



## **MSHDA Utility Allowance Policy and Procedures for LIHTC Developments: Preamble June 15, 2010**

The Michigan State Housing Development Authority (MSHDA) is issuing this Preamble to provide owners and management agents of conventionally financed LIHTC developments with a better understanding of MSHDA's Utility Allowance (UA) Policy. The UA Policy includes two new UA methods which MSHDA is implementing effective June 15, 2010 (Actual Consumption Method and HUD Utility Model). This document also provides an overview of the forms and reference documents used in applying the new methods.

The UA Policy and the accompanying documents are the sole authoritative source for utility allowance policy and procedures for all conventionally financed LIHTC developments in Michigan. The Policy may also serve as a handy reference guide to clarify which utility allowance method is required for all MSHDA-financed and/or federally assisted multifamily rental developments with LIHTC. Please contact MSHDA Asset Management for detailed information regarding the Asset Management Utility Allowance Policy and procedures for MSHDA financed developments.

### **Introduction:**

On July 29, 2008, the IRS published the long-awaited final utility allowance Regulations, which impacted the rents for Low Income Housing Tax Credit (LIHTC) properties with resident-paid utilities. The Regulations increased the types of utility data that owners may use to calculate resident-paid utility allowances by including three additional utility calculation methods (Agency Estimate-Actual Consumption Method, HUD Utility Model and Energy Consumption Method).

MSHDA is issuing a UA Policy and accompanying documents to implement two of the new methods (Actual Consumption Method and HUD Utility Model) in accordance with Final Treasury Regulations Section 1.42-10 (26 C.F.R. Part 1 Section 42 - Utility Allowances Regulations Update) effective May 2, 1994 and amended July 29, 2008. Each new method requires MSHDA's review, approval and the payment of an administrative fee per IRS Regulations.

### **Background Information:**

To qualify as a LIHTC rent-restricted unit, the Internal Revenue Code requires that a qualified resident's gross rent must not exceed 30 percent of the applicable income limitation. Gross rent includes the cost of utilities, if utilities are paid directly by the tenant.

### **Problems with the Original UA Methods:**

Prior to publication of the new UA Regulation, owners/management agents of conventionally financed LIHTC developments were limited to two options, PHA rates or estimates obtained from the local utility company. In the past, PHA rates have typically been higher than actual usage since they do not take into account the energy efficiency of newly constructed or rehabilitated properties and estimates from the local utility company have become increasingly difficult to obtain.

## **New UA Methods to Address Utility Allowance Problems**

The new UA Regulations should result in allowances that more accurately reflect the improved energy efficiency of newer LIHTC properties and provide owners with other options when uncooperative utility companies are not forthcoming with the estimates.

The new methods are:

- Agency Estimates (Actual Consumption Method) – MSHDA implementation date June 15, 2010
- HUD Utility Model – MSHDA implementation date June 15, 2010
- Energy Consumption Method (Engineer Model)– Requires an engineering study from an agency-approved engineer or qualified professional (MSHDA currently does not have an approved list of engineers or qualified professionals at this time, therefore this method is not currently available)

MSHDA's PHA rates for 2010 utilize the HUD Utility Model which should more accurately reflect the average utility rates for each region across the State. However, this method does not account for different construction ages, different appliance and mechanical efficiency levels, and varying construction qualities unique to individual developments.

## **MSHDA UA Policy**

In preparation for implementing these new processes, MSHDA participated in a number of conferences, trainings and discussions and participated in the sharing of best practices ideas with industry experts and State Housing Finance agency staff from across the nation. MSHDA also developed a cross-divisional Utility Allowance Team consisting of staff members from Compliance (Legal Affairs), Asset Management, Rental Development and Homeless Initiatives (RDHI) and Housing Voucher Programs with the goal of obtaining consistency in UA Policies and Procedures throughout the Authority whenever and wherever possible. Finally, MSHDA Compliance staff worked directly with several owners/management agents to test the proposed process and data collection spreadsheet with actual consumption data. While some Housing Finance Agencies have already implemented new processes/procedures for some or all of the allowable methods, many others are still struggling with the administrative burden and time consuming process of creating and monitoring these new complex processes within their resource limitations.

