortgagee, which commissioned the inspection, must complete the inspection even though this may mean having another inspection completed. REAC makes every effort to cure problems arising from the review. If this is not possible, REAC will notify the mortgagee of the problems and provide time to correct the errors. However, some errors such as inadequate sampling are not correctable without another visit to the property to complete the sample required.

*Comment.* The rule should provide a process for the owner and management agent to receive inspection related communications and to allow the owner the option to allow simultaneous electronic release of this information to additional parties, such as front line manager, legal counsel board chair, etc. This would expedite communications and allow front line operators to have maximum time to prepare needed responses.

*Response.* Once electronic Internet access is completed, the owner may designate personnel to act to retrieve and respond to inspection reports. HUD will, however, always look to the owner of record as the party responsible for action or inaction.

*Comment.* The errors for which an owner may request a technical review and have a reinspection violate the precepts of fairness. The definitions of material errors refer to obvious mistakes, but these are the exception, not the rule. An inspector's decision

about the seriousness with which an owner would have a legitimate disagreement cannot be challenged. The degree of deficiency is subjective. Three different inspectors with the same training and manual at the same building could come up with disparate scores because of their own unique perspective. The rule should allow an owner to request a technical review in any circumstance where the property score is below a standard 1 level. The grounds for appeal should be broadened to cover serious problems with the inspection definitions and with an inspector's failure to carry out the protocol.

*Response.* HUD disagrees with the comments. The seriousness of a defect is not subjective. Each defect is defined and each inspector is fully trained and tested to achieve maximum objectivity in determining the severity of defects. In addition, the REAC Quality Assurance personnel are charged with reviewing work performed by inspectors at regular intervals and at random.

*Comment.* A percentage change in the numeric score is a better trigger for reinspection and rescoring, not a change in the standard classification.

*Response.* HUD disagrees. A large percentage score may not move a property out of a particular operating mode while a small point increase could change the oversight and general program eligibility of an owner.

*Comment.* The rule should make clear that the lender does not conduct follow-up inspections.

*Response.* The lender may wish to make follow-up inspections as part of its own quality assurance plan. However, if an inspection is accepted by REAC, resolution of the deficiencies is the responsibility of HUD.

*Comment.* An issue arises when a reinspected project may not obtain the full benefit of a higher score even if original inspection error is rectified. With the "loss limiting" algorithms built into the system because of the scoring categories, an owner cannot know if removal of one of several defects will raise the score to meet a threshold.

*Response.* The inspection summary includes the value of all defects and thus shows all possible points deducted. The inspection summary also shows the total possible points for the site, a given unit or a given building exterior, etc., and this allows a determination of the extent to which points lost may exceed the loss limit referred to in the comment. (Under the scoring algorithms, the points deducted for the site of an individual unit building's exterior, systems or common areas

cannot exceed the possible points.) If an error is found that has significant impact on the score, the owner may request a technical review. HUD does not wish to burden the system with technical review requests that do not have a significant impact.

*Comment.* All errors must be corrected, even if the correction would not result in the score crossing the threshold. HUD should provide an explanation to the owner/manager of the total score that could be achieved assuming all identified errors are corrected. If HUD determines that error correction will not result in recategorization, the score should be adjusted to correct for these errors. If HUD determines a new inspection is warranted, it should be at HUD's expense. Only when the owner challenges errors that do not exist should the owner pay for the reinspection and any reinspection, if not paid by HUD, should be an allowable project expense.

*Response.* HUD now provides the absolute point reduction for each and every defect cited. When no defects are present, the maximum score is 100 points. The comment appears to suggest that HUD engage in evaluating owner request for technical review for even fractional points which have no effect on the property. HUD believes this process does not consider the overall objective—which is property that is decent, safe, sanitary and in good repair. HUD will require the owner to make full payment for a new inspection that is performed based on an owner's technical review request where the result does not cross a signification threshold. This remains a necessary part of the process from HUD's perspective in order not to burden the process with inconsequential request.

*Comment.* Upon receipt of satisfactory second round inspections, HUD should remove from the permanent project file, at the owner's request, the first round results.

*Response.* HUD disagrees and will not remove the results of inspection reports from the permanent project file. However, if a subsequent inspection crosses the threshold from standard 2 to standard 1, the owner will immediately be eligible for the every-three-year inspection. The administrative record will continue to hold all valid information.

*Comment.* The procedures for appeals should be modified in several respects to improve effectiveness and efficiency of the approval process. The procedures should be modified to allow the expense of the appeal to be covered in the budget; to place the burden on HUD to

work with owners to advise them of the numerical impact of any and all elements of interest to the owner until the significant thresholds have been published and all inspection reports issued in a way to allow an owner to readily determine whether or not certain elements, if successfully appealed, would meet the administrative threshold requirement; and require HUD to reissue all inspection reports using the new end column format showing the numerical value for each deficiency at the owner's request.

*Response.* If a technical review is successful, HUD issues a new report. All reports now show the points deducted for each cited defect. The expenses of a reinspection that does not result in a significant improvement will remain the responsibility of the owner and will not be treated as a property expense.

*Comment.* HUD should be flexible in the type of documentation required for appeals. Owners may have a notarized letter from the local HUD office or from a local building code office, or a similar type of declaration in the absence of statutory language.

*Response.* HUD is flexible in the type of third party reasonable documentation and will continue to be so.

*Comment.* The term "burden of proof" is a legal standard for judicial or administrative settings with trained judges and rules with regard to submission of written and oral evidence. This term should not be used lightly without definition to control appeals from REAC inspectors. It would be appropriate to state the owner is expected to provide factual information supporting its appeal, but once HUD has that information, HUD's determination should be objective without "weighing" documentation based on HUD's interpretation of the term.

*Response.* While "burden of proof" is a term used in the judicial or administrative hearing context, the use of such term is not confined to those settings. HUD believes that § 200.857(d)(2) makes clear the standard of factual information and supportive document (*i.e.*, proof) that the owner must submit.

