



GREGORY W. SULLIVAN
INSPECTOR GENERAL

The Commonwealth of Massachusetts
Office of the Inspector General

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July 31, 2012

Aaron Gornstein, Undersecretary
Department of Housing and Community Development
100 Cambridge Street – Suite 300
Boston, MA 02114

Dear Undersecretary Gornstein,

Enclosed is the final summary of the review conducted by this office regarding affordable tenant income certifications and the associated oversight in five randomly selected rental developments constructed under the commonwealth's affordable housing law (MGL Chapter 40B).

This office greatly appreciates the timely and professional manner in which the Department of Housing and Community Development ("Department") has addressed and responded to the draft findings and recommendations that this office shared with you this past May. Included is a copy of your letter dated June 22, 2012 where you provided responses to the recommendations discussed at our meeting. The actions highlighted in your letter that the Department will be undertaking to address the identified issues/concerns will strengthen the overall control and oversight process exercised by both Chapter 40B rental development owners and the project administrators in ensuring that affordable apartments developed under Chapter 40B are only occupied by income qualified households.

Please let me know if you need any assistance as you move forward with implementation of the identified changes. This office looks forward to future collaboration with the Department on other housing and community development issues.

Sincerely,

Gregory W. Sullivan

Gregory W. Sullivan
Inspector General

CC: The Honorable James Eldridge, Senate Chair, Joint Committee on Housing
The Honorable Kevin Honan, House Chair, Joint Committee on Housing
Steve Carvalho, DHCD Chief of Staff
Thomas Gleason, MassHousing Executive Director
Daniel Morgado, Town of Shrewsbury – Town Manager
Kathy Pryce-Jones, Avalon Affordable Housing Asset Manager
Richard Bluestein Esq., Counsel for Beacon Communities

Overview

This office reviewed the practices followed by the Department of Housing and Community Development (DHCD), the Massachusetts Housing Finance Agency (MassHousing) and two prominent rental developers/owners in the commonwealth - AvalonBay Communities, Inc. (Avalon) and Beacon Communities, LLC (Beacon) to provide reasonable assurance that only income qualified households are provided tenancy in the affordable apartment units developed under Chapter 40B, the commonwealth's affordable housing law.

Chapter 40B encourages the development of affordable housing by granting to developers waivers from zoning and other local ordinances and bylaws in return for an agreement from the developers to provide a percentage of the housing units to income-qualified affordable households (buyers and/or tenants) and a commitment from the developers or project owners to limit their development profit.

Previous investigations by this office of Chapter 40B home ownership projects identified pervasive abuse by developers of the limited dividend requirement. This abuse was enabled through lax oversight of the projects by the state government and subsidizing agencies, and a lack of independence and skepticism on the part of "independent" auditors and monitoring agents. We found that Chapter 40B developers are routinely able to profit above and beyond what is allowed by law to the detriment of taxpayers, municipalities, and local efforts to produce affordable housing.

In addition to the routine financial abuses engaged in by developers to shield their excess profits from municipalities, this Office's findings regarding the Chapter 40B home ownership program also included concerns about the purchase of affordable units by individuals who were not from income qualified households. These concerns, identified through our examination of certain home ownership development projects prompted this office to expand its review into Chapter 40B rental housing.

This report addresses five rental housing development projects built under the provisions of Chapter 40B. Four of these projects were developed by Avalon: Avalon at Flanders Hill (Westborough), Avalon at Newton Highlands (Newton), Avalon at Crane Brook (Peabody/Danvers) and Avalon Shrewsbury (Shrewsbury). One project was

developed by Beacon: the Cordovan at Haverhill Station (Haverhill). These five developments were randomly selected for review by this office.

Two of the projects developed and operated by Avalon were subsequently sold. Avalon at Flanders Hill was sold in 2009 to a Delaware limited liability company for \$40.8 million and is now known as Flanders Hill at Westborough. Avalon at Crane Brook was sold in 2011 to a Delaware limited liability company for \$64.5 million and is now known as 14 North.

Although, approximately 70% of the Chapter 40B projects proposed and/or built between 1997 and 2008 were homeownership developments these projects only comprise approximately 30% of the total affordable units proposed and/or developed during this timeframe. Conversely, Chapter 40B rental projects proposed and/or built between 1997 and 2008 encompass nearly 30% of all Chapter 40B projects but account for roughly 70% of the affordable units.

