New York State Office of the State Comptroller
Thomas P. DiNapoli

Division of State Government Accountability

The 80/20 Housing Program

Homes and Community Renewal
Housing Finance Agency

Report 2015-S-83

May 2017

Executive Summary

Purpose

To determine whether housing developers participating in the Housing Finance Agency's 80/20 Program complied with Program requirements regarding the number of designated affordable units and tenant eligibility; and to analyze the costs and resources used to achieve program results at four participating developments. The audit scope included the 68 developments in the 80/20 Program, that were occupied and had allocated 20 percent of their apartments to low-income tenants, between January 1, 2012 and December 31, 2015.

Background

Homes and Community Renewal (HCR) is an umbrella entity consisting of all the State's major housing and community renewal agencies and authorities, including the Housing Finance Agency (HFA). HFA's mission is to create and preserve high-quality, affordable, multifamily rental housing. Its 80/20 Program (Program) provides low-interest financing to multifamily rental developers who commit to designating at least 20 percent of a development's units to low-income households. The federal government provides income tax credits, and municipalities provide real estate tax abatements, as incentives to developers. In New York City, participating Program developers receive tax abatements through Section 421-A of New York's Real Property Tax Law. As of December 31, 2015, 68 developments, mostly in Manhattan, were occupied and had allocated 20 percent of their apartments (approximately 4,500 units) to low-income tenants. The remaining 80 percent are rented at market rates, but are subject to rent stabilization.

The U.S. Department of Housing and Urban Development defines very low-income (low-income) as 50 percent of an Area's Median Income (AMI) adjusted for household size. For a New York City family of four, the 2016 income eligibility limit was $45,300. Applicants must earn less than the income limits for their respective household size to qualify for these low-income units. Also, once tenants move into an affordable apartment, they may continue to reside in their unit regardless of their income and continue to pay the affordable rent amount.

If the household income of a tenant in a low-income unit exceeds 140 percent of the allowable income, the next available unit in the building, of comparable size (whether affordable or market rate), must be rented to a low-income tenant to maintain the 80/20 ratio. However, developers in New York City have opted to offer 15 percent of their designated low-income units to households with incomes below 40 percent of AMI. These units are referred to as "deep rent skewed." Under this option, if the income of a tenant in a low-income unit (including deep skewed units) exceeds 170 percent of the income limit, the next available low-income unit must be rented to a deep skewed tenant. Thus, under the deep rent skewed option, the next available market rate unit does not have to be offered to a low-income tenant. Tenants who exceed the 170 percent income limit continue to pay the low-income rents and additional units are not made available for other low-income parties.

Key Findings

• Based on the rents charged and the regulatory agreements for our four sampled developments, we concluded that the proper numbers of affordable apartment units were made available to low-income tenants.

- We reviewed a sample of 43 low-income tenants and found that, in most cases, the developments used "reasonable judgment" in determining eligibility, based on the information in the files. However, for 4 of the 43 tenants sampled, we question whether the developers exercised reasonable judgment in evaluating tenant file information.
- While the Program requires all applicants and adult family members to sign consent forms authorizing developments to collect information to verify applicant incomes, not all developments took this step. For 18 (42 percent) of the 43 tenants reviewed, applicant incomes were not verified with the Internal Revenue Service (IRS).
- The incomes of about one-third of the original tenants in the 68 developments exceeded the income eligibility limits, in effect during the audit period, for an applicant to move into a unit. In fact, as of December 31, 2015, more than 160 households occupying low-income units reported incomes of greater than $100,000.
- The total benefits to developers to create the 363 affordable units in our four sampled developments could not be fully calculated. Benefits that could be quantified (local tax abatements per Section 421-A and federal tax credits) amounted to almost $427.3 million for the four sampled developments. This did not include the benefits of HFA low-interest loans.

Key Recommendations

- Require Program developments to verify the incomes of all prospective tenants, prior to moving into an apartment, with the IRS.
- Work with the management staff at participating Program developments to develop sound and consistent methodologies to project applicant income when determining eligibility.
- Ensure that adequate information is collected to enable decision makers to adequately assess the costs and benefits of the Program.

Other Related Audits/Reports of Interest

New York City Department of Housing Preservation and Development: Enforcement of Mitchell-Lama Surcharge Provisions (2015-N-3)
Affordable Housing Corporation: Affordable Home Ownership Development Program (2013-S-31)

State of New York
Office of the State Comptroller

Division of State Government Accountability

May 31, 2017

Ms. RuthAnne Visnauskas
Commissioner/Chief Executive Officer
Homes and Community Renewal
Hampton Plaza
38-40 State Street
Albany, NY 12207

Dear Ms. Visnauskas:

The Office of the State Comptroller is committed to providing accountability for tax dollars spent to support government-funded services and operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of the Housing Finance Agency entitled *The 80/20 Housing Program*. This audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution, Article ll, Section 8 of the State Finance Law, and Article X, Section 5 of the State Constitution.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