*Comment.* Responsibility to show errors should not rest solely with the owner but with HUD and the inspector as well. When the deficiency has a significant numeric impact and the owner cannot locate the deficiency, HUD and/or the inspector should be required to produce evidence (and visit the site to point out the deficiency). Otherwise, HUD should remove the notation and the scoring impact. During subsequent inspections, HUD should (i) reinstate the exit interview for



inspectors to point out deficiencies as they enter them so owners can locate them and understand the type, (ii) make notations in the comments section of repairs done in presence of inspectors, and (iii) include the owner's statements about long range maintenance plans, etc.

*Response.* HUD agrees and both the proposed rule and this final rule allow for mutual resolution of the claim of a non-existent deficiency. HUD believes, however, that the first level of claim that an error has occurred must come from the owner in the form of reasonable documentation. Examples of reasonable documentation have already been provided.

Additionally, as noted earlier in this preamble, inspectors are now requested to communicate observed deficiencies orally on site. All inspectors have been trained to "call out" inspection deficiencies as they are observed. This methodology eliminates the need for the "close out conference" and provides the owner or owner's representative with a running account of what is being recorded as the inspection process is conducted. Revised definitions concerning deficiencies allow the inspector to consider specific areas that may be cured on site in the presence of the inspector. For example, if an electrical panel in a unit is blocked but the blockage (such as a picture) can be easily moved in the presence of the inspector, the defect will not be recorded. An additional example is the following—in the event that the site shows significant litter in and around a small area, the inspector will not record the defect if staff is actively working to remove the litter.

*Comment.* Owners should not have to bear costs of reinspection even if results do not change classification. It is punitive for owners to bear the cost of reinspection and it serves to dissuade appeals if owners bear the cost when the appeal is unsuccessful. If inspectors make technical/obvious mistakes that would improve a numeric score from 32 to 58, owners should not bear the cost. Owners should not have to pay for what in most circumstances will be an honest difference of opinion.

*Response.* A difference of opinion is not the same as an error. HUD does not wish to attempt to dispute an owner's opinion but is willing and able to correct errors committed by inspectors. As noted in Section II of this preamble, HUD has revised the rule at this final rule stage to include in the definition of "significant improvement" a movement of 10 points or more as a result of the technical review. Payment for reinspections that result in less than

significant improvement will be the responsibility of the owner.

*Comment.* HUD should clarify that a third party inspection is objective evidence supporting any claim of technical error. HUD also should clarify that the evidence may be from the owner if it is reasonable and supported with more than a new allegation.

*Response.* If an owner believes that such an inspection meets the standard of reasonable documentation, it will be considered. However, such inspection should be comparable to the REAC inspection. The inspection should present documentation that cites specific HUD requirements not opinions.

*Comment.* A shortfall of the proposed rule is the inability of the owner/manager to obtain a revised higher score by completing repairs or presenting an acceptable plan for completion to HUD. The rule should permit an owner/manager to petition for reinspection based on repaired conditions, with the owner paying for all or part of the reinspection cost.

*Response.* The inspection protocol is intended to capture the condition of the property at a certain point in time. HUD realizes there will always be some outstanding maintenance items. Routine maintenance needs have no significant impact on the score.

#### *Enforcement Actions*

*Comment.* Dividing appeal decisions between REAC and HUD Field Offices makes for a complicated and confusing appeal system. REAC is responsible for the technical aspects of inspections, inputting data, scoring, and objective information. HUD Field Offices and Hubs are responsible for area specific, qualitative judgments such as local code conflicts with inspection protocol or whether the facilities are the responsibility of a third party or whether ongoing rehabilitation or maintenance should delay the inspection. Appeals should be directed to one HUD office. All appeals should be directed to the Office of Housing.

*Response.* HUD does not use the term "appeal" in the rule but understands that the issues the commenters are raising concern the technical review process that is under REAC's jurisdiction and the adjustment of physical condition score due to local circumstance which, the proposed rule provided was under the jurisdiction of the applicable HUD Field Office or Hub. HUD agrees with the commenters that requests for review of concerns about a property's score should all be directed to one office and the final rule provides that the office is REAC.

*Comment.* The rule needs to provide a standard for when the HUD Field Office determines to refer a matter to HUD's Departmental Enforcement Center (DEC).

*Response.* The final rule provides that a property that receives a physical inspection score of 30 or below will be referred to the DEC for evaluation. This is a clear and objective standard.

*Comment.* The rule is clear about the owner's responsibilities, but less clear about the owner's right to receive a copy of its file so that everyone is reviewing the same information. The file includes information and history beyond the physical inspection report.

*Response.* The significant information for the owner is the inspection report. To the extent other information is needed as background, the information is generally available to the owner from the local HUD Field Office.

*Comment.* The role of HUD's Field Offices should be clarified in the rule and Field Office staff should be encouraged to make judgments when their experience is at variance with inspection results.

*Response.* While HUD highly values input from its Field Office staff, the key feature of HUD's physical inspection process is to provide for an objective system. Conclusions drawn from relationships with owners and personal knowledge of the properties are inconsistent with an objective evaluation of the physical condition of a property.

*Comment.* The rule should provide assurance that no enforcement action would be initiated prior to a decision on appeal.

*Response.* HUD cannot make this commitment. Circumstances may compel HUD to take immediate enforcement action. In fact, the rule specifically provides that the administrative process described in the rule does not prohibit the Office of Housing, the Departmental Enforcement Center or HUD generally from taking whatever action may be necessary (when necessary) as authorized under existing statutes, regulations, contracts or other documents to protect HUD's interests in multifamily properties and to protect the residents of these properties. (See 24 CFR 200.857(h)(4).)

*Comment.* The rule states that the administrative process in the rule will not be construed to limit HUD's ability to take other enforcement actions; however the extent to which such actions can be taken should be described in the rule.

*Response.* HUD declines to repeat in this regulation the enforcement actions that are available to HUD and that are



listed in other HUD program regulations that may be applicable to owners (depending on the HUD program in which they participate) or contracts or other documents. Generally, HUD participants that are covered by these other requirements are familiar with them.