There are two primary reasons for this difference: the relative size of the developments and the policy/methodology for counting affordable units. Rental developments on average tend to be larger than homeownership developments. In rental housing developments, usually all the units in the development, including those rented at Fair Market Rents are counted as affordable units and are reflected in the Subsidized Housing Inventory (SHI) maintained by DHCD. Whereas in a homeownership development, only those units which are deed-restricted for sale to low or moderate income households are counted or included in the SHI.

Highlighted below is a summary of the five Chapter 40B rental development projects reviewed by this office. There were a total of 1,358 apartments in these developments with 345 of these units or 25% targeted for affordable households. Although only 25% of the units were targeted for affordable tenants, all 1,358 apartments are counted as affordable units in the SHI. If this had been a homeownership development only the 345 units targeted for sale to affordable buyers would be counted as part of the SHI.

Development	Location	Project Administrator	Total # of Units	Affordable Units
Avalon Flanders Hill	Westborough	MassHousing	280	70
Avalon Newton Highlands	Newton	MassHousing	294	74
Avalon Crane Brook	Peabody/Danvers	MassHousing	387	78
Avalon Shrewsbury	Shrewsbury	DHCD	251	63
Cordovan Haverhill Station	Haverhill	DHCD	146	61
TOTALS			1,358	345

Limited dividends or profits are another area of difference between rental and homeownership developments. Developers of Chapter 40B homeownership projects are typically limited to a 20% profit on the total development costs whereas annual dividend distributions to Chapter 40B rental developers/owners are limited to 10% of the owner's equity in the project. The determination of owner's equity is allowed to increase over time based on appraisal values versus actual development costs. Unlike homeownership projects, the current regulations do not establish any limits on profits from the sale of a rental development from one owner to another. There currently is no sharing of excess rental development profits associated with the sale of such a development. All financial benefits/profits derived from the sale of a rental development built under Chapter 40B inure to the developer with no profit share for the municipality.

Review Focus/Methodology

The primary focus of this office’s review was to determine the adequacy of the controls and oversight exercised by both the Chapter 40B rental development owners and the project administrators in ensuring that affordable apartments developed under Chapter 40B are only occupied by income qualified households.

As previously highlighted, Chapter 40B housing projects developed under Chapter 40B must include a percentage of “affordable” housing units. Typically in a rental development, at least 25% of the units must be restricted to moderate-income households (earning less than 80% of the “Area Median Income” (AMI)), or at least 20% of the units must be restricted to low-income households (those earning less than 50% of the AMI). The AMI is set by the Federal Office of Housing and Urban Development (HUD) and includes factors for the size of a family – larger families have proportionally larger AMI’s. As reflected in the matrix below, the five projects reviewed encompassed a diverse mix of affordability limits from 30% to 80% of AMI.

	Flanders Hill	Newton Highlands	Crane Brook	Shrewsbury	Cordovan
AMI Income Limit	# of Units	# of Units	# of Units	# of Units	# of Units
30%	NA	NA	31	NA	15
50%	NA	26	47	NA	NA
60%	NA	NA	NA	NA	46
65%	NA	11	NA	NA	NA
80%	70	37	NA	63	NA
Total Affordable Units	70	74	78	63	61

Both Beacon and Avalon employ internal staff specifically for compliance related activities. Avalon utilizes a centralized compliance department known as Avalon Blue Skies to certify its low and moderate-income tenants. Beacon utilizes both corporate and on-site staff to meet its compliance needs. Employees at both companies utilize pertinent subsidy program guidelines/federal guidelines including the HUD Occupancy Handbook 4350.3 to certify low-and moderate-income tenants.

The guidance from the HUD handbook is essential to a developer/owner like Beacon that utilizes federal subsidies to develop its projects. Recipients of federal subsidies are required to comply with federal rules and the handbook provides necessary operational guidance for these related affordable housing activities. Since DHCD's Chapter 40B regulatory structure and program guidelines provide limited guidance with respect to certifying low and moderate income tenants, the HUD handbook is also useful for a developer/owner like Avalon that does not typically develop a project by accessing federal funds. In accordance with the HUD handbook, both Avalon and Beacon require that affordable tenants periodically submit specific income and asset documentation in order to be certified as a qualified low and/or moderate income tenant.

