

**FHA Multifamily Housing Policy Handbook**  
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## UNIT 4 ASSET PRESERVATION

### CHAPTER 4.4 FLEXIBLE SUBSIDY LOANS

#### 4.4.1 PURPOSE

This chapter addresses two aspects of servicing flexible subsidy loans: 1) it provides guidance for the U.S. Department of Housing and Urban Development’s (HUD) review and approval of a project owner’s request to defer repayment of an Operating Assistance (OA) flexible subsidy loan when it becomes due; and 2) it provides guidance for HUD’s collection of delinquent Capital Improvement (CI) flexible subsidy loans and those already deferred OA flexible subsidy loans that are delinquent.

#### 4.4.2 AUTHORITY/BACKGROUND

A. Section 201 of the Housing and Community Development Amendments of 1978

- 1) The statutory authority of Section 201 of the Housing and Community Development Amendments of 1978 authorized HUD to provide OA loans as temporary funding to replenish project reserves, cover operating costs, and to pay for limited physical improvements. OA loans were provided in the form of a non-amortizing loan.
- 2) The statute also authorized HUD to provide CI loans to assist projects with the cost of major capital improvements when funding such improvements could not be done with project reserves. CI loans were generally provided in the form of an amortizing loan.
- 3) The flexible subsidy statute also required for both OA and CI loan programs that the owner maintain the project for low- and moderate-income persons for the remaining term of the original underlying mortgage.
- 4) HUD Handbook 4355.1 REV-1 (5/92), *Flexible Subsidy*, provides further information on the background of the flexible subsidy program. The flexible subsidy loan program is no longer an active program for new awards but many multifamily housing projects continue to have outstanding loans.

B. 24 CFR Part 219

- 1) OA loans were provided as contingent/deferred loans with no maturity date and are evidenced by a residual receipts note, financial assistance contract, and a use agreement. The interest rate is one percent per annum, not compounded, and is subject to the terms contained in the residual receipts note. The regulation at 24 CFR 219.220(b)(1995) requires repayment of an OA loan at the earliest of the expiration of the term of the mortgage, termination of mortgage insurance, prepayment of the mortgage, or sale of

104                    the project. 24 CFR Part 219 was subject to streamlining on April 1, 1996;  
105                    however, 24 CFR §219.2 provides a savings provision for Part 219.

106                    2) CI loans were provided in the form of an amortizing loan with an interest rate  
107                    between 3 and 6 percent. The owner executed a CI note and mortgage. CI  
108                    mortgages may be either recorded or subject to a Deferred Recording  
109                    Agreement. A flexible subsidy use agreement was executed and  
110                    incorporated by reference in the mortgage. CI loans also have a financial  
111                    assistance contract which was incorporated by reference in the mortgage.  
112                    Loan terms and conditions were as set out in 24 CFR §219.320(1995).

### 113                    C. HELP Loans

114                    The Emergency Supplemental Appropriations Act of 1994, Pub. L. 103-211 (2-  
115                    12-94), made available \$100 million in flexible subsidy funds specifically for use  
116                    assisting multifamily owners to recover from the southern California earthquake  
117                    of 1994. HUD implemented the HUD Earthquake Loan Program (HELP)  
118                    pursuant to Notice H 94-15. HUD created two categories of assistance under  
119                    HELP – HELP for Limited Repair Needs for eligible costs up to \$5,000 per unit,  
120                    which did not require that additional use restrictions be placed on the property;  
121                    and HELP for Major Repair Needs for eligible costs in excess of \$5,000 per unit,  
122                    which did require use restrictions of at least 10 to 15 years or until the HELP was  
123                    paid in full. For either HELP program, owners were permitted to request an  
124                    amortizing note or a non-amortizing note. If an owner requested a non-  
125                    amortizing note, repayment was required, at the option of the Secretary, upon the  
126                    earliest of: 1) 15 years from the date of loan closure, 2) upon termination or  
127                    maturity of the mortgage, 3) upon transfer of physical assets, sale, or refinance.