*Comment.* The rule should make clear that HUD, not the lender, is responsible for the compliance plan process. Section 200.857(h) refers to the owner's compliance action but does not refer to HUD's participation in the process.

*Response.* This section clearly provides for the actions and duties that the DEC may and will undertake and the DEC is a part of HUD.

*Comment.* HUD should establish a Departmental Evaluation Center in addition to the Departmental Enforcement Center. Section 200.857(f) of the proposed rule speaks of evaluation through administrative review. It is problematic for properties to emerge from DEC even when no fault is found and scoring problems result from complicated property situations.

*Response.* HUD's Departmental Enforcement Center has the expertise to perform the administrative review described in § 200.857(f). There is no need to establish a separate evaluation center.

#### *Cost of the Physical Inspection*

*Comment.* The rule does not specify or limit the financial burden of an inspection to be placed on lenders. The rule should state that there will be no material change in the inspection process that will materially increase costs, and the rule should define "material increase in cost" to be no greater than 5 percent.

*Response.* Although the rule does not specify a limitation to the financial cost of an inspection placed on lenders, as discussed in the November 1999 proposed rule, HUD has taken significant steps to minimize the costs of inspection to lenders and owners. HUD's inspection software and guidebook is distributed to HUD's program participants without cost. HUD also has placed these materials on the web so that they can be downloaded and therefore no shipping costs are incurred. Additionally, in the proposed rule, HUD advised that it would not materially alter the physical inspection requirements in a manner which would material increase the cost of performing the inspection (see 64 FR 66535, middle column.)

*Comment.* Section 200.857(h) in the rule should be revised to remove the word "software" because this raises concern that HUD may add features that

are enhancements (provide pictures from digital camera) but not necessary to the inspection process and therefore make the software more costly.

*Response.* The use of the word "software" is the appropriate term. The term describes that set of stored procedures and operating instructions that allow the data collection device to function. Inspection data is already in the software. Digital pictures are not part of the functionality of the software.

#### *Regulatory Amendments That Adversely Affect FHA Lenders*

*Comment.* The changes to the physical inspection process proposed by the November 1999 rule would be a violation of § 207.499 and the mortgage insurance contracts. The change in the inspection process, as provided in this rule, is likely to change and increase costs for lenders in a manner not contemplated in existing mortgage insurance contracts. The changes expand the role and scope of the inspections performed to date. HUD will greatly increase the costs by requiring new computer systems and software and these new protocols may exceed the lender's service income. To control costs there must be (i) an adequate number of certified inspectors and inspection companies to ensure competition; and (ii) reduced frequency of inspections for better performing properties.

*Response.* The insurance contract provides for the mortgagee to perform the inspection pursuant to HUD requirements and, the insurance contract has not been adversely affected.

*Comment.* HUD should add a provision to this rule that states that the FHA Commissioner may amend these regulations but the amendments shall not adversely affect the interest of a mortgagee or lender under the contract of insurance.

*Response.* HUD declines to add this provision to the rule. HUD needs the flexibility to promulgate such amendments that HUD believes are necessary to make the housing programs effective and to fulfill the statutory obligations and objectives imposed on HUD for these programs.

#### *Timing of Implementation of the Rule*

*Comment.* Implementation of the rule should be four months after existing mortgagees have been provided with baseline scores and after HUD has successfully tested the computer system for scheduling and retrieving inspections.

*Response.* To accommodate concerns in this area, HUD has agreed to perform all inspections required through

December 31, 2000. This will allow additional transition and planning time for lenders.

*Comment.* Because the parameters and definitions in the current baseline inspections are being refined and revised, and the baseline inspection is almost complete, it does not make sense to require new inspections to be performed during the revision process.

*Response.* HUD did not require any new inspections during this period of baseline inspections.

*Comment.* The rule should provide for retroactive application to ensure owners have fair opportunity to address scores and be on record that the score is inappropriate. Otherwise, there may be injurious results to owners and their reputation which remains permanently on the record.

*Response.* Owners have always had the opportunity to address scores if they believe they are inappropriate. Project Managers will ensure that any complaint, inquiry or concern is addressed. Should the Hub/Program Center Director believe a complaint about a score or anything else from an owner is valid, it should be addressed. HUD Field Office will forward the complaint to the Office of Asset Management at HUD Headquarters for review and action. Should Headquarters believe additional follow-up is necessary, Headquarters will forward to HUD's Real Estate Assessment Center for appropriate review and action. Complaints are posted in "REMS" at the Field Office level. If forwarded to Headquarters they are logged and monitored to ensure the owner receives a response by Headquarters and/or the Real Estate Assessment Center.

#### *Entity Responsible for Inspection/Duplicate Inspection Requirements*

*Comment.* The rule needs to clarify that for properties with more than one HUD insured loan, only the first mortgage lender is required to conduct the physical inspection with the second mortgage lender having access to the inspection. The rule also needs to clarify that only one mortgage inspects when there is a first and second mortgage.

*Response.* HUD agrees and the final rule makes these clarifications.

*Comment.* The rule should specify the responsible party for Section 8 assisted properties. The rule does not address administrative difficulty and duplication of costs for lenders who perform inspections, and Section 8 contract administrators. For those properties with a mortgagee different from the section 8 contract administrator, the rule should provide

that the Section 8 contract administrator performs the inspection.

*Response.* The intent of HUD is to have inspections performed no more frequently than annually and that a single inspection will suffice for all parties that have a need to perform these inspections. For the HUD insured portfolio, the lender will perform all required inspections; HUD will not duplicate this effort. Newly appointed contract administrators will not perform or arrange for property inspections. HUD will perform the property inspection if there is no mortgagee. Existing contract administrators are required to inspect annually all units in a property that they are responsible for administering. However, the oversight the contract administrator performs does not include the HUD physical inspection protocol: HUD will perform this inspection. When the contracts are renewed, the administration will be turned over to more recently appointed contract administrators, and at that time, inspections will be performed only by HUD.