In order to determine the adequacy of the procedures/controls related to the certification of low/moderate income tenants at these Beacon and Avalon developments, this office reviewed both the detailed income/asset verification procedures employed by both owners and the oversight provided by the project administrators (DHCD and/or MassHousing). This office selected a sample of tenants from one of the Avalon developments (Avalon Shrewsbury) and also a sample of tenants from the sole Beacon project (Cordovan at Haverhill Station). Tenant files for the sample of tenants selected for detailed testing were reviewed and the pertinent income and asset documentation was verified/reconciled against the tenant certification reports previously prepared by the project owners (Beacon and Avalon) and submitted to the respective project administrators (DHCD and MassHousing).

Some of the primary financial verifications performed and documentation reviewed by this office included the following as required in the HUD handbook:

- Employment verification including the three most recent and consecutive paystubs or a letter from an employer detailing employment status, hourly/annual salary, number of average hours worked per week, amount of potential bonus, amount and date of merit increase and the average number of overtime hours worked per week including overtime hourly rate and the three most recent years of W2's and 1099's.
- Social Security and Supplemental Security Income verification.
- Pension income statements or a letter from a pension provider documenting amount of gross monthly pension.

- Unemployment income statements detailing the amount due to the applicant on a weekly basis.
- Recurring Gift Form(s) detailing the amounts received from any party not residing with the tenant.
- Child support and alimony documentation including complete court decree reflecting court ordered amounts.
- Checking account and savings account bank statements.
- Most recent and complete statements for other assets including 401k, 403b, IRA, Keogh, stocks, bonds, trusts, capital investments, etc.
- Disclosure of real estate/property holdings, most recent tax assessment from the locality where the property is located and the most recent mortgage statement reflecting the mortgage balance.
- Copies of all lease agreements for rental properties.

In addition to the detailed sample testing performed by this office of the income verification/certification work performed by the project owners on the two developments selected, this office also reviewed the oversight procedures that were followed by the respective project administrators as part of their role for ensuring compliance to tenant affordability requirements.

Highlighted below are the associated findings based on this office's review.

Findings

Avalon Shrewsbury

Avalon Shrewsbury is a 251 unit development in the Town of Shrewsbury built under Chapter 40B using the Local Initiative Program (LIP). The project was completed in 2007. Sixty-three of the apartments are affordable units and are designated for tenants who earn less than 80% of the Area Median Income.

This office's review of a random sample of tenant files and the associated income/asset documentation supporting the income certifications performed by Avalon did not identify any material issues. However, the review highlighted some errors or omissions in Avalon's certification process; in one instance, Avalon failed to account for alimony income disclosed by a tenant in their income calculations. In two other instances, Avalon failed to account for assets held by its tenants. None of these lapses had a material financial impact that would have affected the income certification determinations for these tenants.

These mistakes notwithstanding, this office found that all tenant income certification documentation was readily available and complete. All tenant files reviewed included the financial statements/documents required by Avalon policy to certify low-and moderate-income tenants. This office does not believe the errors discovered during our review are indicative of a larger problem. These mistakes are related to clerical recording of the data onto the tenant certification reports submitted by Avalon to DHCD. In dealing with this office, the Avalon staff was professional and transparent about their tenant income certification process.

Although this office found that the Avalon income certification process is adequate for ensuring that Avalon Shrewsbury tenants are income-qualified and that the correct numbers of units are provided to moderate-income tenants, this office is concerned with the overall oversight process. We discovered that DHCD, the Town of Shrewsbury, and Avalon did not abide by the terms of the project's regulatory agreement and the associated LIP project guidelines regarding ongoing affordability oversight for the project.

Consistent with DHCD's LIP guidelines, the regulatory agreement for Avalon Shrewsbury states that the project owners "...shall certify at least annually to the Municipality whether the tenant of each low-and moderate-income unit remains an Eligible Tenant. This determination shall be reviewed by the Municipality and certified by the DHCD." Avalon, DHCD and the Town of Shrewsbury are each a party to the regulatory agreement.

In September 2010 this office contacted the Town of Shrewsbury in order to understand and examine the tenant certification review process employed by the town. At that time, Shrewsbury's Town Manager, Daniel Morgado, informed this office that the town was unaware of its obligation to review Avalon Shrewsbury's annual income certifications. Further, Mr. Morgado indicated that he had not heard from Avalon Shrewsbury since the project was completed in 2007.