Office of the State Comptroller
Division of State Government Accountability

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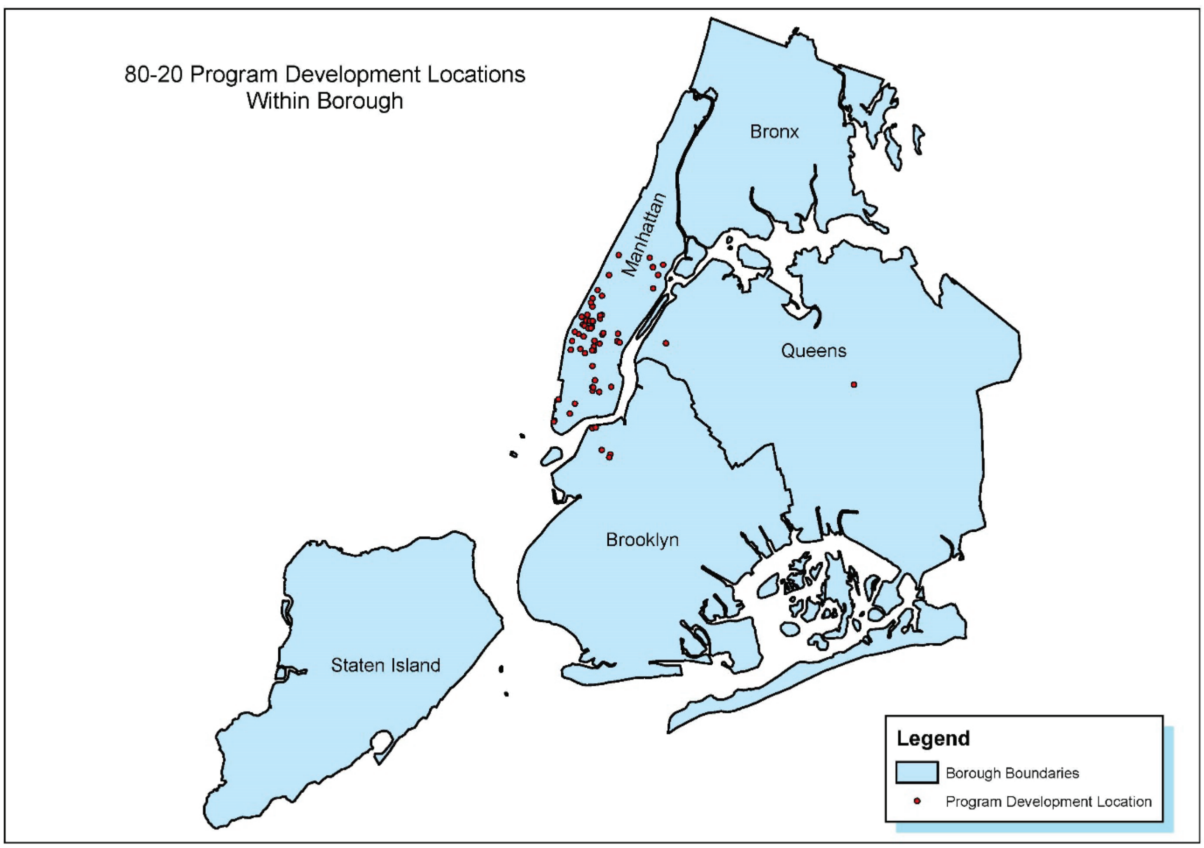
Background

Homes and Community Renewal (HCR) is an umbrella entity consisting of all the State's major housing and community renewal agencies and authorities, including the Housing Finance Agency (HFA). HFA's mission is to create and preserve high-quality, affordable, multifamily rental housing. Its 80/20 Housing Program (Program) provides low-interest financing to multifamily rental developers who commit to designate at least 20 percent of a development's units to low-income individuals and families. The federal government provides income tax credits, and municipalities provide real estate tax abatements, as incentives to developers. In New York City, participating Program developers receive tax abatements through Section 421-A of New York's Real Property Tax Law.

HFA has offered this Program to developers since 1990. During the period January 1, 2012 through December 31, 2015, 93 housing developments participated in the Program. As of December 31, 2015, 68 developments, mostly in Manhattan, were occupied and had allocated 20 percent of their apartments (approximately 4,500 units) to low-income tenants. The remaining 80 percent are rented at market rates, but are subject to rent stabilization.

The following map shows the locations of the 67 developments located in New York City. (Note: The remaining development is located in Rochester, New York.)



The U.S. Department of Housing and Urban Development (HUD) provides guidance for housing programs and defines very low-income (low-income) as 50 percent of an Area's Median Income (AMI) adjusted for household size. For a New York City family of four, for example, the 2016 income eligibility limit was $45,300. Applicants must earn less than the income limits for their respective household size to qualify for these low-income units. However, once tenants move into an affordable apartment, they may continue to reside in their unit regardless of their income and continue to pay the affordable rent amount.

Tenants occupying low-income units must report their respective incomes to building management annually. If the household income in a low-income unit exceeds 140 percent of the allowable income, the next available unit in the building, of comparable size (whether affordable or market rate), must be rented to a low-income tenant to maintain the 80/20 ratio. The Program also permits developers to offer 15 percent of their designated low-income units to households with incomes below 40 percent of AMI. These units are referred to as "deep rent skewed." Under this Program option, if the income of a tenant in a low-income unit (including deep rent skewed units) exceeds 170 percent of the income limit, the next available low-income unit must be rented to a deep skewed tenant. However, under the deep skewed option, the next available market rate unit does not have to be offered to a low-income tenant. Tenants who exceed the 170 percent income limit continue to pay the low-income rents and additional units are not made available for other low-income parties. Virtually all Program developers in New York City have utilized the deep rent skewed option.