*Comment.* HUD needs to clarify how the Comprehensive Needs Assessment, which includes a detailed inspection, interacts with the Uniform Physical Conditions Standards inspection. HUD requires owners who request Section 8 renewals to have a Comprehensive Needs Assessment. Section 8 renewals may be on a 1 to 5 year basis so the CNA is used more frequently. HUD needs to eliminate duplicate requirements.

*Response.* The Comprehensive Needs Assessment (CNA) and the Uniform Physical Condition Standards (UPCS) are related in that they both address property assessment but they are different types of property assessment. The CNA was designed to estimate the need for capital improvement over an extended period into the future. The CNA uses or can use the UPCS inspection results as a starting point in the CNA assessment. The result of the UPCS inspection, however, is a snapshot of the property at a specific point in time. The inspection results are statistically valid and therefore are useful as an overall evaluation of property condition at the point in time of the inspection. The CNA is not valid, in the same statistical manner as the UPCS, but the CNA is an estimate of physical needs which allows the owner to make long term plans to accumulate resources to assure the long term viability of property. The UPCS inspection will provide feedback to the owner and HUD about the CNA planning process and its validity as time passes. The two are related and should

be used together but one cannot take the place of the other.

*Comment.* There is concern about a statement in the preamble that states other HUD offices may inspect for various purposes. The possibility of other inspections for other purposes seems duplicative and wasteful.

*Response.* This statement refers to HUD's statutory and regulatory requirements under other programs to monitor compliance with specific program requirements, which may include physical inspection, but generally are directed to other program requirements. For example, HUD's Office of Fair Housing and Equal Opportunity monitors owner compliance with requirements for accessibility and/or appropriate accommodations for persons with disabilities. This monitoring, however, is not a physical inspection to determine the quality and maintenance of the accessibility features, but rather one to determine that the owner has provided accessibility features and accommodations where they are required. The inspection conducted under HUD's Uniform Physical Condition Standards does not monitor compliance with accessibility requirements. Although HUD's physical inspection process collect specific data requested by HUD's Office of Fair Housing, it is important to note that this data is not part of the physical condition scoring process. Therefore, the examinations of accessibility features conducted by HUD's Office of Fair Housing and Equal Opportunity and REAC are not duplicative of one another.

#### *Rulemaking Procedures*

*Comment.* The inspection and scoring process, as noted in the preamble to the proposed rule was first introduced in HUD's Public Housing Assessment (PHAS) rule, which was limited to PHAs. HUD should have specifically sought comment from tenants in multifamily housing if it was considering extending that process to multifamily housing.

*Response.* HUD did solicit public comment from multifamily residents, owners, and lenders through publication of the November 26, 1999, proposed rule. It is the November 1999 rule that proposed a scoring process for multifamily housing properties, and the November 1999 proposed rule provided a 60-day public comment period.

## **IV. Findings and Certifications**

### *Paperwork Reduction Act Statement*

The information collection requirements contained in this rule have been submitted to the Office of Management and Budget under the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35). The information collection requirements when approved will be assigned an OMB approval number and the public will be notified of this number. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a valid control number.

### *Executive Order 12866*

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866, *Regulatory Planning and Review*, issued by the President on September 30, 1993. OMB determined that this rule is a "significant regulatory action," as defined in section 3(f) of the Order (although not economically significant, as provided in section 3(f)(1) of the Order). Any changes made in this rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Regulations Division, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC, 20410-8000.

### *Environmental Impact*

A Finding of No Significant Impact with respect to the environment was made at the proposed rule stage in accordance with HUD regulations in 24 CFR part 50 that implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4223). That Finding remains applicable to this final rule and is available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC, 20410-8000.

### *Regulatory Flexibility Act*

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed this rule before publication and by approving it certifies that this rule is not anticipated to have a significant economic impact on a substantial number of small entities. As stated in HUD's June 30, 1998, proposed rule and September 1, 1998, interim rule

on uniform physical condition standards, all HUD housing has been subject to physical condition standards and a physical inspection requirement. There are statutory directives to maintain HUD housing in a condition that is decent, safe, and sanitary. The rules on uniform physical conditions standards and uniform physical inspections do not alter these requirements, nor do they shift responsibility with respect to who conducts the physical inspection of the property. The entities and individuals responsible for the inspection of HUD subsidized properties remain responsible. This rule is a follow-up to the September 1, 1998, final rule on uniform physical inspection standards by establishing an administrative process by which multifamily housing properties are analyzed, scored and ranked. With the exception of exigent circumstances, the administrative process, as described in the preamble, allows for appropriate and reasonable notice and opportunity for review and comment, and a reasonable period for corrective action. With respect to the physical inspection process itself, in the preamble to this proposed rule, HUD reiterated its commitment to provide the software at no cost to covered entities as well as the accompanying guidebooks and to publish a notice that gives covered entities reasonable notice of when the software and guidance are available. With the implementation of any new or modified program requirement, HUD intends to provide guidance to the covered entities, particularly small entities, to assist them in understanding the changes being made.

#### *Executive Order, Federalism*

Executive Order 13132 (entitled "Federalism") prohibits, to the extent practicable and permitted by law, an agency from promulgating a regulation that has federalism implications and either imposes substantial direct compliance costs on State and local governments and is not required by statute, or preempts State law, unless the relevant requirements of section 6 of the Executive Order are met. This rule does not have federalism implications and does not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive Order.

#### *Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104-4; approved March 22, 1995) (UMRA) establishes requirements for Federal

agencies to assess the effects of their regulatory actions on State, local, and tribal governments, and the private sector. This proposed rule would not impose any Federal mandates on any State, local, or tribal governments, or on the private sector, within the meaning of the UMRA.