## **Utility Allowance Documents and Forms**

- **Utility Allowance Policy for LIHTC Developments** – The policy consists of the following subparts: Summary of Final IRS Regulation, outline of utility allowance requirements by funding source, new methods MSHDA is implementing effective June 15, 2010, summary of methods, process overview for Agency Estimate (Actual Consumption Method and HUD Utility Model) and utility allowance administrative fees (applies only to new methods)
- **Utility Allowance Quick Reference Chart**
- **Utility Allowance Instructions for Agency Estimates (Actual Consumption Method)**
- **Consumption Data Certification Workbook**
  - Instructions
  - Consumption data collection spreadsheet
  - Utility Allowance Owner's Certification – Owner's certification of data accuracy

- **Resident Release Authorization Form** – provides resident’s authorization for utility company to release resident consumption data to owner/management agent

## **IRS and HUD Reference Documents**

The following documents were utilized and relied on when MSHDA Compliance staff prepared the UA Policy and Procedures:

IRS Utility Allowance Regulations:

Treasury Regulations Section 1.42-10

<http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&sid=60897a77f3aa6e576afe89369edad3ff&rqn=div8&view=text&node=26:1.0.1.1.1.0.5.83&idno=26>

IRS Notice 2009-44 (Sub-metered Utilities)

<http://www.irs.gov/pub/irs-drop/n-09-44.pdf>

Treasury Regulations

[http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&tpl=/ecfrbrowse/Title26/26cfrv1\\_02.tpl](http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&tpl=/ecfrbrowse/Title26/26cfrv1_02.tpl)

HUD Utility Model

The HUD model calculates different allowances, depending on when the project was built and where it is located.

<http://www.huduser.org/resources/utlmodel.html>

## **Draft Policy Comment Period:**

MSHDA invited the general public, and specifically owners/management agents, to provide written and electronic comments and feedback during a 14 day comment period which began on May 17 and ended May 31, 2010. The final UA Policy and accompanying documents were issued on June 15, 2010. Active owner/management agent participation and communication was essential to that process.

## **Ongoing Policy and Procedures Review:**

MSHDA anticipates an ongoing review of the UA Policy and Procedures will lead to further refinements and improvements. Please submit questions and comments by email to:

[mshdacompliance@michigan.gov](mailto:mshdacompliance@michigan.gov) Include “UA Policy Comments” in subject line.

MSHDA Compliance Website Link

[http://www.michigan.gov/mshda/0,1607,7-141-8002\\_26576---,00.html](http://www.michigan.gov/mshda/0,1607,7-141-8002_26576---,00.html)



LIHTC Compliance Policy #9  
Effective Date June 15, 2010

## **Michigan State Housing Development Authority Policy Statement**

### **Utility Allowances for LIHTC Developments**

On July 29, 2008, the IRS issued final Treasury Regulation Section 1.42-10 (26 C.F.R. Part 1 Section 42 - Utility Allowances Regulations Update) which includes three additional methods for calculating utility allowances. These additional methods are for conventionally financed Low Income Housing Tax Credits (LIHTC) projects. Please read these regulations carefully. The purpose of this Policy Statement is to outline the utility allowance calculation methods and clarify which method(s) an owner of a LIHTC project may utilize. This Policy Statement also provides a summary of the procedure to follow when requesting a utility allowance change for a LIHTC project.

#### **Background**

Owners of projects financed with LIHTC must limit rents and incomes to no more than 50% or 60% (depending upon the minimum set-aside) of Area Median Gross Income (AMGI), which MSHDA publishes annually, based on HUD's income limits. If a utility (other than telephone, cable television or internet) is paid directly by the tenant(s) and not by or through the owner of the building, the utility must be included in the utility allowance. Gross rent includes tenant paid rent plus the utility allowance. Telephone, cable television and internet are specifically excluded by statute (unless mandatory for building security purposes in which case they are included in gross rent). Utility allowances are applied individually to each building in the project. The IRS regulation requires owners to review all utility rates at least once during the calendar year and update the utility allowance if there is a change.

MSHDA annually publishes gross rent limits on the Compliance website, which includes utility allowances for all tenant-paid utilities, including electricity, water, sewer, gas, trash removal and any other mandatory fees. Fees charged to the residents for utilities the owner pays directly to the utility company are considered rent, unless the units are sub-metered to account for actual consumption by the household.

