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rental subsidy for this term. The method of supplying the funds must be clearly established.

§ 3560.261 Improperly advanced rental assistance.

Improperly advanced RHS rental assistance resulting from tenant or borrower error or fraud constitutes unauthorized assistance and the provisions of subpart O of this part apply.

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§ 3560.300 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0189. Public reporting burden for this collection of information is estimated to vary from 15 minutes to 18 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. A person is not required to respond to a collection of information unless it displays a currently valid OMB control number.

Subpart G—Financial Management

§ 3560.301 General.

This subpart contains requirements for the financial management of Agency-financed multi-family housing (MFH) projects, including accounts, budgets, reports, and engagements. Financial management systems and procedures must cover all housing operations and provide adequate documentation to ensure that program objectives are met.

§ 3560.302 Accounting, bookkeeping, budgeting, and financial management systems.

(a) *General.* Borrowers must establish the accounting, bookkeeping, budgeting and financial management procedures necessary to conduct housing project operations in a financially safe and sound manner. Borrowers must maintain records in a manner suitable for an engagement and must be able to

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report accurate operational results to the Agency from these accounts and records.

(b) *Acceptable methods of accounting.*

(1) Borrowers may use a cash, accrual, or modified accrual method of accounting, bookkeeping, and budget preparations as long as the method is consistent with the statements required by the engagement in accordance with the standards identified in § 3560.308.

(2) Borrowers must describe their accounting, bookkeeping, budget preparation, and financial reporting procedures, including Agency-approved engagements, in their management plan.

(3) Borrowers must notify the Agency of any changes in their accounting, bookkeeping, budget preparation, and financial management reporting systems through a revision of their management plan.

(c) *Account requirements.* (1) As used in this paragraph, the term account is used interchangeably to mean a bookkeeping account (ledger) or a bank account.

(2) At a minimum, borrowers must maintain the accounts required by their loan agreement or resolution.

(3) The following list identifies the financial accounts that are required for each housing project. Additional accounts may be required by third-party lenders. Accounts are to be funded in the following priority order, except that paragraphs (c)(3)(iv), (v), and (vi) of this section are funded directly by tenant security deposits or patron capital receipts respectively:

- (i) General operating account;
- (ii) Real estate tax and insurance account (if not part of the general operating account);
- (iii) Reserve account;
- (iv) Tenant security deposit account;
- (v) Membership fee account for cooperative housing; and
- (vi) For cooperative housing only, a patron capital account.

(4) Amounts escrowed for taxes and insurance may be kept in the general operating account as long as the accounting system reflects the amount escrowed.

(5) Regardless of the number or types of accounts established, the borrower must meet the following requirements:

(i) All housing project funds must be held only in financial institution accounts insured by an agency of the Federal Government, backed by collateral provided by the bank, or held in securities meeting the conditions in this subpart.

(ii) Funds maintained in an institution may not exceed the limit established for Federal deposit insurance. If funds exceed the amount covered by Federal deposit insurance, borrowers must obtain a collateral pledge from the institution to cover all funds or must move funds to an institution that will insure the funds.

(iii) All funds and proceeds in any account must be used only for authorized purposes as described in Agency's regulations, loan or grant documents. Use of funds for non-program purposes constitutes non-monetary default as described in §3560.452(c).

(iv) All funds received and held in any account, except the tenant security deposit, membership fee, and patron capital accounts, must be held in trust by the borrower for the loan obligation until used and serve as security for the Agency loan or grant.

(v) Borrowers must be able to account for housing project funds with accounting methods or practices that maintain the proprietary identity of the funds for each project. A borrower may operate one account for multiple projects as long as the funds for each project themselves are accounted for separately.

(vi) Each borrower must have access to at least one demand deposit or checking account.

(vii) Housing project funds may not be pledged as collateral for debts without Agency approval. If such a need arises for an eligible program purpose, the borrower must obtain prior Agency approval.

(6) Tenant security deposit accounts or membership fee accounts and patron capital accounts must be maintained in a separate account in trust for the tenants or members and handled in a manner consistent with state and local laws.

(d) *Documentation of separate accountability.* Housing project funds may be combined in one or more bank accounts for two or more housing

projects as long as the borrower's accounting system segregates and tracks funds for each project separately.