## 128                    4.4.3 FLEXIBLE SUBSIDY DEFERMENTS

### 129                    A. HUD Deferment of OA Loan

130                    1) As projects age, owners are seeking to preserve them as a long-term  
131                    affordable housing resource by taking out loans to repair and upgrade them.  
132                    Project financial resources may not in all cases be adequate to repay the OA  
133                    loan in full when it becomes due. This has prompted owners to request  
134                    deferral of the repayment to the end of the term of a newly obtained mortgage  
135                    or to the end of the term of new affordability restrictions. It is important to  
136                    note that HUD does not forgive OA or CI loans under any circumstances. In  
137                    addition, CI loans cannot be deferred beyond their original term. The CI Note  
138                    becomes due by the terms set out in the CI Note. Therefore, this section on  
139                    deferments does not apply to CI loans.

140                    2) HUD understands that the deferred repayment of an OA loan can be used to  
141                    facilitate recapitalization of a project. Therefore, the policies and procedures  
142                    in this section allow a repayment deferral when an owner demonstrates that

143                    the recapitalization is necessary and there are inadequate resources in the  
144                    transaction to pay the OA loan in full.

145                    3) HUD staff become aware that a flexible subsidy loan is due when a request  
146                    for prepayment approval of an FHA-insured mortgage is submitted by the  
147                    lender, or by the owner for a 202 direct loan or HUD-held loan (formerly  
148                    insured). HUD regional center/satellite office staff are made aware of an OA  
149                    loan becoming due on projects with a state non-insured 236 mortgage, or  
150                    projects financed under a state or local program providing assistance through  
151                    loans, loan assistance or tax abatements that has a rent supplement contract,  
152                    when the owner notifies them that the mortgages are being paid in full. For  
153                    FHA-insured, HUD-held (formerly insured) and 202 direct loans, the owner is  
154                    advised, through the prepayment approval terms and conditions, that the  
155                    flexible subsidy loan is due in full upon the prepayment. For state non-  
156                    insured 236 projects, and projects financed under a state or local program  
157                    with a rent supplement contract, the owner is advised by the multifamily  
158                    regional center/satellite office that the flexible subsidy loan is due in full upon  
159                    prepayment. If sufficient funds are not available to repay the OA flexible  
160                    subsidy loan, the owner may submit a deferment request by following the  
161                    procedures in this chapter.

162                    4) Deferments are applicable to all OA flexible subsidy loans as well as HELP  
163                    Minor and Major Repair loans, as may be approved by HUD.

164                    B. Regional Center/Satellite Office

165                    1) Many mortgages mature by their own terms, triggering repayment of the OA  
166                    or CI loan. Regional center/satellite office staff should routinely query the  
167                    Integrated Real Estate Management System (iREMS) for loans maturing  
168                    within 30-60 days that also have an outstanding OA or CI loan. At that time, a  
169                    letter should be sent to the owner advising that the flexible subsidy OA or CI  
170                    loan is due in full when the mortgage matures ([Exhibit 4.4-1](#)). If the owner has  
171                    an OA loan, the letter should also advise the owner to follow the procedures  
172                    in this chapter in order to submit a request for deferment of the OA loan if  
173                    sufficient funds are not available to repay the loan in full.

174                    2) The regional center/satellite office director has the authority to reject or accept  
175                    a deferment proposal based on the guidance in this chapter. If an OA  
176                    deferment proposal is accepted, the regional center submits a  
177                    recommendation, with all supporting documentation, to the Office of Asset  
178                    Management and Portfolio Oversight (OAMPO) in Headquarters, for review  
179                    and recommendation for a waiver of 24 CFR 219.220(b)(1995) by the  
180                    Assistant Secretary for Housing- Federal Housing Commissioner. If a HELP  
181                    Minor or Major Repair loan deferment is accepted, the regional center will  
182                    submit a recommendation, with all supporting documentation, to OAMPO in  
183                    Headquarters for review and a waiver of loan repayment requirements set out  
184                    in Notice H 94-15.

185            3) For any deferment request that involves a Section 236 mortgage (insured,  
186            HUD-held, or non-insured) and that will be part of a preservation transaction  
187            for the project, the owner submits the deferment request directly to the Office  
188            of Recapitalization (Recap). A transaction manager in Recap will review the  
189            deferment request, prepare a memorandum recommending approval for the  
190            Office of General Counsel (OGC) to review. After OGC review and approval  
191            for recommendation of a waiver, the transaction manager will prepare waiver  
192            memorandums for signature by the Assistant Secretary for Housing-Federal  
193            Housing Commissioner. Recap will follow the same guidance in this chapter  
194            for recommending approval of an OA flexible subsidy loan deferment.