#### **IRS Notice 2009-44 – Sub-metered Utilities**

On May 5, 2009, the IRS issued Notice 2009-44 to clarify IRS Regulation 1.42-10 regarding sub-metered utilities. Owners can charge residents for utility charges if the units are individually metered and these charges can be billed through a third-party service. Actual service charges incurred may be passed on to residents, but the charges cannot exceed \$5 per unit. Such charges are not included in gross rent. Fees may only be assessed for services provided after May 5, 2009. Owners may not bill residents for prior charges. The notice does not indicate methods such as RUBS (Ratio Utility Billing Systems) are acceptable, therefore RUBS is not an allowable method in Michigan.

## Summary of Utility Allowance Calculation Methods

There are seven methods established in law, rule or regulation that owners can use to calculate a utility allowance:

1. Rural Housing Service (RHS, RD or USDA)
2. Housing and Urban Development (HUD)
3. Public Housing Authority Rates (PHA)
4. Local Utility Company Estimates
5. Agency Estimates (Actual Consumption) (*IRS effective date 1/1/09*)
6. HUD Utility Model (*IRS effective date 1/1/09*) or
7. Energy Consumption Model (Engineer Model) (*IRS effective date 1/1/09*)  
**(Michigan does not have an approved list of engineers/professionals at this time, therefore this method is currently not available)**

### #1 - Rural Housing Service Assisted Buildings:

Projects financed with Rural Housing Service (formerly FmHA) 515 loans or receiving rental assistance from RHS, must utilize the RHS approved utility allowance method for all restricted units. Copies of the RHS approved utility allowance must be provided to MSHDA (or its contractors) during file reviews and with the submission of the Annual LIHTC Owner's Certification in the year-end reporting process.

Projects financed with RHS 538 loans must follow method #5 below.

### #2 - HUD Regulated Buildings or Units:

**Buildings** with project-based rental assistance where the rents and utility allowance are reviewed by HUD or the designated contract administrator (PBCA) each year must use the applicable HUD utility allowance for all units in the building. Copies of the HUD approved utility allowance must be provided to MSHDA (or its contractors) during file reviews and with the submission of the Annual LIHTC Owner's Certification in the year-end reporting process. If buildings are restricted by both HUD and RHS, the RHS allowances must be used for those buildings.

**Units** occupied by residents receiving HUD assistance (Section 8 voucher) must use the HUD utility allowance from the Public Housing Authority (PHA) administering the assistance (MSHDA or local PHA) regardless of the utility allowance used for the remainder of the units in the building.

**In summary, buildings regulated by Rural Housing (515 loans), must utilize method #1 to calculate utility allowances. Buildings regulated by Rural Housing (538 loans), must utilize method #5 to calculate utility allowances. Buildings regulated by HUD or units utilizing HUD Assistance must utilize method #2 to calculate the utility allowances. MSHDA financed buildings (Section 8, Section 236 or Bond) must submit utility allowance requests and data to the MSHDA Asset Manager for approval (see method #5).**

**If a building (or unit) is not RHS assisted, HUD regulated or MSHDA financed, utility allowances for rent-restricted units in the building must be determined using one of the following methods:**

### **#3 - PHA Utility Allowance Rates**

Public Housing Authority (MSHDA or Local PHA) utility allowances may be obtained and utilized for the building. Copies of the PHA utility allowance documentation must be provided to MSHDA (or its contractors) during file reviews and with the submission of the Annual LIHTC Owner's Certification in the year-end reporting process.

### **#4 - Utility Company Estimates**

Utility company **estimates** may be obtained in writing from a local utility provider. This method requires written documentation from the utility company stating that the rates are "estimates for this project". For this method, the utility company provides the estimated cost of that utility for units of similar size and construction for the geographic area in which the building is located. A copy of the utility company estimates and backup documentation must be provided and retained by the owner of the building and a copy provided to MSHDA (or its contractors) during file reviews and with the submission of the Annual LIHTC Owner's Certification in the year-end reporting process. A copy must be sent to MSHDA and must also be made available to the tenants of the building.