(1) When borrowers request Agency approval of an accounting system that combines funds from two or more housing projects, they must demonstrate to the Agency that the accounting systems are structured to segregate and maintain separate accountability for each housing project. Such demonstration must include a statement issued by a Certified Public Accountant (CPA) stating that the accounting system is structured to meet this principle of separate accountability.

(2) The accounting system and management plan must document the method for prorating revenue and expenses that are not clearly identifiable as being associated with a particular housing project.

(3) Funds for housing projects managed by the same management company must not be co-mingled.

(e) *Records.* (1) Borrowers must retain all housing project financial records, books, and supporting material for at least three years after the issuance of the engagement and financial reports. Upon request, these materials will immediately be made available to the Agency, its representatives, the USDA Office of the Inspector General (OIG), or the General Accountability Office (GAO).

(2) Borrower accounts and records will be kept or made available in a location with reasonable access for inspection, review, and copying by the Agency, other authorized representatives of the USDA, OIG, or GAO.

(3) Automated records may be used if they meet the conditions of paragraph (f) of this section.

(f) *Forms generated by automated systems.* (1) The forms and formats approved for use by borrowers may be prepared on automated systems when they meet the requirements of this paragraph.

(2) Forms may be automated if they meet the following requirements:

(i) The identical wording and nomenclature of an official form must be included in the automated version of the form, including the Office of Management and Budget (OMB) approval number.

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(ii) The logic or mathematical calculation of an official form must be the same in an automated version of the form.

(iii) The name or logo of the source of the automated form must be visible on each output of the automated form.

(iv) Output size must be 8½ × 11 inches.

(v) Nominal spacing adjustment and colored paper are allowed.

(g) *Farm Labor Housing*. Borrowers with on-farm labor housing units will be considered in compliance with this section by virtue of completing the record keeping and reporting requirements outlined in subpart M of this part.

§ 3560.303 Housing project budgets.

(a) *General requirements*. (1) Using an Agency-approved format, borrowers must submit to the Agency for approval a proposed annual housing project budget prior to the start of the housing project's fiscal year. The capital budget section of the annual project budget must include anticipated expenditures on the project's long-term capital needs as specified in § 3560.103(c).

(2) Budget projections regarding income, expenses, vacancies, and contingencies must be realistic given the housing project's history, current circumstances, and market conditions.

(3) Borrowers must document that the operating expenses included in the budget accurately reflect reasonable and necessary costs to operate the housing project in a manner consistent with the objectives of the loan and in accordance with the applicable Agency requirements.

(4) Borrower must submit supporting documentation to justify housing project utility allowances.

(5) Upon Agency request, borrowers must submit any additional documentation necessary to establish that applicable Agency requirements have been met.

(b) *Allowable and unallowable project expenses*. Expenses charged to project operations, whether for management agent services or other expenses, must be reasonable, typical, necessary and show a clear benefit to the residents of the property. Services and expenses

charged to the property must show value added and be for authorized purposes.

(1) *Allowable expenses*. Allowable expenses include those expenses that are directly attributable to housing project operations and are necessary to carry out successful operations.

(i) Housing project expenses must not duplicate expenses included in the management fee as defined in § 3560.102(i).

(ii) Actual costs for direct personnel costs of permanent and part-time staff assigned directly to the project site. This includes managers, maintenance staff, and temporary help including their:

- (A) Gross salary;
- (B) Employer FICA contribution;
- (C) Federal unemployment tax;
- (D) State unemployment tax;
- (E) Workers compensation insurance;
- (F) Health insurance premiums;
- (G) Cost of fidelity or comparable insurance;
- (H) Leasing, performance incentive or annual bonuses;
- (I) Direct costs of travel to off-site locations by on-site staff for property business or training; and/or
- (J) Retirement benefits.

(iii) Legal fees directly related to the operation and management of the property including tenant lease enforcement actions, property tax appeals and suits, and the preparation of all legal documents.

(iv) All outside account and auditing fees, if required by the Agency, directly related to the preparation of the annual audit, partnership tax returns and 401-K's, as well as other outside reports and year-end reports to the Agency, or other governmental agency.

(v) All repair and maintenance costs for the project including:

- (A) Maintenance staffing costs and related expenses.
- (B) Maintenance supplies.
- (C) Contract repairs to the projects (e.g., heating and air conditioning, painting, roofing).