195            4) If any proposed deferment request does not meet the requirements of this  
196            chapter, the regional center/satellite office director or the director of Recap  
197            will notify the owner in writing of the rejection and cite the deficiencies in the  
198            proposal.

#### 199    **4.4.4 THRESHOLD REQUIREMENTS FOR OWNER SUBMISSION**

200    Acceptance of a request to defer repayment of an OA flexible subsidy loan requires  
201    satisfaction of the following:

##### 202    A. Owner Compliance

203            Aside from the OA loan repayment requirements, the owner must be in  
204            compliance with all business agreements it has with HUD.

##### 205    B. Real Estate Assessment Center (REAC) Inspection

206            1) No deferral will be considered while exigent, health and safety (EHS)  
207            deficiencies are known to exist at the project.

208            2) With respect to the most recent REAC inspection, the project must have  
209            received a score of 60 or above, and all EHS deficiencies must have been  
210            corrected. In addition, all other deficiencies must have been corrected, or the  
211            owner must demonstrate how the deferment and/or refinancing will provide  
212            adequate funding to cure the deficiencies. Evidence must include a repair  
213            plan that details how all of the physical needs of the project will be addressed  
214            and written comments regarding the status of any corrective action in  
215            progress, e.g., what repairs have been completed, what other corrective  
216            actions have been taken, and target dates for completing these actions.

217            3) If a project is undergoing repairs and is overdue for its regularly scheduled  
218            inspection, an inspection must be performed after completion of project  
219            repairs and must score 60 or above. If no repairs are anticipated for the  
220            project and the project is overdue for its regularly scheduled inspection, an  
221            inspection must be performed prior to the deferment and receive a score of  
222            60 or above. In either instance, if the score is below 60 or EHS deficiencies

223            have been identified, the owner must follow the guidance listed above in item  
224            number 2.

225            4) If a project's mortgage has matured and there are no other business  
226            agreements with HUD requiring a REAC inspection, the project must have a  
227            current REAC score of 60 or above. If no inspection has been performed in  
228            three years, an inspection must be conducted prior to the deferment and must  
229            score 60 or above. If the project receives a score below 60, the owner must  
230            demonstrate how the deferment and/or refinance will provide adequate  
231            funding to cure the deficiencies. If EHS deficiencies are identified, they must  
232            be corrected prior to HUD's consideration of the deferral.

233            C. Fair Housing and Civil Rights Requirements

234            1) The project must be in compliance with all applicable fair housing and civil  
235            rights requirements contained in 24 CFR 5.105(a), including, but not limited  
236            to, the Fair Housing Act and its physical accessibility requirements, Title VI of  
237            the Civil Rights Act of 1964, and Section 504 of the Rehabilitation Act of  
238            1973. The owner must submit a certification of compliance with these  
239            requirements and a copy of the most recent Affirmative Fair Housing  
240            Marketing Plan (AFHMP) approved by the Office of Fair Housing and Equal  
241            Opportunity (FHEO). AFHMPs must be approved every 5 years.

242            2) Regional center/satellite office staff must consult FHEO for confirmation that  
243            owners are not:

244            a) defendants in a Fair Housing lawsuit filed by the U.S. Department of  
245            Justice (DOJ) alleging a pattern or practice of discrimination or denial of  
246            rights to a group of persons raising an issue of general public interest  
247            pursuant to 42 U.S.C. 3614(a);

248            b) recipients of a letter of findings identifying systemic noncompliance under  
249            Title VI of the Civil Rights Act of 1964, Section 504 of the Rehabilitation  
250            Act of 1973, or Section 109 of the Housing and Community Development  
251            Act of 1974; or

252            c) recipients of a charge from HUD concerning a systemic violation of the  
253            Fair Housing Act or have received a cause determination from a  
254            substantially equivalent state or local fair housing agency concerning a  
255            systemic violation of a substantially equivalent state or local fair housing  
256            law proscribing discrimination because of race, color, religion, sex,  
257            national origin, disability, and/or familial status.

258            3) HUD will not consider a deferral request unless these noncompliance issues  
259            have been resolved.