Records obtained by this office demonstrate that Avalon submitted yearly certifications through its Blue Skies program to DHCD for the years ending in 2008, 2009, and 2010. Neither DHCD'S nor Avalon's records indicate that Avalon submitted a certification for the year ending in 2007. Although the documentation is missing, Avalon has reinforced to this office that it had in fact conducted a certification that year. However, contrary to the requirements of the regulatory agreement, Avalon did not submit these annual certifications to the Town of Shrewsbury. Avalon eventually submitted certifications for the years ending of 2009 and 2010 to the town but only because the town had requested this action after this office began its review.¹

Based on our review, it is apparent that although DHCD had received the annual certifications from Avalon, DHCD did not perform any independent verification of the information provided. DHCD did not request to review, even on a test basis, the backup documents supporting the income determinations submitted for each tenant. There was no communication from DHCD to the Town of Shrewsbury inquiring on the status of the town's required reviews. In fact, in 2007 when it did not receive a certification from

¹ This office contacted the Town of Shrewsbury in mid September 2010 to determine if Avalon had submitted certifications related to Avalon Shrewsbury. Avalon sent copies of the 2008 and 2009 income certification via email to Shrewsbury Town Manager, Dan Morgado, on October 8, 2010.

either Avalon or the town, DHCD did not pursue any follow-up action in order to remedy the situation.

In a positive turn of events, in 2011 officials from the Town of Shrewsbury met with representatives from this office regarding oversight of Avalon Shrewsbury. With cooperation from Avalon, town officials conducted an independent review/audit of Avalon Shrewsbury's low and moderate income certifications. This review led to an independent determination that the low and moderate income tenants in Avalon Shrewsbury were in fact income qualified for tenancy. It is the understanding of this office that Avalon reimbursed the town for all expenses incurred during the certification process. This office commends the Town of Shrewsbury and Avalon for their cooperative efforts to ensure the affordability of their low and moderate income housing.

The Cordovan at Haverhill Station

The Cordovan at Haverhill Station (Cordovan) was completed in 2007 and contains a total of 146 housing units that include sixty-one (61) affordable apartments. These affordable apartments at the Cordovan are targeted to a deeper level of affordability than the 80% of Area Median Income found at Shrewsbury Avalon. Forty-six (46) of the affordable units are targeted for households at 60% of the AMI and the remaining fifteen (15) affordable units are intended for households at 30% of the AMI.

Beacon financed the Cordovan through several means including Low Income Housing Tax Credits (LIHTC). Established by Congress under the Tax Reform Act of 1986, the LIHTC program funds the production of most of the nation's affordable housing stock. Tax credits provided by LIHTC offer a dollar-for-dollar reduction of an owner's tax obligations, which make them more valuable than tax deductions, which only reduce the qualified tax basis. Developers will often syndicate and sell tax credits to investors to generate project funding.

In Massachusetts, the LIHTC program is administered by DHCD. Recipients of LIHTC funding must comply with several government conditions/restrictions. DHCD publishes a Qualified Allocation Plan ("QAP") that specifies the obligations developers must meet under the program. These obligations are created by federal statute and regulations, notably the Treasury Regulations contained in 26 CFR §1.42-5. The regulations, and as

a result the QAP, provide detailed and structured program guidance for ensuring low and moderate income tenants are income qualified. Project owners are required at least annually to certify to DHCD under pains and penalties of perjury that the owner has received an annual income certification from each low income tenant along with documentation to support that certification. The owners must also certify; the number of units that were reserved for low income tenants, that the rents for those units were restricted, and that in cases of vacancy or low income tenants exceeding income limits the next available unit was designated as an affordable unit.

Under LIHTC, owners are also required to submit to periodic on-site record reviews. The initial on-site review must occur within two years of project completion. Subsequent reviews must occur at least once every three years thereafter. At least 20% of the affordable units in the development, chosen randomly, must be included in each on-site review. For smaller developments, a minimum of three units must be reviewed. As the Massachusetts LIHTC project administrator, DHCD contracts with Spectrum Enterprises, Inc. ("Spectrum") to conduct these reviews. Spectrum's role is to ensure that affordable apartments are rented to households truly qualified for them, and to ensure these homes are safe, secure and well maintained. Annually, DHCD reports to the Treasury its compliance monitoring activity related to these LIHTC projects.

