



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410

OF THE ASSISTANT SECRETARY FOR FEDERAL HOUSING COMMISSIONER

OCT 25 1983

MEMORANDUM FOR: All Regional Administrators-Regional Housing Commissioners
All Field Office Managers

ATTENTION: Loan Management Branch Chiefs
Assisted Housing Management Branch Chiefs

FROM: *Maurice L. Barksdale*
Maurice L. Barksdale, Deputy Assistant Secretary for Multifamily Housing Programs, HM

SUBJECT: Occupancy Policies for Subsidized Housing Cooperatives

While those portions of HUD Handbook 4350.3 which deal with the computation of rents and assistance payments apply to both rental projects and housing cooperatives, other parts of the handbook are not clear in terms of their applicability to cooperatives. The purpose of this memorandum is to clarify HUD's policies on those occupancy matters on which we have received numerous inquiries from both your staffs and industry representatives. Next year we will revise Handbook 4350.3, Occupancy Requirements for Multifamily Projects, to incorporate these and other policies related to cooperatives.

In most of these areas, our policy for cooperatives differs from the policy we have established for rental projects. The policy differences are justified by the homeownership and democratic characteristics of a cooperative. While management agents can unilaterally establish management policies at a rental project, at a cooperative policies are established by a board of directors that has been elected by the members. Several of the policies discussed in this memorandum were established in 1970 when we published the Model Form of Occupancy Agreement (Form FHA-3237 and FHA-3237B) and the Model Form of By-Laws for Cooperatives (Form FHA-3245).

1. Application Fees. Cooperatives may require prospective members to pay application fees if such fees are permissible under State and local laws. The application fee must be approved by the cooperative's board of directors. While the fee must be reasonable in amount and consistently applied, cooperatives need not submit the fee for Field Office approval. The cooperative must treat the application fee as an earnest money deposit. The application fee is not intended to cover the administrative expenses the cooperative incurs in processing applications. If the applicant is accepted for membership, the cooperative must apply the application fee to the purchase of the membership. If the applicant is rejected by the cooperative, the cooperative must refund the full application fee. The cooperative may retain the application fee only if the applicant backs out of the purchase transaction. While we do not permit rental

projects to collect application fees, we are permitting cooperatives to do so because application fees are traditional for homeownership transactions and admission to a cooperative requires completion of more complicated paperwork than does admission to a rental. Collection of an earnest money deposit will minimize instances in which the cooperative spends time and money processing the application and then the applicant backs out.

2. Credit Report Fees. In addition to the application fee discussed in Paragraph 1, the cooperative may charge an applicant for the cost of a credit report. Since this fee is intended to cover the cooperative's out-of-pocket cost, these fees are not refundable and need not be applied to the applicant's purchase costs. While we do not permit subsidized rentals to charge applicants for credit reports, we permit cooperatives to do so for the following reasons:
 - a. For any form of homeownership, it is standard industry practice to obtain credit reports and to make the applicant bear the cost of the credit report.
 - b. During initial occupancy, HUD required cooperatives to obtain credit reports on all applicants and many cooperatives have continued that policy as memberships are resold in later years.
 - c. Costs of credit reports for home-purchase-type transactions can be more expensive than those required for rental purposes.

3. Unit Size and Transfer Requirements. At the time of each member's initial occupancy, the cooperative must assign the member a unit in accordance with the unit size standards prescribed by Paragraph 2-11 of HUD Handbook 4350.3. If the number or composition of the household changes after initial occupancy so that unit size no longer meets the standards set forth in Paragraph 2-11, cooperatives must act in accordance with the unit transfer requirements discussed in Paragraphs a and b below. Enforcement of these unit transfer requirements will minimize instances in which unit-size and HUD's subsidy outlays are larger than justified by the household composition. Project regulatory agreements and program regulations give HUD authority to establish unit size requirements and the preamble and Articles 1, 13 and 21 of the Model Form of Occupancy Agreement give the cooperative authority to enforce unit size requirements. If a cooperative has not been enforcing unit size or transfer requirements, the cooperative should notify all members that it will do so in the future.
 - a. Units Occupied By Families Who Are Not Receiving Tenant-Based Subsidies. While we require rental projects to enforce Handbook 4350.3's unit transfer requirements for Section 236 and BMIR households, we do not require cooperatives to do so. Each cooperative may establish its own policy on whether the cooperative should: (1) offer over-housed members smaller units; and (2) require members, who refuse such offers, to pay the market rate carrying charge. For Section 236 cooperatives, the market carrying charge can be obtained from the HUD-approved rental