Audit Findings and Recommendations

Based on the rents charged for our four sampled developments, we concluded that the proper numbers of affordable apartments were set aside for low-income tenants. We reviewed a sample of 43 low-income tenants and found that, in most cases, the developments used "reasonable judgment" in determining eligibility based on the information in the files. However, for 4 of the 43 tenants, we question whether the developers exercised reasonable judgment. We also found that for 18 of the 43 tenants, the developments did not verify the authenticity of tenant tax returns with the Internal Revenue Service (IRS). As a result, there is a risk that some tenants may not have been eligible for their low-income units.

In addition, the financial benefits received by the owners of the four sampled developments could not be fully calculated. The benefits that could be quantified (specifically tax abatements and tax credits) totaled about $427.3 million for these developments. Developers also derived financial benefits from HFA loans at lower-than-market interest rates. Lastly, over time, the income of about one-third of Program tenants exceeded the income eligibility limits, in effect during the audit period, for an applicant to move into a unit. As of December 31, 2015, more than 160 households occupying low-income units reported household incomes exceeding $100,000.

Compliance With Program Requirements

To assess developer compliance with Program requirements, we selected a sample of four HFA-supervised 80/20 developments participating in the Program during our review period. Three of the selected developments are located in Manhattan, and one is located in Brooklyn. These four developments were required to designate 363 low-income (affordable) housing units per their respective agreements with HFA.

Designated Low-Income Units

To determine whether the selected developments designated the proper number of units to low-income tenants, including deep skewed, we reviewed the regulatory agreements and rent rolls for each of the developments.

Based on the rents charged in these four developments, we concluded that the agreed-upon number of affordable apartments were designated by the sampled developers.

Tenant Eligibility

To determine tenant eligibility, development officials are required to follow specified HUD and IRS income guidelines. HUD guidance requires housing development staff to estimate an applicant's current income using "reasonable judgment." The guidelines illustrate several income scenarios and how the developers should address each scenario.

We selected a judgmental sample of 43 tenants (see Table 1), who resided in the sampled developments during the audit scope period, to determine whether each was eligible for tenancy based on their respective projected incomes and household size at time of move-in.

Table 1
Tenants Sampled by Development

Address of Sampled Development	Borough Location	Number of Tenants Reviewed
80 DeKalb Avenue	Brooklyn	10
316 11th Avenue	Manhattan	11
330 West 39th Street	Manhattan	12
505 West 37th Street	Manhattan	10
Total		**43**

We found that in most cases the developments used "reasonable judgment" in determining eligibility, based on the information contained in tenant files. However, for 4 of the 43 tenants, we found errors or question whether "reasonable judgment" was used in determining their eligibility for this affordable housing. For example:

- A tenant moved into a deep skewed two-bedroom Manhattan apartment (at 316 11th Avenue) in May 2012. His 2011 income tax return listed his filing status as single, no dependents, and reported his total income as $25,851. When he moved into the apartment, the development estimated the applicant's income to be about $29,700, which included $4,943 in interest income on his liquid assets. Since the income limit for a one-person household at the time this tenant moved in was $23,240, he did not meet the eligibility requirements for a one-person household.

  Upon further review of his file, we determined that this tenant claimed his household actually consisted of himself and two children (his niece and nephew). Since the limit for a three-person household at the time this tenant moved in was $29,880, the development concluded that he met eligibility requirements.

  While the tenant's move-in certification form listed the names and birth dates of the two children, both of their Social Security numbers were omitted. HUD requires the verification of Social Security numbers of all household members before an applicant can move into a low-income apartment. Considering the omitted Social Security numbers and the tenant's 2011 income tax filing status, we question whether building management had sufficient documentation to determine that this was a three-person household and, therefore, eligible for a low-income unit. In fact, when this tenant filed his 2012 income tax return, he reported a total income of $238,000, listed no dependents, and listed a wife (whom he had married in 2009).

  (Note: HFA officials advised us that this tenant agreed to move to a smaller affordable apartment when one becomes available. However, when this individual moved in, he exceeded the income eligibility limit for a one-person household.)

- A tenant moved into a deep skewed studio apartment (at 80 DeKalb Avenue) in February 2013, when the income limit for a one-person household was $24,080. The development erroneously calculated the tenant's income to be $22,322, using the applicant's net income rather than gross income of $27,846 (which exceeded the income limit).

  When we discussed this tenant with HFA officials, they told us that they intend to serve the development with a notice of non-compliance. As such, the development must dedicate its next vacant unit as low-income.

- A tenant moved into a one-bedroom deep skewed apartment in Manhattan in October 2014 when the income limit for a one-person household was $23,520. His 2013 income tax return reported collective wages of $24,644, which is greater than the income limit. Shortly before he moved in, the applicant resigned from one of his part-time jobs, and obtained a statement from his other employer that, going forward, he would work only six hours a week at $67 per hour as an adjunct college lecturer. There was no indication that the applicant was questioned about his resignation just prior to the date he moved in. Moreover, the development's annual income report for the very next year (2015) listed this tenant's annual income as $33,000, significantly exceeding the development's estimate based on the prior information submitted.