Similar to the work done for the Avalon Shrewsbury project, this office reviewed a random sample of tenant files and the associated income/asset documentation supporting the income certifications performed by Beacon for its Cordovan development. This office found no issues with any of the tenant files that were sample tested. All documentation required to certify low-and moderate-income tenants was present, and each file reviewed reflected a yearly income certification for every applicable tenant. In addition, the income and asset figures reflected by the documentation provided by each tenant reconciled exactly with the figures calculated by Beacon. The files kept by Beacon were well organized, and worksheets and calculator tape were kept together with the income/asset documentation.

This office's review underscores both the meticulous work performed by Beacon in performing its annual tenant certifications and the proficiency of the oversight activities performed by DHCD/Spectrum in ensuring affordability for this LIHTC project.

Affordability Oversight - MassHousing

This office reviewed the oversight performed by MassHousing with respect to ensuring the affordability for three of the projects developed by Avalon. The review was focused on oversight activities carried out between 2007 and 2011 for the following developments: Newton Highlands (294 units) in Newton, Crane Brook (387 units) in Peabody/Danvers and Flanders Hill (280 units) in Westborough. As previously highlighted, two of these projects (Crane Brook and Flanders Hill) although originally developed by Avalon were subsequently sold and are currently under new ownership.

In terms of affordability, DHCD regulations require only that the *"holders of [a] Use Agreement provide for its monitoring and enforcement."* The regulations do not provide specific direction as to the methods and procedures that should be followed. MassHousing, as holder of the use agreements for the developments in Newton, Peabody/Danvers, and Westborough, requires that the owners submit an annual 40B Compliance Monitoring Spreadsheet. This spreadsheet identifies the affordable units, the tenants' names, the last date of income certification, any public subsidies, the rent charged, the move-in date, and the tenant's financial data (income and assets) at move-in. The spreadsheet serves as the document for project owners to certify tenant income under LIHTC or HUD guidelines for low-and moderate-income housing.

The 40B Compliance Monitoring Spreadsheets form the basis for MassHousing's review of a development's affordability and income certifications. This office requested from MassHousing all Compliance Monitoring Spreadsheets for the Newton Highlands, Crane Brook and Flanders Hill developments and all related findings, reports, communications, policies, and procedures covering the time period between 2007 and 2011.

This office's review found that MassHousing began requiring Compliance Monitoring Spreadsheets in 2010 and therefore did not receive any affordability/income certifications from the three developments for 2007 and 2008. MassHousing also does

not have written policies and procedures addressing compliance monitoring of affordable units in Chapter 40B developments.

Through its review process, MassHousing identified several instances of over-housed or over-income tenants in two of these developments. Although several of these tenant households were above the targeted income levels, none of these households exceeded the stipulated maximum income (140% of targeted income level) reflected in the respective regulatory agreements. This issue of over-income tenants is discussed in more detail in the subsequent section of this letter.

In addition to requiring 40B Compliance Monitoring Spreadsheets for these projects, MassHousing also conducts a yearly Project Management Review (PMR). PMRs end when a developer's mortgage to MassHousing is paid. The primary focus of the PMR's is the physical condition of the properties. Of the nine PMRs reviewed by this office between the years 2007 and 2010, three included an "Affordable Unit Compliance Report" – a spreadsheet listing all affordable units, the tenants, the last date of income certification, any public subsidy, and the rent charged.

Only one PMR, the 2009 Crane Brook PMR, indicated that MassHousing reviewed income documentation. The analyst conducting the PMR review recorded on a checklist that the files for Crane Brook were well organized, that management provided adequate notice for recertification and lease renewals, that third-party verification was obtained, and that the appropriate lease documentation was recorded. The analyst also certified that move-in procedures were conducted in a manner consistent with MassHousing guidelines.

Income Limit Policy Considerations

As previously highlighted, each project owner is required to make available a certain minimum number of apartments to income qualified households. The household income qualifications for these affordable tenants range from 30% of the Area Median Income (Crane Brook and Cordovan) to 80% of the Area Median Income (Flanders Hill, Newton Highlands and Shrewsbury). However, the regulatory agreements for each of these developments include language that permits tenant households, after their initial certification to earn up to 140% of the targeted income. In essence, a household earning up to 140% of the targeted income will continue to pay the reduced affordable rent and the apartments will continue to be categorized as affordable units in the subsidized housing inventory.

As part of the review, this office examined various tenant income certifications in order to determine whether the affordable apartments in each development were rented to income qualified households. Although this office found that in many instances (see below) the affordable households exceeded the targeted income levels, this office did not find any situations where the household income level exceeded the stipulated 140% maximum.