#### *Catalog of Federal Domestic Assistance*

The Catalog of Federal Domestic Assistance numbers for the programs that would be affected by this proposed rule are:

- 14.126—Mortgage—Insurance—Cooperative Projects (Section 213)
- 14.129—Mortgage Insurance—Nursing Homes, Intermediate Care Facilities, Board and Care Homes and Assisted Living Facilities (Section 232)
- 14.134—Mortgage Insurance—Rental Housing (Section 207)
- 14.135—Mortgage Insurance—Rental and Cooperative Housing for Moderate Income Families and Elderly, Market Rate Interest (Sections 221(d)(3) and (4))
- 14.138—Mortgage Insurance—Rental Housing for Elderly (Section 231)
- 14.139—Mortgage Insurance—Rental Housing in Urban Areas (Section 220 Multifamily)
- 14.157—Supportive Housing for the Elderly (Section 202)
- 14.181—Supportive Housing for Persons with Disabilities (Section 811)
- 14.856—Lower Income Housing Assistance Program—Section 8 Moderate Rehabilitation

#### **List of Subjects**

##### *24 CFR Part 5*

Administrative practice and procedure, Aged, Claims, Drug abuse, Drug traffic control, Grant programs—housing and community development, Grant programs—Indians, Individuals with disabilities, Loan programs—housing and community development, Low and moderate income housing, Mortgage insurance, Pets, Public housing, Rent subsidies, Reporting and recordkeeping requirements.

##### *24 CFR Part 200*

Administrative practice and procedure, Claims, Equal employment opportunity, Fair housing, Home improvement, Housing standards, Incorporation by reference, Lead poisoning, Loan programs—housing and community development, Minimum property standards, Mortgage insurance, Organization and functions (Government agencies), Penalties, Reporting and recordkeeping requirements, Social security, Unemployment compensation, Wages.

Accordingly, for the reasons stated in the preamble, title 24 of the CFR is amended as follows:

## **PART 5—GENERAL HUD PROGRAM REQUIREMENTS; WAIVERS**

1. The authority citation for 24 CFR part 5 continues to read as follows:

**Authority:** 42 U.S.C. 3535(d), unless otherwise noted.

2. In § 5.701, paragraphs (a) and (b) are revised to read as follows:

### **§ 5.701 Applicability.**

(a) This subpart applies to housing assisted under the HUD programs listed in 24 CFR 200.853(a).

(b) This subpart applies to housing with mortgages insured or held by HUD, or housing that is receiving assistance from HUD, under the programs listed in 24 CFR 200.853(b).

\* \* \* \* \*

3. Section 5.705 is revised to read as follows:

### **§ 5.705 Uniform physical inspection requirements.**

Any entity responsible for conducting a physical inspection of HUD housing, to determine compliance with this subpart, must inspect such HUD housing annually in accordance with HUD-prescribed physical inspection procedures. The inspection must be conducted annually unless the program regulations governing the housing provide otherwise or unless HUD has provided otherwise by notice.

## **PART 200—INTRODUCTION TO FHA PROGRAMS**

4. The authority citation for 24 CFR part 200 continues to read as follows:

**Authority:** 12 U.S.C. 1701–1715–18; 42 U.S.C. 2535(d).

5. A new subpart P is added to 24 CFR part 200 to read as follows:

### **Subpart P—Physical Condition of Multifamily Properties**

Sec.

200.850 Purpose.

200.853 Applicability.

200.855 Physical condition standards and physical inspection requirements.

200.857 Administrative process for scoring and ranking the physical condition of multifamily housing properties.

### **Subpart P—Physical Condition of Multifamily Properties**

#### **§ 200.850 Purpose.**

The purpose of this subpart is to establish the physical conditions standards and physical inspection requirements that are applicable to certain multifamily housing properties.

#### **§ 200.853 Applicability.**

This subpart applies to:

(a) Housing assisted by HUD under the following programs:

(1) All Section 8 project-based assistance. "Project-based assistance" means Section 8 assistance that is attached to the structure (see 24 CFR 982.1(b)(1) regarding the distinction between "project-based" and "tenant-based" assistance);

(2) Section 202 Program of Supportive Housing for the Elderly (Capital Advances);

(3) Section 811 Program of Supportive Housing for Persons with Disabilities (Capital Advances); and

(4) Section 202 loan program for projects for the elderly and handicapped (including 202/8 projects and 202/162 projects).

(b) Housing with mortgages insured or held by HUD, or housing that is receiving insurance from HUD, under the following authorities:

(1) Section 207 of the National Housing Act (NHA) (12 U.S.C. 1701 *et seq.*) (Rental Housing Insurance);

(2) Section 213 of the NHA (Cooperative Housing Insurance);

(3) Section 220 of the NHA (Rehabilitation and Neighborhood Conservation Housing Insurance);

(4) Section 221(d)(3) of the NHA (Market Interest Rate (MIR) Program);

(5) Section 221(d)(3) and (5) of the NHA (Below Market Interest Rate (BMIR) Program);

(6) Section 221(d)(4) of the NHA (Housing for Moderate Income and Displaced Families);

(7) Section 231 of the NHA (Housing for Elderly Persons);

(8) Section 232 of the NHA (Mortgage Insurance for Nursing Homes, Intermediate Care Facilities, Assisted Living Facilities, Board and Care Homes);

(9) Section 234(d) of the NHA (Rental) (Mortgage Insurance for Condominiums);

(10) Section 236 of the NHA (Rental and Cooperative Housing for Lower Income Families);

(11) Section 241 of the NHA (Supplemental Loans for Multifamily Projects). (Where, however, the primary mortgage of a Section 241 property is insured or assisted by HUD under a program covered in this part, the coverage by two HUD programs does not trigger two inspections); and

(12) Section 542(c) of the Housing and Community Development Act of 1992 (12 U.S.C. 1707 note) (Housing Finance Agency Risk Sharing Program).

#### **§ 200.855 Physical condition standards and physical inspection requirements.**

(a) *Applicable standards and requirements.* The physical condition

standards and physical inspection requirements in 24 CFR part 5, subpart G, are applicable to the properties assisted or insured that are listed in § 200.853.