(D) Make ready expenses including painting and repairs, flooring replacement and appliance replacement as well as drapery or mini-blind replacement. (Turnover maintenance).

(E) Preventive maintenance expenses including occupied unit repairs and maintenance as well as common area systems repairs and maintenance.

(F) Snow removal.

(G) Elevator repairs and maintenance contracts.

(H) Section 504 and other Fair Housing compliance modifications and maintenance.

(I) Landscaping maintenance, replacements, and seasonal plantings.

(J) Pest control services.

(K) Other related maintenance expenses.

(vi) All operational costs related to the project including:

(A) The costs of obtaining and receiving credit reports, police reports, and other checks related to tenant selection criteria for prospective residents.

(B) The cost of duplicating forms for those properties not owning a copier. This will include the costs of producing or purchasing forms and mailing or delivering those forms to the project site.

(C) All bank charges related to the property including purchases of supplies (e.g., checks, deposit slips, returned check fees, service fees).

(D) Costs of site-based telephone including initial installation, basic services, directory listings, and long-distances charges.

(E) All advertising costs related specifically to the operations of that project. This can include advertising for applicants or employees in newspapers, newsletters, radio, cable TV, and telephone books.

(F) Postage and delivery costs from the site including expenses to the Agency or other governmental agencies, tenants, verifying third parties, central management offices, etc.

(G) Partnership or corporate business expenses including state taxes and other mandated state or local fees as well as other relevant expenses required for operation of the property by a third-party governmental unit. Costs of continuation financing statements and site license and permit costs.

(H) Expenses related to site utilities including actual costs and surcharges as well as deposits and expense of utility bonds in lieu of bonds.

(I) Site office furniture and equipment including site based computer

and copiers. Service agreements and warranties for copiers, telephone systems and computers are also included (if approved by the Agency).

(J) Real estate taxes (personal tangible property and real property taxes) and expenses related to controlling or reducing taxes.

(K) All costs of insurance including property liability and casualty as well as fidelity or crime and dishonesty coverage for on-site employees and the owners.

(L) Costs of collecting rents on-site including bookkeeping supplies and recordkeeping items.

(M) Costs of preparing and maintaining tenant files and processing tenant certifications including all office supplies, copies and other associated expenses.

(N) Public relations expense relative to maintaining positive relationships between the local community and the tenants with the management staff and the borrowers. Chamber of Commerce dues, contributions to local charity events, and sponsorship of tenant activities, are examples.

(O) Tax Credit Compliance Monitoring Fees imposed by HFAs.

(P) All insurance deductibles as well as adjuster expenses.

(Q) Professional service contracts (audits and compilations, tax returns, energy audits, utility allowances, architectural, construction, rehabilitation and inspection contracts, etc.)

(R) On-site training pre-approved by the Agency provided by outside training vendors.

(S) Site manager salary for additional hours associated with congregate housing.

(vii) With prior Agency approval, cooperatives and nonprofit organizations may use housing project funds to pay asset management expenses directly attributable to ownership responsibilities. Such expenses may include:

(A) Errors and omissions insurance policy for the Board of Directors.

(B) Board of Director review and approval of proposed Agency's annual operating budgets, including proposed repair and replacement outlays and accruals.

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(C) Board of Director review and approval of capital expenditures, financial statements, and consideration of any management comments noted.

(D) Long-term asset management reviews.

(2) *Unallowable expenses.* Housing project funds may not be used for any of the following:

(i) Equity skimming as defined in 42 U.S.C. 543 (a).

(ii) Purposes unrelated to the housing project.

(iii) Reimbursement of inaccurate or false claims.

(iv) Settlement agreements, court ordered decrees, legal fees, or other costs that result from the filing of civil rights complaints or legal action alleging the borrower, or a representative of the borrower, has committed a civil rights violation.

(v) Fines, penalties, and legal fees where the borrower or a borrower's representative has been found guilty of violating laws, including, but not limited to, civil rights, and building codes.

(vi) Association dues to be paid by the project should be related to training for site managers or management agents. To the extent that association dues can document training for site managers or management agents related to project activities by actual cost or pro-ration, a reasonable expense may be billed to the project.

(vii) Pay for bonuses or monetary performance awards to site managers or management agents that are not clearly provided for by the site manager salary contract.

(viii) Billing for parties that are large or unreasonable, such as renting expensive party halls or hotel rooms and payment for alcoholic beverages or gifts to management agent staff.