Summary findings by project for the most current certifications reviewed by this office are reflected below:

- Cordovan: two households or 3% of the total affordable units exceeded the targeted income levels – one of the households was at 112% of the targeted income and the other was at 128%.
- Newton Highlands: thirteen households or 18% of the total affordable units exceeded the targeted income levels – the incomes ranged from 101% to 138% of the targeted income, with the average at 118%.
- Flanders Hill: eight households or 11% of the total affordable units exceeded the targeted income levels – income ranged from 104% to 118% of the targeted income, with the average at 109%.
- Shrewsbury: six households or 10% of the total affordable units exceeded the targeted income levels – the incomes ranged from 102% to 130% of the targeted income, with the average at 114%.

- Crane Brook: due to the fact that the certification information provided did not identify the number of household members for each apartment, this office could not determine whether any of the tenant households were over the income limit.

It is the understanding of this office that the maximum income guideline stipulation at 140% of targeted income that is reflected in each of the regulatory agreements is based on the limits found in the LIHTC program. Although this guidance may be appropriate for low income projects that are developed using LIHTC it is the opinion of this office that this approach is not suitable for use in the moderate income developments. In order to qualify for LIHTC funding, a project typically must have a tenant income mix in which (a) 20% of the total units in the project are set aside for households at 50% of the AMI or less or (b) forty percent of the total units are set aside for persons earning 60% of the AMI or less. As previously highlighted, the Cordovan is the only project of the five reviewed that was funded using LIHTC. The Cordovan includes a total of 61 (42% of the total units) affordable units. Fifteen (10% of the total units) of the affordable units are targeted for households at 30% of the AMI or less and 46 (32% of the total units) units are targeted for households at 60% of the AMI or less.

Assuming conservatively that there was a household at the Cordovan that was at the maximum allowable income level – this household would still be below (at 84%) the AMI for the region. However, this is not the case for the other developments such as Flanders Hill, Newton Highlands and Shrewsbury. These non LIHTC funded projects include predominately moderate income as opposed to low income units. Applying the 140% guidance limit to many of these “affordable” units could result in tenancy by households that are above (by as much as 12%) the AMI for the region. Our review identified an “affordable” household, living in one of the developments that had income (in each year over a three year period) above the AMI for the region. In the opinion of this office this is not the intent of the affordable housing legislation.

Conclusion

Based on this review this office concludes the following:

- The affordable tenant income certification practices employed by Avalon and Beacon are reasonable and adequate;
- The state's oversight efforts regarding affordability for these five rental developments are mixed. DHCD's oversight of the sole LIHTC project reviewed (Cordovan) was adequate, detailed and structured and utilized the services of an external review firm (Spectrum) that is experienced in reviewing and ensuring income certifications. State oversight efforts for the other four developments reviewed were weak and do not provide adequate assurance that affordable tenants are income qualified. This office is of the opinion that the risk potential is exacerbated in those developments that are owned by companies that do not have the financial strength and internal focus/commitment that both Beacon and Avalon possess;
- There is a lack of documented policies and procedures addressing oversight of tenant affordability and the associated income certifications. Due to the absence of formal policies and procedures there is a lack of structure, consistency and direction for conducting reviews/audits of affordable tenant qualifications;
- The current practices (as reflected in each regulatory agreement) that provide for a maximum income guideline stipulation (after initial certification) at 140% of targeted income for both low income and moderate income units results in occupancy by tenants in moderate income apartments that are above the median income for the region. In the opinion of this office this practice runs counter to the spirit and intent of the Chapter 40B legislation and limits the housing opportunities of more financially deserving or needier households, and;
- The current practice of allowing developers/owners of Chapter 40B rental developments to sell/flip their projects with no limitation on developer profit, runs counter to the intent and spirit of the affordable housing legislation and adversely impact development of additional affordable housing. In the opinion of this office, this represents a significant financial opportunity for the development of additional affordable housing throughout the commonwealth.