260            D. Management and Occupancy Review (MOR)

261            The project must receive satisfactory MOR ratings for the prior three review  
262            cycles. Otherwise, the owner must provide written comments regarding the  
263            status of any corrective action in progress, other corrective actions taken, and  
264            target dates for completing these actions. If an MOR has not been conducted at  
265            the project in the past 5 years, at a minimum, HUD staff must perform a desk  
266            review.

267            E. Annual Financial Statements (AFS)

268            The owner must have properly submitted all required AFS, and must have  
269            resolved all compliance flags, if any. In addition, monthly accounting reports for  
270            the prior three-year period must be submitted if the owner is required to submit  
271            them. For projects with a mortgage subject to Section 236, owners must have  
272            current excess income reports for the prior seven-year period, and must have no  
273            outstanding excess income payables.

274            F. Project's Mortgage

275            The project's underlying mortgage has been current for the past three years.

276            G. Absence of Defaults or Violations

277            The owner cannot have outstanding notices of default (NOD) or notices of  
278            violation (NOV) with any business agreements with HUD. Otherwise, the owner  
279            must demonstrate how the deferral and/or refinancing will provide adequate  
280            funding to cure the violation(s).

281            **4.4.5 PROGRAMMATIC REQUIREMENTS**

282            The owner requesting a deferral of repayment of an OA loan must comply with the  
283            requirements outlined in this section.

284            A. Use Agreement

285            1) The owner must execute and record a use agreement that is superior to all  
286            liens, including the refinanced mortgage. The use agreement extends project  
287            affordability for 20 years beyond the date of the original underlying mortgage  
288            maturity or the date of full repayment of the OA loan, whichever is longer.

289            2) In cases where the underlying mortgage has matured and the owner has not  
290            obtained new financing, the term of the OA loan may not exceed 20 years.

291            3) The use agreement also provides for continued HUD oversight and  
292            monitoring. The appropriate use agreements can be found in [Exhibits 4.4-2](#)  
293            [through 4.4-8](#).



294            B. Application of Residual Receipts

295            1) In the case of projects receiving project-based Section 8 assistance through a  
296            Housing Assistance Payments (HAP) contract subject to the old regulations  
297            (Notice of Selection issued prior to November 5, 1979) and those with project-  
298            based Loan Management Set-Aside (LMSA) HAP contracts, the residual  
299            receipts account balance must be applied to the outstanding balance of the  
300            OA loan in conjunction with HUD's approval of the deferral. In addition, for  
301            those projects subject to the above contracts beyond the date of deferral  
302            approval, all future residual receipts must be applied to the outstanding  
303            balance of the OA loan unless otherwise approved by HUD on a case-by-  
304            case basis.

305            2) Projects with Section 8 HAP contracts subject to the revised regulations  
306            (Notice of Selection for New Construction issued on or after November 5,  
307            1979; and Notice of Selection for Substantial Rehabilitation issued on or after  
308            November 20, 1980), are required to utilize residual receipts above \$250 per  
309            unit for HAP offset payments following the guidance found in Chapter 3.3 of  
310            this Handbook. Therefore, there are no residual receipts available to be  
311            applied to the outstanding OA loan.

312            C. Cooperative Projects

313            In the case of cooperatives, all funds in the General Operating Reserve  
314            account at the time of deferment approval only will be applied to the OA loan  
315            balance.

316            D. Application of Reserve for Replacement (RfR) Funds to the OA Loan Balance

317            1)     At the time of deferral approval, funds above the threshold minimum  
318            balance of \$1,000 per unit must be applied to the outstanding OA loan balance.  
319            After deferment, there is no further requirement to apply funds above the  
320            threshold minimum balance towards the OA loan.

321            2)     If some or all of the RfR funds are being used as a source in a refinance,  
322            the owner must provide supporting documentation (Sources and Uses  
323            statement). In these cases, there may not be available RfR funds to apply  
324            towards the OA loan. A refinance/sale must provide the necessary funds for  
325            all required repairs and upgrades to the project.

326            E. Owner Maximum Annual Distribution

327            If and to the extent the owner remains limited in its distributions of project funds  
328            after deferral approval, the owner must apply 15 percent of the owner maximum  
329            annual distribution to the outstanding deferred OA loan. The payment will be  
330            cumulative in the event there is no surplus cash available when the calculation is  
331            made. Surplus cash is defined in any surviving HUD business agreement  
332            between the owner and HUD.