- In April 2010, a self-employed tutor moved into a one-bedroom apartment (at 505 West 37th Street) when the income limit for a one-person household was $26,900. The development determined her estimated income to be $25,970, based on the tutor's statement that her self-employment income would decline. However, the applicant's comparable income for calendar years 2008 and 2009 was $32,233 and $27,095, respectively. Further, for 2010, the tenant reported income totaling $32,855, consisting of both her self-employment income and wages from a new job.

Based on the aforementioned cases, we concluded that HFA should provide additional procedural guidance to developments to help ensure that appropriate steps are taken to assess Program applicants' eligibility.

The Program also requires all applicants and adult family members to sign consent forms authorizing developments to collect information to verify applicant incomes. However, not all developments took adequate steps to verify income. For 18 (42 percent) of the 43 tenants reviewed, applicant incomes were not verified with the IRS. Therefore, these applicants' Program eligibilities were determined without the benefit of this verification, and consequently, the tenants' eligibility is questionable. Development representatives told us they use discretion in choosing how to verify applicant information. Nonetheless, when we discussed our concerns with HFA officials, they indicated that they plan to make IRS verification of applicants' income a standard Program requirement.

Costs and Benefits of the Program

In addition to creating low-income units, by initiating major construction projects, 80/20 developers create jobs – in turn contributing to the local economy. In turn, as a result of Program participation, developers receive significant financial incentives/benefits in the form of federal income tax credits and local government real estate property tax abatements, in addition to the low-interest loans they receive from HFA.

In New York City, certain areas are designated as "exclusion zones" for certain types of New York City tax exemptions. Developers building in these areas are only eligible for these tax exemptions if they construct affordable units either on-site or off-site. When building such units on-site, the affordability requirement is often met by using the 80/20 Program. Most of the current 80/20 occupied developments in New York City are within certain zones (in Manhattan, Brooklyn and Queens) and receive benefits from both the 80/20 Program and New York City. Developers building in the zones are only eligible for a tax exemption if they construct affordable units either on-site (usually in an 80/20 development, with 20% low-income units) or off-site (by purchasing "certificates" that are used to create affordable housing elsewhere in New York City).

Based on the available information, we were able to only partially estimate the financial benefits received by the owners of our four sampled developments (see Table 2). The HFA interest rates for the four sampled developments during 2014 and 2015 ranged from 0.01 to 1.62 percent, which were likely lower than market rates during that period. However, we could not precisely quantify the developments' savings as a result of these low-interest loans as HFA did not provide information on alternative market rate financing for these developments.

Using available information, Table 2 summarizes the estimated tax credit and abatement benefits (amounting to almost $427.3 million) that we calculated for the four developments. The federal tax credits received by the owners are based on the construction costs associated with the development. The real estate tax abatement, created per the aforementioned Section 421-A of New York's Real Property Tax Law, is based on the assessed value of the buildings. However, without data related to the cost of market rate financing, we could not estimate the total financial benefits received by the developers.

Table 2

Estimated Program Tax Benefits to Developments
($ Amounts in Millions)

Address of Development	Number of Low-Income Units	Number of Units in Development	Estimated 421-A Property Tax Abatement	Projected Federal Tax Credit	Estimated Combined Tax Benefit
80 DeKalb Avenue (Brooklyn)	73	365	$56.3	$11.3	$67.6
316 11th Avenue (Manhattan)	80	369	87.3	15.2	102.5
330 West 39th Street (Manhattan)	42	199	55.1	7.6	62.7
505 West 37th Street (Manhattan)	168	835	169.7	24.8	194.5
Totals	**363**	**1,768**	**$368.4**	**$58.9**	**$427.3**

Further, the number of affordable units occupied by households under the income limit usually declines over time as tenants' incomes rise when developers opt to use the deep rent skewed option. Under the non-deep skewed option, however, the 80/20 ratio is maintained so that if a low-income tenant exceeds 140 percent of the allowable income, the next available unit of comparable size in the building must be rented to a low-income tenant. Once tenants move into an affordable apartment, they may continue to reside in their unit regardless of their income and continue to pay the affordable rent amount. According to the annual income reports of the 68 developments occupied during our audit period, the income of about one-third of the originally eligible tenants rose above the income eligibility limits, in effect during the audit period, for an applicant to move into a unit.

As of December 31, 2015, more than 160 households occupying low-income units reported household incomes exceeding $100,000, with some of those households reporting incomes of more than $250,000. Each of the households with incomes of more than $250,000 paid rents of less than $1,000 per month, with the lowest monthly rent being about $780. Although this is allowed under the Program, given the limited availability of low-income units under the deep skewed alternative, it is not clear that New York State's low-income households optimally benefit from the Program because many affordable units are occupied by tenants with relatively high annual incomes.

Recommendations

1. Require Program developments to verify the incomes of all prospective tenants, prior to moving into an apartment, with the IRS.

2. Work with the management staff at participating Program developments to develop sound and consistent methodologies to project income when determining eligibility.

3. Ensure that adequate information is collected to enable decision makers to adequately assess the costs and benefits of the Program.

Audit Scope and Methodology

The objective of our audit was to determine whether developments in the Program complied with Program requirements regarding the number of designated affordable units and tenant eligibility. We also analyzed the costs and resources used to achieve program results at four participating developments. Our audit included the developments in the Program, that were occupied and had allocated 20 percent of their apartments to low-income tenants, between January 1, 2012 and December 31, 2015.