schedule. For BMIR cooperatives, the market carrying charge should be computed in accordance with Paragraph a(2)(a) of Item 46 of the HUD-50059 instructions that were included in Mr. Abrams' April 21, 1983 memorandum. HUD gives cooperatives this discretionary authority because: (1) members who do not receive tenant-based subsidies could have accrued substantial equity by virtue of their payments toward debt service and interior improvements approved by the cooperative; and (2) these members' continued occupancy does not cause HUD to pay unnecessary subsidy outlays.

- b. Units Occupied by Families Receiving Tenant-Based Subsidies (Rent Supplement, RAP or Section 8). Except as provided at the end of this paragraph, when an appropriately-sized unit becomes available a cooperative must require an over-housed member to either: (1) transfer to the appropriately-sized unit offered by the cooperative and continue to receive assistance; or (2) remain in the same unit and pay a higher carrying charge. The choice between option #1 and #2 rests with the member. In cooperatives developed under the Rent Supplement or Section 8 program, members who choose option #2 must pay the HUD-approved Rent Supplement or Section 8 carrying charge. In cooperatives developed under the BMIR or Section 236 program, members who choose option #2 must pay the carrying charge required by the policy the cooperative developed pursuant to Paragraph 3a above. If the cooperative elected to surcharge BMIR and Section 236 households who choose not to move to smaller units, the families discussed in this paragraph must pay the HUD-approved market carrying charge. If the cooperative chose not to impose such surcharges, these families must pay the HUD-approved BMIR or Section 236 basic carrying charge. When an appropriately-sized unit is available, a cooperative may permit an over-housed member to remain in the same unit and continue to receive Section 8/Rent Supplement/RAP assistance only as long as there is no market for the size of unit the member would be vacating.
4. Transfer Fees. A cooperative may collect fees for processing transfers of membership if such fees are approved by the Board and consistent with the cooperative's by-laws and occupancy agreements. While these fees must be reasonable in amount, the cooperative need not request HUD approval of the amount of the fee. HUD's Model Form of By-Laws for Cooperatives (Form FHA-3245) gives cooperatives the right to determine the amount of these fees. Section 8 of that Form states that "In all transfers of membership, the corporation shall be entitled to a fee it deems appropriate to compensate it for processing the transfer." While a strict literal interpretation of this clause of the By-Laws would mean cooperatives could collect transfer fees both when a member voluntarily initiates a transfer and when the cooperative forces a transfer pursuant to Paragraph 3 above, HUD did not intend to authorize cooperatives to collect fees in the latter instance. Imposing transfer fees in connection with forced transfers could discourage members from supplying required reports of changes in family composition. Hence, cooperatives may not charge transfer fees when transfers are required pursuant to changes in household composition.