333            F. Low-Income Housing Tax Credit (LIHTC)  
334            The owner must apply 15 percent of any LIHTC developer fee or deferred LIHTC  
335            developer fee to the outstanding OA loan.

336            G. Amortization of the Flexible Subsidy Loan  
337            HUD determines the amortization terms of the amended loan, including all  
338            outstanding principal and interest. If repayment will be from surplus cash only,  
339            HUD prepares a Surplus Cash Note.

340            H. Renewal of Housing Assistance Payments Contract

341            1) If there is a project-based Section 8 HAP contract in place at the project, the  
342            owner and regional center/satellite office director must mutually agree to  
343            terminate the existing HAP contract and execute a 20-year renewal contract  
344            that includes [Exhibit 4.4-3](#).

345            [2\) Exhibit 4.4-3](#) must be completed to provide that upon expiration, the 20-year  
346            renewal contract shall automatically renew for an additional term at least  
347            equal to the number of years remaining on the existing HAP contract being  
348            terminated by mutual agreement of HUD and the owner.

349            3) The HAP contract must include language that requires electronic submission  
350            of AFSs and adherence to the REAC physical inspection standards.

351            **Note:** The requirement for a 20-year renewal contract applies to project-  
352            based Section 8 HAP contracts only. Some Section 202 Direct Loan projects  
353            receive subsidies through a Project Assistance Contract (PAC). HUD does  
354            not have the authority to renew PACs for terms longer than one year.

355            **4.4.6 OWNER'S PROPOSAL**

356            A. Deferred Repayment of the OA Flexible Subsidy Loan

357            A successful application is one which shows that deferred repayment of the OA  
358            loan is necessary to achieve long-term project preservation. In addition to  
359            meeting the threshold and programmatic requirements, the owner must provide  
360            HUD the following information:

361            1) A copy of the residual receipts note, financial assistance contract, and use  
362            agreement evidencing the OA loan.

363            2) A copy of the current year's budget, most recent interim financial statement,  
364            and the last three fiscal years of audited AFS. The owner must use these  
365            statements to project available funds for 10 years going forward that will be  
366            available to fund monthly payments on the OA loan. Projections should detail

367                    trending assumptions and any changes in operations that may result in  
368                    deviations from historical results.

369                    3) A Sources and Uses statement for the transaction and a pro-forma operating  
370                    statement demonstrating that:

371                    a) All funds received in conjunction with the deferment transaction will be  
372                    used for project purposes.

373                    i) In a refinancing case, equity take-outs and other fees are prohibited.

374                    ii) In the case of a sale, the purchase price may not exceed the existing  
375                    project debt.

376                    Exception: In the case of a project sale using LIHTC, the difference  
377                    between the amount of the existing project debt and the appraised  
378                    value of the property on the sale date is secured by a seller note that  
379                    must be subordinate to all other notes and liens on the real estate and  
380                    requires repayment only to the extent of available surplus cash.

381                    b) In cases involving the use of LIHTC, permissible project expenses include  
382                    only those usual and customary fees and expenses for operating a tax  
383                    credit project, including:

384                    i) payment of the equity syndicator's asset management fees;

385                    ii) payment of the allocating state agency's compliance and asset  
386                    monitoring fees;

387                    iii) mandatory interest payments of up to one percent due on subordinate  
388                    debt provided by a governmental lender; and

389                    iv) deferred developer's fees, plus interest accrued at the applicable  
390                    federal rate, which may be deferred for no more than 12 years.

391                    The deferred developer's fee may be included as an operating budget line  
392                    item but can only be paid from surplus cash, as that term may be defined  
393                    in any surviving HUD business agreements. The project rents may not  
394                    exceed market rents for comparable units in the area. At the end of the  
395                    12-year fee deferment period, the project rents must be reassessed since  
396                    the deferred fee will have been fully paid.

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401            4) If resources are insufficient to repay the OA loan (in whole or in part) when it  
402            becomes due, the owner must show evidence of attempts made to secure loans  
403            or grants to repay the loan and document at least two rejections of loan  
404            applications.