To accomplish our objective and assess related internal controls, we interviewed HFA and development officials, and reviewed relevant Program policies and reports, records and audits related to Program activities, as well as relevant sections of the Internal Revenue Code, New York Real Property Tax Law, and HUD guidelines. We also visited four participating developments to assess compliance with Program requirements by reviewing their rent roles and tenant application files. To assess tenant eligibility, we reviewed a judgmental sample of tenant files to determine whether their income and household size were adequately supported. To determine the taxpayer Program costs, we reviewed New York City Department of Finance property tax bills and IRS Low-Income Housing Credit forms for selected Program developments. We also reviewed development interest payments to HFA.

We selected a judgmental sample of 4 developments from a population of 93 developments that participated in the Program during the period January 1, 2012 through December 31, 2015. As of December 31, 2015, 68 developments (mostly in Manhattan) were occupied and had allocated 20 percent of their apartments to low-income tenants. Our sample was selected to include developments having filled 20 percent of their affordable units, tenants with higher current incomes, buildings with a high number of low-income units, and at least one development outside Manhattan. The 43 tenants were selected both randomly and judgmentally. Thirty were randomly selected, and the other 13 were selected because they presented a higher level of risk.

We conducted our performance audit in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained during the audit provides a reasonable basis for our findings and conclusions based on our audit objective.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions, and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these management functions do not affect our ability to conduct independent audits of program performance.

Authority

The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution, Article ll, Section 8 of the State Finance Law, and Article X, Section 5 of the State Constitution.

Reporting Requirements

We provided a draft copy of this report to HCR officials for their review and formal comment. We considered HCR officials' comments in preparing this final report and attached those comments in their entirety to it. In their response, HCR officials generally concurred with certain observations and related recommendations in the report, and they disagreed with others. In particular, officials indicated that they have taken steps to strengthen the verification of prospective tenants' incomes. Officials also responded, however, that they do not believe it is necessary to perform further evaluation of the 80/20 Program at this time. Our rejoinders to certain HCR comments are included in the report's State Comptroller's Comments.

Within 90 days after final release of this report, we request the Commissioner/Chief Executive Officer of Homes and Community Renewal report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where the recommendations were not implemented, the reasons why.

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Vision

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To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.

Agency Comments

NEW YORK STATE OF OPPORTUNITY.

Homes and Community Renewal

ANDREW M. CUOMO
Governor

RUTHANNE VISNAUSKAS
Commissioner/CEO

March 9, 2017

Mr. Kenrick Sifontes
Audit Director
Office of the State Comptroller
Division of State Government Accountability
59 Maiden Lane – 21st Floor
New York, New York 10038

Dear Mr. Sifontes:

Attached is Agency management's response to the final draft of the 80/20 Housing Program audit report (2015-S-83). Our response was presented to and approved by the Board Members at their March 9th meeting.

On behalf of our management team at HFA, we thank the staff at OSC for the professional manner in which they have conducted their examination of the Program.

If you have any questions, please feel free to call Daniel E. Murphy, Senior Vice President, at (212) 872-0482 or Stephen B. Chopey, Vice President, at (212) 872-0320, in our offices at 641 Lexington Avenue, New York, New York 10022.

Sincerely,

RuthAnne Visnauskas
Commissioner/CEO

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HCR Management's Response to 80/20 Housing Program Report

I. Key Findings

- ***Based on the rents charged and the regulatory agreements for our four sampled developments, we concluded proper numbers of affordable apartment units were made available to low-income tenants.***

  HFA Response:

  We agree with the first key finding above. The proper number of residential units were made available to low-income tenants.

- ***We reviewed a sample of 43 low-income tenants and found that in most cases, the developments used "reasonable judgment" in determining eligibility based on the information in the files. However, for four of the 43 tenants sampled, we question whether the developers exercised reasonable judgment in evaluating tenant file information.***

  HFA Response:

  Of the four files identified, we strongly disagree with the OSC auditors' finding that 3 of them indicated that the developments failed to exercise "reasonable judgement" in determining program eligibility. Our independent review of the three files in question revealed they were properly vetted and reasonable judgement was applied to determine program eligibility, based on the acceptable certification guidelines as per the IRS code, section 42 low income housing tax credit program. * Comment 1

  For the fourth file, our independent review determined that while the development procured all the necessary program-required third party verification documents, it used an the incorrect computation was applied to determine income eligibility. Specifically, the net income from the paystubs was utilized instead of the gross earnings (as required by IRS program guidelines). This particular error resulted in the Agency issuance of an official notice of non-compliance to the IRS, which has since been cured by the development.

- ***While the program requires all applicants and adult household members to sign consent forms authorizing developments to collect information to verify applicant incomes, not all developments took this step. For 18 (42 percent) of the 43tenants reviewed, applicant incomes were not verified with the internal Revenue Service.***

*See State Comptroller's Comments, page 24.

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HFA Response

OSC's recitation of the steps that developments must take to verify income is incorrect. As we explained repeatedly during the audit process, verifying incomes with the IRS is not a requirement of the federal housing tax code or the City of New York 421 (a) tax abatement programs. Instead, income tax returns are considered a secondary source of income verification by the IRS. Developments are allowed to use acceptable means of income verification that accurately project the tenant's income (i.e., most recent 6 paystubs & third party letter from the tenant's employer). The preferred income verification mode per IRS guidelines is the third-party employment verification letter from the employer.