(b) *Entity responsible for inspection of property.* The regulations that govern the programs listed in § 200.853, or regulatory agreements or contracts, identify the entity responsible for conducting the physical inspection of the property which is HUD, the lender or the owner. For properties with more than one HUD insured loan, only the first mortgage lender is required to conduct the physical inspection. The second mortgage lender will be provided a copy of the physical inspection report by the first mortgage lender.

(c) *Timing of inspections.* (1) For a property subject to an annual inspection under this subpart, the inspection shall be conducted no earlier than 9 months and no later than 15 months from the date of the last required inspection. In no event, however, shall the physical inspection be conducted after the end of the calendar year following the one year anniversary date of the last required inspection.

(2) For a property subject to an inspection every two years under this subpart, the inspection shall be conducted no earlier than 21 months and no later than 27 months from the date of the last required inspection. In no event, however, shall the physical inspection be conducted after the end of the calendar year following the two year anniversary date of the last required inspection.

(3) For a property subject to an inspection every three years under this subpart, the inspection shall be conducted no earlier than 33 months and no later than 39 months from the date of the last required inspection. In no event, however, shall the physical inspection be conducted after the end of the calendar year following the three year anniversary date of the last required inspection.

(4) For a newly endorsed multifamily property, the first inspection required under this subpart will be conducted no earlier than 21 months but not later than 27 months from the date of final endorsement. In no event, however, shall the inspection be conducted after the end of the calendar year following the two year anniversary date of final endorsement.

#### **§ 200.857 Administrative process for scoring and ranking the physical condition of multifamily housing properties.**

(a) *Scoring and ranking of the physical condition of multifamily*

*housing properties.* (1) HUD's Real Estate Assessment Center (REAC) will score and rank the physical condition of certain multifamily housing insured properties listed in § 200.853 in accordance with the procedures described in this section. The physical condition inspection of the property, upon which REAC bases its score and ranking, is conducted by the responsible entity in accordance with § 200.855.

(2) Depending upon the results of its physical condition inspection, a multifamily housing property will be assigned one of three designations—standard 1 performing, standard 2 performing and standard 3 performing—in accordance with the ranking process described in paragraph (b) of this section.

(b) *Methodology for Ranking.* (1) Multifamily housing properties will be ranked in accordance with the methodology provided in this paragraph (b). Multifamily housing properties are scored on the basis of a 100 point scale. Because scores may include fractions, a score that includes a fraction below one half point will be rounded to the next lower full point and a score that includes a fraction of one half point or higher will be rounded to the next higher full point (e.g., 89.4 will be rounded to 89, 89.5 will be rounded to 90).

(i) *Standard 1 Performing Property.* If a property receives a score of 90 points or higher on its physical condition inspection, the property will be designated a standard 1 performing property. Properties designated as standard 1 performing properties will be required to undergo a physical inspection once every three (3) years.

(ii) *Standard 2 Performing Property.* If a property receives a score of 80 points or higher but less than 90 on its physical condition inspection, the property will be designated a standard 2 performing property. Properties designated as standard 2 performing properties will be required to undergo a physical inspection once every two (2) years.

(iii) *Standard 3 Performing Property.* If a property receives a score of less than 80 points, the property will be designated a standard 3 performing property. Properties designated as standard 3 performing properties will continue to undergo an annual physical inspection as currently required under covered HUD programs.

(2) Owners of multifamily housing properties scoring in a standard 1 or standard 2 range which have been cited by the REAC as having a Exigent Health and Safety (EHS) deficiency(s) must resolve the deficiency(s), as required by paragraph (c)(2) of this section, to be

classified as standard 1 and standard 2 properties.

(3) Regardless of the performance designation assigned to an owner's property, an owner is obligated to maintain its property in accordance with HUD's uniform physical condition standards as required by 24 CFR part 5, subpart G, the Regulatory Agreement and/or the Housing Assistance Payment (HAP) Contract. Good management principles require an owner to conduct routine inspections of its projects, develop improvement plans, and again, maintain its property to meet the standard of decent, safe, sanitary and in good repair.

(c) *Owner's review of physical inspection report and identification of objectively verifiable and material error.*

(1) Upon completion of a physical inspection of a multifamily housing property, the REAC will provide the owner or owner's representative, on the date of the physical inspection, notice of any items classified as EHS deficiencies. REAC also will provide the owner with the entire physical inspection report (electronically through the internet or by mail approximately 10 working days from the date of the report), which provides the physical inspection results and other information relevant to the inspection, including any items classified as EHS deficiencies and already provided to the owner, on the date of the inspection (EHS deficiencies are relayed by the inspector on the date of the inspection).

(2) The owner must carefully review the physical inspection report, particularly those items classified as EHS. The owner is also responsible for conducting its own survey of the total project based on the REAC's physical inspection findings. The owner must mitigate all EHS items immediately, and the owner must file a written report with the applicable Multifamily Hub Director within 3 business days of the date of the inspection, which is the date the owner was provided with the EHS notice. The report filed by the owner must provide a certification and reasonable evidence that the EHS items have been resolved.

(3) If, following review of the physical inspection results and score, the owner reasonably believes that an objectively verifiable and material error (or errors) occurred in the inspection, which, if corrected, will result in a significant improvement in the property's overall score ("significant improvement" is defined in paragraph (d)(4) of this section), the owner may request a technical review within the following period, as applicable:

(i) 15 calendar days from the date the owner receives the physical condition score from REAC if the results and score are electronically transmitted via the Internet to the owner; or

(ii) 30 calendar days from the date the owner receives the physical condition score from REAC if the results and score are transmitted to the owner by hard copy by certified mail.

(d) *Technical review of physical inspection results.* A request for a technical review of physical inspection results must be submitted in writing to the Director of the Real Estate Assessment Center and must be received by the REAC no later than the 15th calendar day or 30th calendar day, as applicable under paragraph (c)(3) of this section, following submission of the physical inspection report to the owner as provided in paragraph (c)(1) of this section.