(ix) Billing for practices that are inefficient such as routine use of collect calls from a site manager to a management agent office.

(c) *Priorities.* The priority order of planned and actual budget expenditures will be:

- (1) Senior position lienholder, if any;
- (2) Operating and maintenance expenses, including taxes and insurance;
- (3) Agency debt payments;
- (4) Reserve account requirements;

(5) Other authorized expenditures; and

(6) Return on owner investment.

(d) *Agency review and approval.* (1) The Agency will only approve housing project budgets that meet the requirements of paragraphs (a), (b) and (c) of this section.

(2) If no rent change is requested, borrowers must submit budget documents for Agency approval 60 calendar days prior to the start of the housing project's fiscal year. The Agency will notify borrowers if the budget submission does not meet the requirements of paragraphs (a), (b), and (c) of this section. The borrower will have 10 days to submit the additional material.

(3) If a rent change is requested, the borrower must submit budget documents to the Agency and notify tenants of the requested rent change at least 90 calendar days prior to the start of the housing project's fiscal year.

(i) The Agency will notify borrowers if the budget submission does not meet the requirements of paragraphs (a), (b), and (c) of this section, or if the rent and utility allowance request has been denied in accordance with §3560.205(f). The borrower will have 10 days to submit the additional material to address any issues raised by the Agency.

(ii) The rent change is not approved until the Agency issues a written approval. If there is no response from the Agency within the 30-day period, the rent change is considered automatic. The following budgets are not eligible for automatic approval:

(A) Budgets with rent increases above \$25 per unit; and

(B) Budgets that are submitted late or that miss other deadlines set by the Agency.

(4) If the Agency denies the budget approval, the Agency will notify the borrower in writing.

(5) If budget approval is denied, the borrower shall continue to operate the housing project on the basis of the most recently approved budget.

§ 3560.304 Initial operating capital.

(a) *Purpose.* To provide a source of capital for start-up costs, such as the purchase of equipment, and paying operating, maintenance, and debt service expenses. Borrowers are required to

make an initial operating capital contribution to the general operating account as described in § 3560.64.

(b) *Authorized uses of initial operating capital.* Initial operating capital may be used only to pay for approved budgeted expenses.

(c) *Withdrawal of initial operating capital.* Initial operating capital funds may be withdrawn by a borrower if:

(1) The initial operating capital was provided from the borrower's own funds;

(2) The borrower requests the withdrawal after the second year of housing project operations and prior to the 7th year of operations;

(3) The housing project has had a 90 percent occupancy rate for a period of 12 months prior to the withdrawal request;

(4) The withdrawal will not affect the financial viability of the housing project;

(5) Contributions to the reserve account are at authorized levels;

(6) The withdrawal request will not result in rent increases; and

(7) There are no outstanding deficiencies in management's physical maintenance of the housing project.

§ 3560.305 Return on investment.

(a) *Borrower's return on investment.* Borrowers may receive a return on their investment (ROI) in accordance with the terms of their loan agreement and the following:

(1) If there is a positive net cash flow in housing project operations, the ROI may be taken by the borrower after the housing project's fiscal year, provided that the balance of the reserve account is equal to or greater than required deposits minus authorized withdrawals. If the annual financial reports indicate that an ROI should not have been taken, borrowers will be required to return any unauthorized ROI.

(2) If there is negative cash flow in housing project operations, the Agency may authorize the borrower to take the ROI only after the Agency has reviewed the housing project's annual financial reports and determines:

(i) Surplus cash exists in either the general operating account as defined in § 3560.306(d)(1) or the reserve account, if the balance is greater than the re-

quired deposits minus authorized withdrawals.

(ii) The housing project has sufficient funds to address identified capital or operational needs.

(b) *Unpaid return on investment.* An earned, but unpaid ROI for the previous year only may be requested by the borrower and authorized by the Agency under the provisions of § 3560.305(a)(2) provided the current year's ROI has been paid first and a rent increase is not required to generate funds to pay the unpaid ROI.

§ 3560.306 Reserve account.

(a) *Purpose.* To meet the major capital expense needs of a housing project, borrowers must establish and maintain a reserve account.

(b) *Financial management of the reserve account.* Borrower management of the reserve account is subject to the requirements of 7 CFR part 1902, subpart A regarding supervised bank accounts.