*
Comment
2

- ***The incomes of about one-third of the original tenants in the 68 developments exceeded the income eligibility limits, in effect during the audit period, for an applicant to move into a unit. In fact, as of December 31, 2015, more than 160 households occupying low income units reported incomes of greater than $100,000.***

HFA Response

HFA strongly disagrees with this finding, as it reflects a misunderstanding of the tax credit program's parameters. The tax credit program, unlike section 8 and other rent subsidy programs, allows for tenant incomes to grow beyond the original income limits requirements so long as the tenant was certified to be income eligible at the time of the initial income verification. In the 80/20 program, an in place tenant's income can continue to exceed the income limit during the recertification process without hardship to the tenant. However, the development must follow the next available unit rule when a tenant's income exceeds 170% of the income limit in place at the time of the annual recertification. This rule requires the development to rent the next available affordable (low income at 40% AMI) unit to an income qualified tenant in order to bring the project back into compliance.

*
Comment
3

- ***The total benefits to developers to create the 363 affordable units in our four sampled developments could not be fully calculated. Benefits that could be quantified (local tax abatements per Section 421-A and federal tax credits) amounted to almost $427.3 million for the four sampled developments. This did not include the benefits of HFA low-interest loans.***

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HFA Response

Cost benefits of the Tax Credit, 80/20 program is addressed in item 3 of the Recommendations section of HFA's response.

II. Audit Findings

OSC's review of File No. 1. - 316 11th Ave.

Tenant Eligibility

- *We selected a judgmental sample of 43 tenants (See Table 1), who resided in the sampled developments during the audit scope period, to determine whether each was eligible for tenancy based on their respective projected incomes and household size at time of move-in.*
- *We found most developments used "reasonable judgment" in determining eligibility based on the information in the files. However, for four of the 43 tenants sampled, we found errors or question whether the developers exercised reasonable judgment in evaluating tenant file information. For example:*

A tenant moved into a deep skewed two bedroom Manhattan apartment (at 316 11th Avenue) in May 2012. His 2011 income tax return a return listed his filing status as single, no dependents, and reported hos total income as $25,851.

When he moved into apartment, the development estimated applicant's income to be about $29,700, which included $4,943 in interest income on his liquid assets. Since the income limit for a one-person household at the time this tenant moved in was $23,240, he did not meet the eligibility requirement for a one person household.

Upon further review of his file, we determined that this tenant claimed his household actually consisted of himself and two children (his niece and nephew). Since the limit for a three-person household at the time this tenant moved in was $29,880, the development concluded he met eligibility requirements.

While the tenant's move-in certification form listed the names and birth dates of the two children, both of their Social Security numbers were omitted. HUD requires the verification of Social Security numbers of all household members before an applicant can move into a low-income apartment. Considering the omitted Social Security numbers and the tenant's 2011 income tax filing status, we question whether building management had sufficient documentation to determine that this was a three-person household and, therefore, eligible for a

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low-income unit. In fact, when this tenant filed his 2012 income tax return, he reported a total income of $238,000, listed no dependents, and listed a wife (whom he had married in 2009).

(Note: HFA officials advised us that this tenant agreed to move to a smaller affordable apartment when one becomes available. However, when this individual moved in, he exceeded the income eligibility limit for a one-person household).

<u>HFA Response to 316 11th Ave.</u>

HFA does not share OSC's view that the developer used unreasonable judgment in this instance. The periodic LIHTC review was conducted at The OHM (316 11th Avenue) on October 9th and 10th. .The following finding was communicated to Ownership and Management in the 12/15/2014 concerns letter:

* Comment 4

[redacted] the 2012 income tax return lists a Spouse with filing Status "Married Filing Joint Return". The Spouse is not listed as an occupant in the household or on the initial certification. Note: 2011tax return lists resident as "Single". There were no verifications on file for the checking account, savings account, and stocks and bonds listed on the 2012 initial certification. The tenant was self-employed with income of $24,745 at move in. And the 2014 annual recertification the tenant is now employed with verified income of $206,201. The household assets increased from $247,151 to $456,502 in 2014. The tenant indicated his niece and nephew were occupying the unit at initial and through the 2013 annual recertification, however, he was not claiming them as dependents on his tax returns nor did the file contain guardianship documentation. The 2013 Income Tax Return lists a Spouse who is not documented as residing in the unit and the niece and nephew are not listed as household members. There is no housing application on file to determine how household was selected from your applicant waiting list. Management needs to follow up with the household to determine eligibility for the 2 bedroom LIHTC unit.

* Comment 5

On January 15, 2015 HFA received a response from the development indicating they had begun a holdover action against [redacted] because he has been non-responsive to their request to provide information in response to our findings. On March 9, 2015, the Agency received from Management a sworn statement regarding [redacted] stating his niece moved out of the household on August 30, 2012, and his nephew never resided with him in the household. He further stated he notified management of the change in household composition during his 2013 recertification. The sworn statement further acknowledges he was married and his wife resided in South Africa. He stated he separated from his wife in January 2012 and they did not reside in the household together. The couple divorced in February 2014 (copy of the request for the divorce decree was provided). Management also submitted a request from [redacted] to be

* Comment 5

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transferred to a one bedroom apartment when one was available. HFA also received copies of the application, credit report, statements regarding the stocks and bonds. After the documents were reviewed, HFA determined the findings were adequately addressed and closed out the file findings.