Recommendations

As a result of the review, this office makes the following recommendations in order to improve the overall affordability for rental developments built under Chapter 40B. DHCD should:

- Establish through its regulations, clear directions for the project administrators of Chapter 40B rental developments. These directions should address the requirements for timely and thorough audits/reviews of affordable tenant income certifications and require that developers and owners certify tenant income according to LIHTC or HUD standards;
- Draft and publish detailed policies and procedures addressing requirements for oversight of Chapter 40B rental developments including but not limited to the frequency of reviews, the scope of the reviews, and the documentation standards required for certifying tenant income. Consideration should be given to implementing a process for all Chapter 40B rental developments similar to what is followed for LIHTC funded developments that includes oversight functions performed by an external firm (similar to Spectrum) hired by the state;
- Conduct a review of all LIP rental projects to ensure that each of these developments is in compliance with the associated guidelines and regulatory agreements and that the project oversight has not stalled as it had with respect to the Avalon project in Shrewsbury. DHCD should encourage municipalities to take an active role in the oversight process of these rental developments similar to the role that the Town of Shrewsbury is currently playing with respect to the Avalon project;
- Revise its current practice of allowing moderate income households (at 80% of AMI) after their initial income certification, to earn up to 140% of the targeted income and still be treated as qualified affordable tenants in the development. Consideration should be given to capping this upper limit to 110% of the targeted level for the moderate income apartments while maintaining the 140% limit for low income units, and;
- Revise its current practice and memorialize through its regulations the requirement that all sales/transfers of rental developments should trigger a cost certification for the project. Similar to homeownership projects, profits in excess of stipulated maximum limits should be targeted for payment to the local municipality and/or the commonwealth for use in developing additional affordable housing opportunities.



Commonwealth of Massachusetts
DEPARTMENT OF HOUSING &
COMMUNITY DEVELOPMENT

Deval L. Patrick, Governor ♦ Timothy P. Murray, Lt. Governor ♦ Aaron Gomstein, Undersecretary

June 22, 2012

Gregory W. Sullivan
Office of the Inspector General
John W. McCormack Building
One Ashburton Place, Room 1311
Boston, Massachusetts 02108

RECEIVED

JUN 26 2012

OFFICE OF THE INSPECTOR GENERAL

Re: Recommendations on Monitoring of Chapter 40B Rental Developments

Dear Inspector General Sullivan:

Thank you for a very productive meeting last month on issues related to Chapter 40B, including ongoing project monitoring for rental developments. During our meeting, you presented draft findings and recommendations regarding your office's review of five rental developments. As you requested, I am providing responses to your recommendations as follows:

1. The Department will develop standard procedures for the ongoing review of Chapter 40B rental developments. These procedures will provide guidance for all of the state subsidizing agencies on rental projects, including: rental documents to be reviewed; income eligibility requirements; income verification by independent third parties; rent levels; annual rent limitations; tenant files and tenant file management. As you have noted, the Low Income Housing Tax Credit Program follows strong procedures. LIP operating procedures will mirror LIHTC procedures to the extent possible.
2. The Department will examine existing LIP documentation and revise or expand it as necessary so that DHCD's monitoring practices for LIP rental projects are clearly described. At this time, DHCD anticipates procuring the services of a qualified monitoring contractor, such as Spectrum, to provide monitoring services for all LIP rental projects. Services will include, but not be limited to, site and unit inspections, file reviews, and tenant certification reviews. DHCD anticipates the contractor will be procured during FY13.
3. In accordance with your suggestion, the Department will review the status of existing LIP rental projects. The status of these projects has been reviewed previously, but it is timely to review the status again.

4. We have taken under advisement your concerns and recommendations regarding tenants whose incomes may increase up to 140% of the initial income limit after the first annual income certification. We will determine if we will modify this income limit after further consultation with the state and federal housing agencies and other stakeholders. This has broad ramifications because this income limit, used in conjunction with the "available unit rule," conforms to the standard established by the federal Low Income Housing Tax Credit Program. Consequently, it is required for projects using the tax credits and is generally utilized for most housing programs in the state and around the country. Any policy change would potentially impact all existing affordable rental developments in the Commonwealth that have received state subsidies, not just developments built pursuant to Chapter 40B.
5. All state subsidizing agencies are now using standard rental regulatory agreement provisions. The regulatory agreements now incorporate monitoring fees to ensure that rental developments are in compliance with annual certifications. We will further develop and standardize procedures for annual notices to the owner/developers of LIP developments.

I appreciate the review, analysis and recommendations that your office has performed. These will assist the Department as we continue our commitment to creating housing opportunities for low- and moderate-income individuals and families.

Sincerely,



Aaron Gornstein

Undersecretary for Housing and Community Development