405            5) The owner must also provide a written statement agreeing to comply with  
406            each of the programmatic requirements listed above.

407      **4.4.7 TERMS OF MODIFIED FLEXIBLE SUBSIDY LOAN**

408            A. Interest Rate

409            The interest rate remains the same as the rate on the existing OA loan. The  
410            regional center/satellite office may consider reducing the interest rate if the  
411            underwriting analysis justifies the need. In no case, however, may the rate be  
412            less than one percent.

413            B. Due on Sale

414            There shall be a due on sale, mortgage prepayment, mortgage expiration, or  
415            mortgage insurance termination clause, as applicable.

416            C. Repayment Term

417            1) In instances where the underlying mortgage has matured and the owner has  
418            not obtained new financing, the term of the deferred OA note may not exceed  
419            20 years.

420            2) If there is a refinancing, the term of the deferred OA note shall not exceed the  
421            term of the new mortgage.

422            D. Payoff Terms

423            Any remaining unpaid principal balance, plus accrued interest, is due and  
424            payable at the earliest occurrence of the following events:

425            1) after written notice to cure a failure to make monthly payments of principal  
426            and interest on the note and no payment is made within the time period set  
427            out in the notice to cure;

428            2) upon prepayment, maturity, or foreclosure of the refinanced first mortgage  
429            note (if applicable); or

430            3) upon the sale, transfer, assignment, or any other disposition of the project.

431            E. Debt Repayment

- 432            1) The owner can choose to make level annuity monthly payments that fully  
433            amortize the OA loan over a specified period.
- 434            2) If the modified OA loan is to be repaid under the terms of a surplus cash note,  
435            the note shall indicate the specific percentage of surplus cash due within 60  
436            days of the required filing of the audited or owner-certified AFS. Surplus cash  
437            is defined in any surviving HUD business agreement.
- 438            3) The regional center/satellite office, in its discretion, may permit a combination  
439            payment of level annuity monthly payments supplemented by a percentage  
440            of, or all available surplus cash annually.
- 441            4) The owner must apply 15 percent of the owner maximum allowable annual  
442            distribution from surplus cash to the outstanding OA loan. The payment is  
443            cumulative in the event there is no surplus cash available when the  
444            calculation is made.
- 445            5) The owner is required to pay 15 percent of any LIHTC developer fee or  
446            LIHTC deferred developer fee to the outstanding OA loan. The deferred  
447            developer fee period is no more than 12 years.

448            F. Right to Sell Flexible Subsidy Loan

449            HUD reserves the right to sell the OA note. If HUD sells the OA note, the owner  
450            will be required to submit an AFS to the new holder of the note in the same form  
451            submitted to HUD.

452            **4.4.8 UNDERWRITING ANALYSIS**

453            A. Complete Submission

454            The regional center/satellite office is responsible for determining that the owner's  
455            submission is complete and meets the threshold and programmatic requirements  
456            outlined in this chapter. If the submission is incomplete, it should be immediately  
457            returned to the owner. The regional center/satellite office confirms with HUD's  
458            Fort Worth Accounting Office the accuracy of the OA loan balance used in the  
459            owner's cash flow projections.

460            B. Management and Occupancy Reviews and Real Estate Assessment Center  
461            Inspection Reports

462            Regional center/satellite office staff perform an analysis of MORs and REAC  
463            inspection reports for owner/management agent capability to resolve current and  
464            future problems.

465            C. Sources and Uses Statement

466            The regional center/satellite office conducts a review of the Sources and Uses  
467            statement to confirm all funds received in conjunction with the transaction will be  
468            used for project purposes.

469            D. Base Year Net Operating Income

470            Regional center/satellite office staff determine the base year (first full year after  
471            closing of the refinancing) net operating income available to amortize the OA  
472            loan. The review must include the project's income, expenses, vacancy rate, and  
473            net operating income submitted by the owner, and make adjustments where  
474            necessary.

475            E. Analysis of Income and Expenses

476            Besides rent, other sources of income and adjustments must be analyzed. This  
477            includes, but is not limited to, parking, commercial space, laundry, tenant  
478            charges, and historical bad debt. The impact of the proposed use restriction is  
479            also examined. The regional center/satellite office selects three comparable  
480            projects from the Online Property Integrated Information Suite (OPIIS) and  
481            determines if the income and expense estimates provided by the owner fall within  
482            five percent of comparable projects. In the event of variations in excess of five  
483            percent, the regional center/satellite office provides the owner with an analysis  
484            and the owner then provides necessary justification.