**Important Note:** *utility "averages" are not the same as utility "estimates" (see #5 for more information regarding averages).*

### **For Deregulated Utility Service Areas**

The IRS regulation requires that the written local estimate must include all "component deregulated charges" for providing the utility service. In deregulated areas (entire State of Michigan), an estimate from one utility company is allowed even if several companies can provide the same utility service to the unit. However, in order for that utility company's rates to be used, the estimate must come from a provider that actually offers utility services to the building.

### **#5 - Agency Estimates (Actual Consumption Method)**

#### **MSHDA Financed Projects**

If a building is MSHDA financed (Section 236, Bond, HOME, 1602, and TCAP developments), owners/management agents must submit actual consumption data to the assigned Asset Manager according to the established policies and procedures of MSHDA's Office of Asset Management during the budget process.

Developments with project based Section 8 will need to submit actual consumption data to the Contract Administrator 60 days prior to the annual HAP Contract anniversary date.

#### **LIHTC Projects (without MSHDA Financing)**

An owner may calculate utility allowances using actual utility company consumption data. A summary of the procedures for this method is included in this Policy. Owners wishing to utilize this method must follow the guidelines set forth in this policy and the detailed instructions and submit the required forms, which are available under Utility Allowances in the forms section of MSHDA's Compliance website at the address below. Payment of an administrative fee is required for those wishing to utilize this

method (see Fee section below). MSHDA Compliance must approve the estimates prior to implementation of the utility allowances.

[http://www.michigan.gov/mshda/0,1607,7-141-8002\\_26576\\_26589---,00.html](http://www.michigan.gov/mshda/0,1607,7-141-8002_26576_26589---,00.html).

#### **#6 - HUD Utility Model**

An owner may calculate utility allowance estimates using the HUD Utility Schedule Model which is found on the HUD web site at [www.huduser.org/datasets/lihtc.html](http://www.huduser.org/datasets/lihtc.html). A summary of the procedures for this method is included in this Policy. Owners using this model will need to provide MSHDA with documentation providing the source and content of all factors entered into the model spreadsheet. This model requires the identification of a weather station in close proximity to the project and requires the owner to collect local utility rate data. Payment of an administrative fee is required for those wishing to utilize this method (see Fee section below) and MSHDA Compliance must approve the estimates prior to implementation of the utility allowances.

#### **#7 - Energy Consumption Model**

**MSHDA does not have an approved list of engineers/qualified professionals, therefore the Energy Consumption Model is not available for utility allowances in Michigan at this time.**

IRS regulations for the Energy Consumption Model state that “utility consumption estimates must be calculated by either a properly licensed engineer or a qualified professional approved by the agency that has jurisdiction over the building”. When implemented, this method will require owners to calculate utility estimates using an energy and water sewage consumption analysis model. The model must take into account factors including unit sizes, building orientation, design and materials, mechanical systems, appliances and characteristics of the building location.

#### **Projects Excluded from Submitting Utility Allowance Change Requests (Methods #5, #6 and #7)**

Projects meeting any of the following conditions are excluded from submitting a utility allowance request to MSHDA Compliance.

1. The project has any unresolved non-compliance issues (including but not limited to uncorrected 8823). Until such time as compliance deficiencies are remedied, the project cannot submit utility allowance change requests under the Actual Consumption or HUD Model methods.
2. The project is not able to provide twelve months of continuous utility usage data. New projects must use the PHA rates (method #3) until one year of actual consumption data is available. If it is not possible to submit the required sample size containing units that meet the continuous occupancy standard due to high vacancies or other extenuating circumstances, the owner must utilize an alternative calculation method. If the required sample data is available for some, but not all of the unit types, please contact MSHDA Compliance for additional guidance.
3. The project is RHS assisted or HUD-regulated. These projects must continue using the required utility allowance as defined in IRS Regulation IRS 1-42.10.
4. The project is MSHDA financed. These projects must submit actual consumption data to the assigned Asset Manager according to the established policies and procedures

of MSHDA's Office of Asset Management. New construction projects must use the PHA rates (method #3) until one year of actual consumption data is available.

### **Notification Requirements and Effective Dates (Method #3)**

Utility allowances must be implemented and rents adjusted (if applicable) no later than 90 days after the new utility schedules are published/effective.