(1) *Request for technical review.* The request must be accompanied by the owner's reasonable evidence that an objectively verifiable and material error (or errors) occurred which if corrected will result in a significant improvement in the overall score of the owner's property. A technical review of physical inspection results will not be conducted based on conditions that were corrected subsequent to the inspection. Upon receipt of this request from the owner, the REAC will review the physical inspection and the owner's evidence. If the REAC's review determines that an objectively verifiable and material error (or errors) has been documented and that it is likely to result in a significant improvement in the property's overall score, the REAC will take one or a combination of the following actions: undertake a new inspection; correct the original inspection; or issue a new physical condition score.

(2) *Burden of proof that error occurred rests with owner.* The burden of proof rests with the owner to demonstrate that an objectively verifiable and material error (or errors) occurred in the REAC's inspection through submission of evidence, which if corrected will result in a significant improvement in the property's overall score. To support its request for a technical review of the physical inspection results, the owner may submit photographic evidence, written material from an objective source such as a local fire marshal or building code official, or other similar evidence.

(3) *Material errors.* An objectively verifiable material error must be present to allow for a technical review of physical inspection results. Material errors are those that exhibit specific characteristics and meet specific

thresholds. The three types of material errors are as follows.

(i) *Building data error.* A building data error occurs if the inspection includes the wrong building or a building that was not owned by the property, including common or site areas that were not a part of the property. Incorrect building data that does not affect the score, such as the address, building name, year built, etc., would not be considered material, but is of great interest to HUD and will be corrected upon notice to the REAC.

(ii) *Unit count error.* A unit count error occurs if the total number of units considered in scoring is incorrect. Since scoring uses total units, the REAC will examine instances where the participant can provide evidence that the total units used is incorrect.

(iii) *A non-existent deficiency error.* A non-existent deficiency error occurs if the inspection cites a deficiency that does not exist.

(4) *Significant improvement.* Significant improvement refers to the correction of a material error, asserted by the owner, which causes the score for the owner's property to cross an administratively significant threshold (for example, the property would be redesignated from standard 3 performing to standard 2 performing or from standard 2 performing to standard 1 performing), or to result in an increase of 10 points or more.

(5) *Determining whether material error occurred and what action is warranted.* Upon receipt of the owner's request for technical review of a property's physical inspection results, the REAC will evaluate the owner's property file and the evidence provided by the owner that an objectively verifiable and material error occurred which, if corrected, would result in a significant improvement in the property's overall score. If the REAC's evaluation determines that an objectively verifiable and material error (or errors) has been reasonably documented by the owner and if corrected would result in a significant improvement in the property's overall score, then the REAC shall take one or a combination of the following actions:

- (i) Undertake a new inspection;
- (ii) Correct the inspection report; or
- (iii) Issue a new physical condition score.

(6) *Responsibility for the cost of a new inspection.* If a new inspection is undertaken by the REAC and the new inspection score results in a significant improvement in the property's overall score, then HUD shall bear the expense of the new inspection. If no significant improvement occurs, then the owner

must bear the expense of the new inspection. The inspection cost of a new inspection, if paid by the owner, is not a valid project operating expense. The new inspection score will be considered the final score.

(e) *Adjustment of physical condition score based on considerations other than technical review and reinspection.*

(1) Under certain circumstances, HUD may find it appropriate to review the results of a physical inspection which are anomalous or have an incorrect result due to facts and circumstances affecting the inspected property which are not reflected in the inspection or reflected inappropriately in the inspection. These circumstances include, but are not necessarily limited to, inconsistencies between local code requirements and the HUD physical inspection protocol; conditions which are permitted by variance or license or which are preexisting physical features non-conformities and are inconsistent with the HUD physical condition protocol; or cases where the owner has been scored for elements (e.g., roads, sidewalks, mail boxes, resident owned appliances, etc.) that it does not own and is not responsible for maintaining.

(2) To seek a score adjustment on the basis of these circumstances as provided in paragraph (e) of this section, the owner must submit a request for an adjustment to REAC with appropriate proof of the circumstances that resulted in the incorrect physical conditions results. This process may result in a reinspection and/or rescoring of the inspection after review and approval of the owner's submission of appropriate proof of the anomalous or inappropriate application.

(3) An owner may submit the request for this adjustment to REAC either prior to or after the physical inspection has been concluded. If the owner submits a request for adjustment after the physical inspection has been concluded, the owner must submit its request to REAC within 45 days following the submission of the physical inspection report, as provided in paragraph (c)(1) of this section. HUD may, but is not required to review a request made after this period has expired.

(4) This adjustment process, provided in this paragraph (g), may result in a reinspection and/or rescoring of the inspection after review and approval of the owner's submission of appropriate proof of the anomalous or inappropriate application.

(f) *Issuance of final score and publication of score.* (1) The physical condition score of the property is the final score if the owner files no request for technical review, as provided in

paragraph (c) of this section, or for other adjustment of the physical condition score, as provided in paragraph (e) of this section. If the owner files a request for technical review or score adjustments in accordance with paragraphs (c) and (e) of this section, the final physical condition score is the score issued by HUD after any adjustments are determined necessary and made by HUD at the conclusion of these processes.

(2) HUD will make public the final scores of the owners through posting on HUD's internet site, or through **Federal Register** publication or other appropriate means.

(g) *Owner's responsibility to notify residents of inspection; and availability of documents to residents.*

(1) *Notification to residents.* An owner must notify its residents of any planned physical inspections of their units or the housing development generally.

(2) *Availability of documents for review.* Once the technical review and database adjustment periods have expired, as provided in paragraphs (d) and (e) of this section, respectively, the owner must make its physical inspection report and all related documents available to its residents during regular business hours upon reasonable request for review and copying. Related documents include the owner's survey plan, plan of correction, certification and related correspondence.

(i) Once the owner's final physical condition score is issued and published, the owner must make any additional information, such as the results of any reinspection, appeal requests, available for review and copying by its residents upon reasonable request during regular business hours.

(ii) The owner must maintain the documents related to the physical inspection of the property, as described in this paragraph (g)(2), available for review by residents for a period of 60 days from the date of submission to the owner of the physical condition score for the property in which the residents reside.