(c) *Funding of the reserve account.* Borrowers must make payments to the reserve account in the amount established in loan documents, beginning with the first loan payment or a date specified in loan documents.

(d) *Transfer of surplus general operating account funds.* (1) The general operating account will be deemed to contain surplus funds when the balance at the end of the housing project's fiscal year, after all payables, exceeds 20 percent of the operating and maintenance expenses. If the borrower is escrowing taxes and insurance premiums, include the amount that should be escrowed by year end and subtract such tax and insurance premiums from operating and maintenance expenses used to calculate 20 percent of the operating and maintenance expenses.

(2) If a housing project's general operating account has surplus funds at the end of the housing project's fiscal year, the Agency will require the borrower to use the surplus funds to address capital needs, make a deposit in the housing project's reserve account, reduce the debt service on the borrower's loan, or reduce rents in the following year. At the end of the borrower's fiscal year, if the borrower is required to transfer surplus funds from the general operating account to the

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reserve account, the transfer does not change the future required contributions to the reserve account.

(e) *Account requirements.* Borrowers must establish and maintain the reserve account according to § 3560.65, § 3560.302(c)(5), and the following requirements:

(1) Reserve accounts must be deposited in interest-bearing accounts or securities; and

(2) Reserve accounts must be supervised accounts that require the Agency to countersign on all withdrawals; except, this requirement is not applicable when loan funds guaranteed by the Section 538 GRRH program are used for the construction and/or rehabilitation of a direct MFH loan project. Direct MFH loan borrowers, who are exempted from the supervised account and countersigned requirement, as described above, must follow Section 538 GRRH program regulatory requirements pertaining to reserve accounts. In all cases, Section 538 lenders must get prior written approval from the Agency before reserve account funds involving a direct MFH loan project can be disbursed to the borrower.

(f) *Funds invested in securities.* In addition to the requirements specified in paragraph (e) of this section, the following requirements apply when reserve funds are invested in securities:

(1) The reserve account must be held either at a Federally insured domestic institution such as a bank, savings and loan association, credit union, or at a domestic institution authorized to sell securities.

(2) The borrower must record the price actually paid for the securities. When designated as a reserve deposit, the price paid must equal the required contribution to reserves.

(3) Borrowers must be knowledgeable about industry practices and consider the impact of typical fees and charges for purchases and sales and maintenance of an account when making investment decisions. Such fees may be paid for out of reserves, only with the consent of the Agency. Housing project funds may not be used to pay for a financial advisor.

(g) *Use of the reserve account.* (1) Borrowers must request Agency approval of reserve account withdrawals prior to

the withdrawal. Borrowers must inform the Agency of planned uses of reserve accounts in their annual capital budget if known at budget planning time. Any item on the approved capital budget does not require additional pre-approval by the Agency.

(2) The Agency will indicate any conditions governing withdrawals from a reserve account at the time it approves the withdrawal.

(3) In emergency situations, the Agency may specify special procedures to provide an expedited approval process for the use of the reserve account.

(4) The Agency may approve the use of reserve funds for operating costs when circumstances that are determined by the Agency to be beyond the borrower's control have resulted in a shortfall in the housing project's general operating account.

(5) Funds from the replacement reserve account cannot be used to pay any fees associated with the Section 538 GRRH loan guarantee, as determined by the Agency.

(h) *Allowable uses.* Allowable uses of reserve funds include the following:

(1) Major capital improvements and replacements.

(2) Housing project operating expenses provided the requirement of paragraph (g)(4) of this section has been met, including:

(i) Payments due on the loan, or

(ii) Payment of a return on investment at the end of the borrower's fiscal year if such payment comes from surplus operating funds in the reserve account.

(3) With Agency approval, borrowers operating on a for-profit or a limited profit basis may make an annual withdrawal from the reserve account, equal to no more than 25 percent of the interest earned on a reserve account during the prior year.

(4) For other purposes, which in the judgment of the Agency will promote the loan purposes, strengthen the security or facilitate, improve, or maintain the housing and the orderly collection of the loan without jeopardizing the loan or impairing the adequacy of the security.

(i) *Records.* Borrowers must maintain records documenting all expenses that

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were paid by withdrawals from the reserve account.