### **Notification Requirements and Effective Dates (Methods #4, #5, #6 and #7)**

Owners must provide notification to MSHDA and the residents at the beginning of the 90 day period established in Regulation 1.42-10. The notification date begins on the date MSHDA receives the utility allowance request. The effective date to begin using an approved utility allowance is after the end of the 90 day period. Owners are required to make utility estimates available to the residents and MSHDA at the beginning of the 90 day period. Increases in rents due to changes in the utility allowance are not allowed prior to the end of the 90 day period.

MSHDA will review the utility allowance request during the 90 day period and will request additional information if necessary. MSHDA will issue an approval/acknowledgement letter prior to the proposed effective date of the utility allowance change. The owner must pay all costs incurred in obtaining utility estimates and providing notification to MSHDA and residents. Approved utility allowance changes cannot be implemented prior to the end of the 90 day period even if the owner receives MSHDA approval prior to that date.

### **Annual Utility Allowance Requirements**

Utility Allowance Documentation forms must be submitted to MSHDA annually along with the LIHTC Owner's Certification in the year-end reporting process.

For developments utilizing methods #4, #5, #6 or #7, utility allowances must be reviewed, updated and submitted to MSHDA at least 90 days prior to the one year anniversary of the effective date of the utility allowance change. The submission of Utility Allowance Documentation forms and other backup documentation is required before any change in utility calculation can be approved. It is permissible to change calculation methods from year to year.

### **Administrative Fees (Methods #5, #6, #7)**

All requests for approval of utility allowance changes under the following methods require a fee to be submitted with the request. Fees are noted below. Requests will not be reviewed until the required fee has been received:

- Actual Consumption (#5) - \$3 per unit in the project with a minimum of \$50 and a maximum of \$300
- HUD Utility Model (#6) - \$150 Fee Per Project
- Energy Consumption Model (#7 **method not available at this time**)

## **Summary of Process for Actual Consumption (#5) and HUD Utility Model (#6)**

### **Step #1 Submit Utility Allowance Change Requests**

A request for utility allowance change may be submitted to the Authority at any time during the year; however requests may not be submitted more frequently than once per year. The Owner Utility Allowance Certification forms (Certification) must be updated annually, even if a change is not requested. A request to change utility allowances must be submitted to MSHDA at least 90 days prior to the implementation date of the proposed change.

**Required Documentation – Actual Consumption (#5)** - Owners are required to submit information from the utility provider showing actual usage and rates. Actual consumption data must be no more than 60 days old when submitted to MSHDA for review. Sample data must include twelve months of utility invoices for a representative number of continuously occupied units (occupied 50 of 52 continuous weeks) as specified in the utility allowance instructions. The Certification must be signed by the owner or an authorized management agent representative. The effective date of the Certification may be no later than 60 days beyond the end of the twelve month period used to calculate the utility allowance.

**Required Documentation – HUD Utility Model (#6)** - Owners using this model will need to provide MSHDA with documentation providing the source and content of all factors entered into the model spreadsheet. This model requires the identification of a weather station in close proximity of the project and requires the owner to collect local utility rate data.

### **Step #2 Owner Estimate Reviews, Approvals and Denials**

Owners that submit complete and accurate information will receive email notification from MSHDA within 45 days of receipt of the information approving the request, or requesting additional information. Owners who do not receive an email within 45 days must contact MSHDA Compliance. Non-receipt of an email is not considered MSHDA approval. If MSHDA grants approval of the actual consumption or HUD Utility Model estimates, the approved utility allowance will be effective for one calendar year. The owner is responsible for submitting a new request 90 days before the expiration of the utility allowance in effect.

Owners/Management Agents must provide a copy of the current Certification to MSHDA (or its contractors) during file reviews and with the submission of the Annual LIHTC Owner's Certification in the year-end reporting process. Owners not able to obtain adequate consumption history from the utility company must utilize an alternative methodology to calculate the utility allowance.

Certifications from previous years and backup documentation may be requested by MSHDA (or its contractors) when conducting file reviews or year-end reports. Failure to provide the utility allowance certifications or documentation will result in a noncompliance violation.