(3) The owner must post a notice to the residents in the owner's management office and on any bulletin boards in all common areas that advises residents of the availability of the materials described in paragraphs (g)(2) of this section. The notice should include the name, address and telephone number of the HUD Project Manager.

(4) Residents are encouraged to comment on this information provided by the owners and submit any

comments directly to the applicable Field Office. Should residents discover the owner provided HUD with a false certification during the review they are encouraged to notify the Hub or Program Center where appropriate inquiry and action will be taken.

(h) *Administrative review of properties.* The file of a multifamily property that receives a score of 30 points or less on its physical condition inspection will be referred to HUD's Departmental Enforcement Center (DEC) for evaluation. The files of any of the multifamily housing properties may be submitted to the DEC or to the appropriate HUD Multifamily Hub Director (MFD) for evaluation, or both, at the discretion of the Office of Housing.

(1) *Notification to owner of submission of property file to the MFD and DEC.* The Department will provide for notification to the owner that the file on the owner's property is being submitted to the MFD and/or the DEC for evaluation. The notification will be provided at the time the REAC issues the physical inspection report to the owner or at such other time as a referral occurs.

(2) *30-Day period for owner to provide the DEC with supporting and relevant information and documentation.* The owner has 30 calendar days, from the date of the REAC notification to the owner, to provide comments, proposals, or any other information to the DEC which will assist the MFD and DEC in conducting a comprehensive evaluation of the property. A proposal provided by an owner may include the owner's plan to correct deficiencies (corrective action plan). During the 30-day response time available to the owner, the DEC may encourage the owner to submit a corrective action plan. The corrective action plan, if timely submitted during the 30-day period (whether on the owner's initiative or at the request of the DEC), may serve as additional information for the DEC to consider in determining appropriate action to take at the conclusion of the evaluation period. If not submitted during the 30-day response time, a corrective action plan may be required of the owner at the conclusion of the DEC's evaluation of the property.

(3) *Evaluation of the property.* During the evaluation period, the DEC will perform an analysis of the multifamily housing property, which may include input from tenants, HUD multifamily officials, elected officials, and others as may be appropriate. Although the MFD will assist with the evaluation, for insured mortgages, the DEC will have

primary responsibility for the conclusion of the evaluation of the property after taking into consideration the input of interested parties as described in this paragraph (h)(2). The DEC's evaluation may include a site visit to the owner's property.

(4) *Continuing responsibilities of HUD Multifamily Program Offices and Mortgagee.* During the period of DEC evaluation, HUD's multifamily program offices continue to be responsible for routine asset management tasks on properties and all servicing actions (e.g., rent increase decisions, releases from reserve account approvals). In addition, during this period of evaluation, the mortgagee shall continue to carry out its duties and responsibilities with respect to the mortgage.

(i) *Enforcement action.* If, at the conclusion of the evaluation period, the DEC determines that enforcement action is appropriate, the DEC will provide notification to the owner of the DEC's decision to formally accept the property for enforcement purposes.

(1) *DEC Owner Compliance Plan.* (i) After notification to the owner of the DEC's decision, the DEC will produce a proposed action plan (DEC Compliance Plan), the purpose of which is to improve the physical condition of the owner's property, and correct any other known violations by the owner of its legal obligations. The DEC Compliance Plan will describe:

(A) The actions that will be required of the owner to correct, mitigate or eliminate identified property deficiencies, problems, hazards, and/or correct any other known violations by the owner;

(B) The period of time within which these actions must be completed; and

(C) The compliance responsibilities of the owner.

(ii) The DEC Compliance Plan will be submitted to the MFD for review and concurrence. If the MFD does not concur, the DEC Compliance Plan will be submitted to the Deputy Assistant Secretary for Housing and the Deputy Director of the DEC for review and concurrence. If the DEC Compliance Plan remains unapproved, a final decision on the plan will be made by HUD's Deputy Secretary in consultation with the General Counsel, the Assistant Secretary for Housing, and the Director of the DEC.

(iii) Following submission of the DEC Compliance Plan to the owner, the owner will be provided a period of 30 calendar days to review and accept the DEC Compliance Plan. If the owner agrees to comply with the DEC Compliance Plan, the plan will be forwarded to the appropriate Multifamily Office for implementation and monitoring of completion of the plan's requirements.

(2) *Counter compliance plan proposal by owner.* The owner may submit an acceptable counter proposal to the DEC Compliance Plan. An owner's counter proposal to a DEC Compliance Plan must be submitted no later than the 30th day following submission of the DEC Compliance Plan to the owner. The DEC, in coordination with the MFD, may enter into discussions with the owner to achieve agreement to a revised DEC Compliance Plan. If the owner and the DEC agree on a revised DEC Compliance Plan, the revised plan will be forwarded to the appropriate

Multifamily Office for implementation and monitoring of completion of the plan's requirements.

(3) *Non-cooperation and Non-compliance by owner.* If at the conclusion of the 30th calendar day following submission of the DEC Compliance Plan to the owner, the DEC receives no response from the owner, or the owner refuses to accept the DEC Compliance Plan, or to present a counter compliance plan proposal, or if the owner accepts the DEC Compliance Plan or revised DEC Compliance Plan, but refuses to take the actions required of the owner in the plan, the DEC may take appropriate enforcement action.

(4) *No limitation on existing enforcement authority.* The administrative process provided in this section does not prohibit the Office of Housing, the DEC, or HUD generally, to take whatever action may be necessary when necessary (notwithstanding the commencement of this process), as authorized under existing statutes, regulations, contracts or other documents, to protect HUD's financial interests in multifamily properties and to protect the residents of these properties.

(j) *Limitations on material alteration of physical inspection software.* HUD will not materially alter the physical inspection requirements in a manner which would materially increase the cost of performing the inspection.

Dated: December 4, 2000.

**William C. Apgar,**

*Assistant Secretary for Housing—Federal Housing Commissioner.*

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