OSC's review of File No. 2. – 80 DeKalb Avenue.

- ***A tenant moved into a deep skewed studio apartment (at 80 DeKalb Avenue) in February 2013, when the income limit for a one-person household was $24,080. The development erroneously calculated the tenant's income to be $22,322, using the applicant's net income rather than gross income of $27,846 (which exceeded the income limit).***

  When we discussed this tenant with HFA officials, they told us that they intend to serve the development with a notice of non-compliance. As such, the development must dedicate its next vacant unit as low-income.

HFA Response to 80 DeKalb

This is the only unit of the four units cited by OSC that HFA is in agreement with the OSC findings. HFA's independent review of this file confirmed that if the development would have used the gross earning on the paystubs during the initial certification the applicant would have been deem ineligible. This oversight by the development resulted in HFA filing a noncompliance notice to the IRS (form 8823), which has been recently cured by the development. The ineligible tenant that resulted by management's error moved out and management was able to restore the proper number of tax credit units by replacing the over income tenant with an income qualified household. This action enabled the Agency to file a notice of cure of the noncompliance with the IRS.

OSC's review of File No. 3. – 330 West 39th Street.

- ***A tenant at 330 West 39th Street moved into a one-bedroom in October 2014 when the income limit for a one-person household was $23,520. His 2013 income tax return reported collective wages of $24,644, which is greater than the income limit. Shortly before he moved in, the applicant resigned from one of his part time jobs, and obtained a statement from his other employer that, going forward, he would only work six hours a week at $67 per hour as an adjunct college lecturer. There was no indication that the applicant was questioned about his resignation just prior to the date he moved in. Moreover, the tenant's annual income listed his annual income as $33,000, significantly exceeding the development's estimate based on the prior information submitted.***

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HFA Response to 330 W. 39th Street

HFA does not share OSC's view that the developer used unreasonable judgment in this instance. In response to this finding, HFA requested and reviewed the complete tenant file for this one person household. The Agency's review of the tenant's file indicated that this tenant was income eligible at the time of initial certification. At the time of the initial certification (2014) the tenant was employed. The owner/agent projected his annual income based on the employment verification letter obtained from the applicant's employer and the questionnaire form completed by the tenant. The tenant's income was calculated using a conservative approach, based on the facts before them at the time of the application process and not investigative judgement at the time of the review. The development correctly determined the applicant's income to be **$23,535.04.** It is a conservative approach since the tax return had indicated that the self-employment had resulted in a net loss, which pursuant to section H subsection 3 of chapter 5 of the HUD Handbook 4350.3 revision 1, a net loss is counted as zero. The project also annualized his income based on twelve months even though he does not work a full year as indicated on the employment verification form provided by his employer.

* Comment 6

OSC's review of File No. 4. – 505 West 37th Street.

- ***In April 2010, a self-employed tutor moved into a one-bedroom apartment (at 505 West 37th Street) when the income limit for a one-household person was $26,900. The development determined her estimated income to be 25,970, based on the tutor's statement that her self-employment income would decline. However, the applicant's income tax returns for years 2008 and 2009 reported income of $32,233 and $27,095, respectively. Further, for 2010, the tenant reported income totaling 32,855, consisting of both her self-employment income and wages from a new job.***

HFA Response to 505 W. 37th Street

HFA does not share OSC's view that the developer used unreasonable judgment in this instance. This unit was included as part of the 2014 Periodic Review of 505 West 37th Street. HFA found the household to be income qualified at the 2010 40% of Area Median Income ($21,520). The household's income and assets were calculated as follows:

* Comment 7

The file contained a self-employment affidavit indicating the net business income over the next twelve months would be $17,600 $22,000-gross less anticipated business expense of $4400 equals $17,600). Attached to the self-employment affidavit was a certified letter from the tenant's CPA explaining the tenant's anticipated income for the next twelve months as $17,600. The tenant's previous tax return (2009) indicates the net income from business as $22,400. The 2010 income tax returns were in the 2011 annual recertification file and the tenant had a $69,291 net loss for business income. In accordance with HUD Handbook 4350.3, REV-1, pages 5-13, Section H. #3.: If the net income from a business is negative, it must be counted as zero income. Therefore, the 2010 income tax return is further documentation the household's annual income was within the 40% of Area Median Income at the household's 2010 move-in. The Household's initial certification was calculated by HFA staff as follows:

Income from Self –Employment:	$17,600.00	
Income from Assets	$ 3,823.57	(used Actual Interest income because it's higher than the inputted amount)
Total HH Income	**$21,423.57**	
	Applicable 2010 40% Income Limit $21,520	

The Agency concludes the household was qualified for a 40% of Area Median Income unit at move-in and was not deemed over-income.

III. OSC Recommendations

OSC Recommendation No. 1: Require Program developments to verify the incomes of all prospective tenants, prior to moving into an apartment, with the IRS.

HFA Response:

Consistent with existing practice, we will continue to advise owners/agents to improve confirmation of tenant affidavits and affirmations with adequate support prior to all future move-ins, based on HUD and section 42 of the IRS code guidelines.

OSC Recommendation No. 2: Work with the management staff at participating Program developments to develop sound and consistent methodologies to project income when determining eligibility.