(j) *Changes to reserve requirements.* (1) As projects age, the required reserve account level may be adjusted to meet anticipated “life-cycle” needs, including equipment and facility replacement costs, by amending the loan agreement/resolution.

(2) The Agency may approve a change in the reserve account funding level based on the findings of an approved capital needs assessment. The approval to increase reserve account funding levels will take into consideration the housing project’s approved budget and the housing project’s ability to support increased reserve account deposits without causing basic rents to exceed conventional rents for comparable units in the area.

(k) *Excess reserves.* Amounts in the reserve account which exceed the total required by the loan or grant agreement must be used, at the direction of the Agency, for any of the following:

(1) Pay for expenses specified in a long-term capital plan;

(2) Make payments and reamortize the Agency loan;

(3) Reduce rents by a transfer to the general operating account;

(4) Fund preservation incentives authorized in subpart N of this part; or

(5) Cover other expenditures determined to be related to the purpose of the housing project and in the best interest of the Federal Government.

(1) *Procurement.* The requirements of § 3560.102(g), (j), and (k), and all other Agency requirements relating to procurement, bidding, identity-of-interest, cost-reasonableness, and construction management apply to any work or services paid out of reserve funds. Structural repairs and other significant work on major building systems such as heating or air conditioning must be done in accordance with the requirements of 7 CFR part 1924, subpart A.

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§ 3560.307 Reports.

(a) *Required reports.* Borrowers must submit required reports using Agency-approved formats.

(b) *Quarterly and monthly reports.* The Agency may require quarterly or monthly reports to monitor financial progress when closer supervision is warranted.

§ 3560.308 Annual financial reports.

(a) *General.* Borrowers must submit annual financial reports that meet the requirements of this section. The annual financial reports to be submitted are the Multi-Family Housing (MFH) Project Budget with actual expenditures and the MFH Balance Sheet. Annual financial reports are due to the Agency within 90 days of the end of the borrower’s fiscal year.

(1) Borrowers with 16 or more units in their housing project must base their annual financial reports on an engagement report completed according to agreed upon procedures established by the Agency as specified in paragraph (b) of this section. Borrowers must include the engagement report with their annual financial reports submitted to the Agency.

(2) Borrowers with less than 16 units in their housing project must submit annual financial reports using a limited scope engagement based on Agency approved procedures and certify that the housing meets the performance standards established in paragraph (c) of this section. Borrowers may use a CPA to prepare this report. For properties that prepare a limited scope engagement, the Agency may undertake random audits, once every two or three years.

(3) If a third party requires it, the borrower may have a CPA prepare an audit in accordance with generally accepted government auditing standards (GAGAS). Costs incurred to obtain this audit are an allowable project expense.

(b) *Engagement requirements.* Borrowers required to submit annual financial reports based on an engagement performed by a CPA must meet the following requirements:

(1) Borrowers must use an Agency approved engagement letter. Borrowers must submit the results of an engagement that examines specific records using agreed upon procedures established by the Agency and that describes the borrower’s performance in

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meeting the standards described in paragraph (c) of this section.

(2) The engagement will be initiated by the borrower using the Agency's engagement letter, which will specify the engagement program and establish the reporting requirements for the engagement.

(3) The engagement must be conducted by a CPA in accordance with American Institute of Certified Public Accountant (AICPA) Standards and Agency requirements.

(4) All engagement reports must be prepared for use by the Agency.

(c) *Performance standards.* Borrowers must ensure that:

(1) Required accounts are properly maintained and tracked separately;

(2) Payments from operating accounts are disclosed and accurately represented on financial reports;

(3) The reserve amount is at the authorized level and there are no encumbrances;

(4) Tenant security deposit accounts are fully-funded and are maintained in separate accounts and meet state and local requirements;

(5) Amount of payment of owner return was consistent with the terms of the applicable loan agreement;

(6) The borrower has maintained proper insurance in accordance with the requirements of §3560.105(b); and

(7) All financial records are adequate and suitable for examination.

(d) *Other financial reports.* (1) Non-profit and public borrower entities must submit audits in accordance with 7 CFR part 3052 that must also include the requirements set forth in the limited scope engagement.

(2) The Agency may require additional opinions of financial condition and compliance, such as audits, to assure the security of the asset, determine whether the housing project is being operated at a reasonable cost, or to detect fraud, waste, or abuse.

(3) Any audits independently obtained by the borrower also must be submitted to the Agency.