5. Late Charges. Handbook 4350.3's restrictions on late charges do not apply to cooperatives. Cooperatives may collect any late charges that are approved by the Board and are consistent with the cooperative's organizational documents and local law. Since Article 18 of the Model Occupancy Agreement gives the Board the authority to determine the amount of the late charge, cooperatives need not submit the fee for HUD Field Office approval. That Article states that "the member shall pay to the corporation a late charge in an amount to be determined from time to time by the Board of Directors for each payment of carrying charges, or part thereof, more than 10 days in arrears."
6. Legal Fees and Eviction and Collection Costs. Cooperatives may collect legal and other out-of-pocket costs incurred in collecting delinquent carrying charges and in terminating a membership following a member's default under an occupancy agreement. Both Section 9c of HUD's Model By-Laws and Article 18 of the Model Occupancy Agreement authorize cooperatives to collect such charges. You should note that Article 18 of the Model Occupancy Agreement requires members to pay attorney fees even if a suit has not been filed. This differs from HUD's policy on legal costs in subsidized rental projects. Rental projects may accept court filing and sheriff fees tendered by tenants who wish to avoid or settle a suit but may charge tenants for administrative costs or attorney fees only after a court has authorized such charges. Any charges levied pursuant to this paragraph must be consistent with local and State law and policies approved by the cooperative's Board.
7. Recertifications. Cooperatives must enforce Handbook 4350.3's annual recertification requirements for both current and new members. Cooperatives must enforce Handbook 4350.3's interim recertification procedures only for all members who execute occupancy agreements after February 15, 1984. Prior to February 15, cooperatives must edit their occupancy agreement forms to incorporate Handbook 4350.3's interim recertification requirements and obtain your office's approval of the revised occupancy agreement form. Cooperatives may impose Handbook 4350.3's interim recertification requirements on current members only if the cooperative amends its By-Laws to make such requirements binding on all members or a member voluntarily agrees to include such clauses in his/her occupancy agreement.
8. Occupancy Agreement and the Model Lease. The Model Lease in HUD Handbook 4350.3 does not apply to cooperatives. Cooperative members should continue to use occupancy agreements. While cooperatives need not amend current members' occupancy agreements, all occupancy agreements executed after February 15, 1984 must incorporate the cooperative's policy on unit transfers and the recertification, termination of assistance and fraud penalties found in Paragraphs 15, 16, 17 and 25, respectively, of Handbook 4350.3's Model Lease.
9. Surcharges for Over-Income Members In BMIR Cooperatives. If a BMIR member's Annual Income exceeds 110% of the BMIR income limit at the time of recertification, the cooperative must surcharge the member as provided in Item 46, Paragraph a(2) of the HUD-50059 instructions. BMIR cooperatives no

longer need to prepare Form FHA-91709, Schedule of Computation of Rental Income in Excess of BMIR Rent Paid by Over-Income Tenants. Cooperatives also no longer need to hold surcharges available for deposit to residual receipts (as required by Handbook 4370.2, Paragraph 11) or to deposit surcharges with the mortgagee (as required by Handbook 4371.2, Paragraph 22). Effective immediately, Field Offices and cooperatives should account for and distribute surcharges in accordance with the guidance listed below. (Surcharge requirements for BMIR rentals will be clarified in a separate memorandum).

- a. If a cooperative has been placing surcharges in a separate escrow account, the cooperative should continue to do so until it submits its next operating budget for HUD approval. At that time, your staff should assess the adequacy of the cooperative's general operating reserve (GOR), replacement reserve and working capital and direct the cooperative as to how to apply the accumulated surcharges. Field Offices may require cooperatives to submit a projection of their future replacement needs if the projection will assist the Field Office in making these assessments. In determining the disposition of on-hand surcharges, Field Offices should usually adhere to the guidance provided below. Field Offices may authorize cooperatives to deposit surcharges in the operating account instead of funding reserve deficiencies only if the cooperative has cash flow problems or the surcharges will be used to meet critical operating needs.
 - (1) If the cooperative's replacement reserve balance and scheduled reserve deposits will not provide sufficient funds to meet future replacement needs, the Field Office must require the cooperative to apply the accumulated surcharges to the projected deficiency in the replacement reserve.
 - (2) If the replacement reserve is adequate but the cooperative has not made all required deposits to its GOR, the Field Office must require the cooperative to use the surcharges to make the past due GOR deposits.
 - (3) If Field Office determines that the the surcharges are not needed to fund GOR or replacement reserve deficiencies, the cooperative may deposit the accumulated surcharges in its project operating account.
- b. When preparing future operating budgets, cooperatives must estimate how much they will collect in surcharges during the upcoming year. The cooperative must show this estimate of surcharge income in the income portion of its operating budget. In reviewing each cooperative's operating budget, you should review the adequacy of the

various reserves the cooperative is required to maintain and assure that carrying charges are set at a level sufficient to meet any deficiencies in these required reserves.

- c. Cooperatives must account for surcharges separately from all other carrying charges. Surcharges collected from over-income members should be recorded in Account Number 5190, Miscellaneous Rental Income.

Please send a copy of this memorandum to each subsidized cooperative's Board and management agent and ask each cooperative to send you a description of its current or proposed policies in each of these areas. Your transmittal letter should ask cooperatives and management agents to direct any questions to your housing management staff. If your staff have any questions on this memorandum, they should call Matt Andrea of the Management Procedures Division on (202) 755-6870.