HFA Response: Some developments have already incorporated the step of authenticating tax returns (via the 4506 T IRS form), as an extra step in their certification process. However, verification of tax returns is not a tax credit program requirement. However, since the Agency has already included a question in its field visit checklist regarding the voluntary use of the 4506 T IRS form, the Agency will endeavor to make this a recommended best practice for all of our tax credit projects, including the subject

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projects under the 80/20 program. We will post this best practice recommendation on our website and announce it via an email blast to our clients.

OSC Recommendation No. 3:* *Ensure that adequate information is collected to enable decision makers to adequately assess the costs and benefits of the Program.

HFA Response: HFA collects and reviews market data on a consistent basis from numerous industry sources. Agency policy makers have given significant consideration to the 80/20 program and do not believe additional evaluation is necessary at this time. HFA is comfortable with our current policy decision that the development of these mixed income projects furthers the Agency's core mission of creating and preserving high quality affordable multifamily rental housing. The policy initiative for the 80/20 program is not based solely on calculating the cost of building a unit of housing, but rather HFA takes a holistic approach considering the cost of a unit of housing along with the location and the local need for affordable housing. Development of mixed income housing builds stronger neighborhoods and enables low-income New Yorkers to live in high opportunity areas. Section 421 (a) is an as-of-right tax abatement program that developers utilize to offset the costs of housing development in New York City.

* Comment 8

Over time, some projects may experience a reduction of units occupied by low income residents since Federal regulation does not permit the eviction of over-income tenants. As noted in the Preliminary Audit Findings as of December 31, 2015 only 167 tenants (or less than 4% of 80/20 tenants occupying affordable units) earned over $100,000/year or 220% of AMI. As noted in the Preliminary Audit Findings two-thirds of tenants who were income qualified at move in remained income qualified. Most of those above the income limit remain below income levels subsidized by other effective housing programs such as the Mitchell-Lama program. Creation of 80/20 housing promotes financially mixed and more diverse housing in the same building and market area.

Under the 421-a program as presently structured, projects have 30 year regulatory agreements. As over-income residents move out, qualifying low income tenants move in. Initial rent stabilization filings for the affordable units are based on the affordable rents at the time the units are registered and the rents in these units continue to be set pursuant to the rent regulation laws for the entirety of the 30-year regulatory term.

State Comptroller's Comments

1. As noted on page 8 of the report, for 4 of the 43 tenants, we found errors or questioned whether reasonable judgment was used in determining the tenant's 80/20 Program eligibility. The basis for our observations regarding the four tenants is presented in the detailed narratives on pages 8 and 9 of the report. Based on the facts presented, we maintain that the audit observations and conclusions in question are proper.
2. In fact, HCR's comment is incorrect. The audit report neither implies nor states explicitly that income verification with the IRS is a legal or regulatory requirement of the Program. Rather, we recommend that developments verify incomes with the IRS to help ensure that applicants meet Program eligibility requirements. Also, in its response to the draft report, HCR indicated that it would endeavor to make the IRS verification a recommended best practice for all its tax credit projects.
3. The auditors understood the Program's tax parameters correctly. As noted on page 6 of the report, "once eligible tenants move into an affordable apartment, they can continue to reside in their unit regardless of their income." Moreover, our report does not assert that occupants of Program units become ineligible for the Program if their incomes exceed prescribed limits subsequent to Program acceptance. Rather, our report provides information on annual tenant incomes after they have moved-in to a unit.
4. As stated in the report, at the time the tenant moved in to his unit, he reported that his household consisted of three individuals – himself, his niece and his nephew. However, his 2011 tax return did not reference the niece and nephew. Furthermore, his move-in certification omitted the niece's and nephew's Social Security numbers. HUD requires the verification of Social Security numbers of all household members before move-in. Also, HCR's response acknowledges that the developer had no verifications on file for the tenant's checking account, savings account and stocks and bonds. Consequently, we continue to question whether development personnel exercised reasonable judgment in awarding a unit to this tenant.
5. We redacted the identity of the tenant in question to protect potentially confidential information.
6. It is unclear how the development estimated the applicant's annual income to be $23,535 when his 2013 IRS return (for the year prior to the award of the unit) indicated income of $24,644, as detailed in the report. Also, as detailed in the report, $24,644 exceeded the income limit (of $23,520) in 2014. Further, we are concerned with HCR's statement that "investigative judgment" was not applied to the review of the tenant's application. Consequently, we continue to question whether reasonable judgment was used to award the unit.
7. HCR's response is in error. HCR's comments pertain to an applicant that is not detailed in or otherwise addressed by the audit report.
8. We do not dispute that the 80/20 Program furthers HFA's core mission of creating and preserving high quality affordable rental housing. We would also agree that a "holistic approach" should be used to evaluate the cost benefit of the Program. However, as detailed in the report, developers received tax abatements and credits totaling $427.3 million to create 363 Program units at the four developments we selected for review.

Further, as also detailed in the report, the financial benefits of HFA's low interest loans to developers could not be readily determined. Consequently, neither auditors nor HCR/HFA officials could perform a complete (or holistic) cost benefit analysis of the Program. Given the 80/20 Program's fiscal and programmatic significance, we encourage HCR/HFA officials to reconsider our recommendation, to help assure that a genuinely holistic assessment of the costs and benefits of the Program can be made.