§ 3560.309 Advancement (loan) of funds to a RRH project by the owner, member of the organization, or agent of the owner.

(a) Prior written approval by the Servicing Office is required. Such ad-

vances may be authorized when justified by unusual short-term conditions. When conditions are not short-term in nature, a servicing plan may be developed and advances may be approved in accordance with the provisions set out in §3560.453 of this part. Justification will be based on the following:

(1) A review of the documented circumstances and the project operating budget before any funds are advanced (loaned). The financial position of the project must not be jeopardized.

(2) Funds are not immediately available from any of the following sources:

- (i) Reserve funds;
- (ii) Initial operating capital; and
- (iii) An imminent rent increase.

(b) The funds will be applied to ordinary project operating and maintenance expenses.

(c) Interest may be charged or paid on the loan from project income; however, interest must be reasonable. The proposal may be denied if Rural Development financing can be provided to resolve the problem in a more cost-effective manner.

(d) No lien in connection with the loan will be filed against the property securing the Rural Development loan or against project income. The advance may show as an unsecured project liability on financial statements prepared for year-end reports until such time as it is authorized to be repaid.

(e) The payback of the advance (loan) may be permitted by the Servicing Official provided the terms and conditions were mutually agreed to by the borrower and Rural Development at the time of the advance and the financial position of the project will not be jeopardized. Payback should only be permitted on the advance when the Rural Development debt is current and the reserve requirements are being maintained at the authorized levels.

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§ 3560.350 OMB control number.

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Subpart H—Agency Monitoring

§ 3560.351 General.

This subpart contains policies for Agency monitoring of operations and management at multi-family housing (MFH) projects.

§ 3560.352 Agency monitoring scope, purpose, and borrower responsibilities.

(a) *Scope of Agency monitoring activities.* The Agency will review reports, records, and other materials related to the housing project, including borrower financial reports, housing project records, and other communications. The Agency also will review material related to a housing project submitted by a tenant or other source. To assess conditions such as a housing project's physical condition, record keeping procedures, and operations and management activities, including borrower compliance with Federal, state, and local laws and Agency requirements, the Agency will conduct periodic on-site monitoring reviews of a housing project.

(b) *Purpose of Agency monitoring activities.* Agency monitoring activities are designed to assess borrower and tenant compliance with Agency requirements, and to:

(1) Ensure housing projects are managed in accordance with the goals and objectives of the Agency's MFH programs and are maintained in accordance with Agency requirements for affordable, decent, safe, and sanitary housing;

(2) Preserve the value of the Agency-financed housing projects;

(3) Detect waste, fraud, and abuse in housing project operations or management and to ensure the cost of oper-

ations and management are necessary and reasonable;

(4) Verify compliance with Affirmative Fair Housing Marketing requirements, Title VI of the Civil Rights Act of 1964, Title VIII of the Civil Rights Act of 1968, as amended, section 504 of the Rehabilitation Act of 1973, the Age Discrimination Act of 1975, Americans with Disabilities Act of 1990, other applicable Federal laws, and Agency requirements related to occupancy and tenant eligibility.

(c) *Borrower responsibilities.* The borrower is responsible for cooperating fully and promptly with Agency monitoring activities. Agency monitoring activities do not diminish borrower operation and management responsibilities and do not relieve borrowers from any Agency requirements including, but not limited to, borrower requirements to comply with:

(1) The terms of all agreements with the Agency, including the loan or grant agreement, assurance agreement, loan resolution, promissory note, mortgage, interest credit agreement, rental assistance agreement, mitigation measures contained in the environmental review document, and workout agreement;

(2) The requirements contained in this part;

(3) The requirements of Title VI of the Civil Rights Act of 1964, Title VIII of the Civil Rights Act of 1968, as amended; section 504 of the Rehabilitation Act of 1973, the Age Discrimination Act of 1975, Americans with Disabilities Act of 1990; and

(4) Applicable Federal, state, and local laws.

§ 3560.353 Scheduling of on-site monitoring reviews.

Generally, the Agency will provide the borrower prior notice of an on-site monitoring review and will conduct the on-site monitoring review in the presence of the borrower. However, the Agency may visit a housing project, without prior notice, to observe physical conditions, operations and management activities, or other borrower or tenant activities. In addition, the Agency may conduct on-site reviews without the presence of the borrower,