485            F. Economic Vacancy Rate

486            The regional center/satellite office verifies the economic vacancy rate by  
487            reviewing the current rent roll and comparing these rents with the approved rent  
488            schedule.

489            **Note:** The economic vacancy rate takes into consideration the concessions and  
490            rent reductions that the owner may have used to increase the physical  
491            occupancy of the project. Because of concessions similar to these, the project  
492            may have a reasonable level of units occupied but the income may be insufficient  
493            to pay all expenses and debt service. The economic vacancy rate may show a  
494            flat to decreasing trend over the last six months.

495            **4.4.9 COLLECTION PROCEDURES FOR DELINQUENT CAPITAL IMPROVEMENT FLEXIBLE**  
496            **SUBSIDY LOANS AND DEFERRED OPERATING ASSISTANCE FLEXIBLE SUBSIDY LOANS**

497            The following collection procedures apply to: 1) all current and future delinquencies of  
498            CI loans, and 2) only those approved deferred OA loans that have an amortizing loan  
499            (deferred through the procedures outlined in this chapter) and are delinquent.

500            A. Credit Alert Verification Reporting System

501            It is HUD's policy that any CI loan that is not brought current or payment is not  
502            negotiated within 90 days of delinquency is reported to the Credit Alert  
503            Verification Reporting System (CAIVRS) (a federal government database of  
504            delinquent federal debtors that allows federal agencies to reduce the risk to  
505            federal loan and loan guarantee programs) and applicable action will be taken to  
506            collect on the loan immediately.

507            B. Extension of Loans

508            CI loans are amortizing (and in some instances non-amortizing) and payments  
509            began immediately after the loan proceeds were distributed. These loans cannot  
510            be extended beyond the maturity date of the original underlying mortgage or, with  
511            respect to non-insured projects, the remaining period during which the owner is  
512            under an obligation to provide for low-income families.

513            C. Execution of Note

514            Upon receipt of a CI loan, the owner was required to execute a note evidencing  
515            the CI loan, which is generally secured (24 CFR 219.320(c)(1995)). Pursuant to  
516            Section 4-4 of HUD Handbook 4355.1, the loan must be secured by the project.  
517            This required the owner to execute a CI mortgage that incorporated a use  
518            agreement ensuring the continuation of the character of the project if the  
519            underlying first note and mortgage are prepaid. If the project's first mortgage is  
520            insured, the CI mortgage was not recorded unless written consent was obtained  
521            from the insured lender who holds the first mortgage. If the insured lender that  
522            holds the first mortgage refuses to approve recording the CI mortgage, the  
523            borrower is required to execute a CI note and CI mortgage (or deed of trust) in  
524            recordable form and a Deferred Recordation Agreement. The Deferred  
525            Recordation Agreement allows the CI mortgage to be recorded when the first  
526            lender gives approval or when the mortgage is assigned to HUD.

527            D. Delinquent Loans

528            Delinquent CI loans and delinquent deferred amortizing OA loans are collected in  
529            accordance with the process detailed below. Upon maturity of the project's first  
530            mortgage, subject to verification of the maturity date of the CI loan, HUD may  
531            commence foreclosure proceedings to sell the project in order to repay the CI  
532            note if the loan is not paid in full. If the CI mortgage is not recorded, upon  
533            maturity of the project's first mortgage, the CI mortgage is recorded when the CI  
534            note becomes due by its term, and HUD may commence foreclosure  
535            proceedings to sell the project in order to repay the CI note, if the loan is not paid  
536            in full.

537            E. Collecting Delinquent CI and Deferred Amortizing OA Flexible Subsidy Loans

538            1) The Office of the Chief Financial Officer (OCFO) is responsible for  
539            maintaining the Northridge Loan System. HUD's Fort Worth Accounting Office  
540            uses Northridge Loan System to track flexible subsidy loan collections and  
541            delinquencies for those CI amortizing loans, since those loans are required to  
542            make monthly payments based on an amortization schedule, as well as any  
543            deferred OA loan that has been formally converted to an amortizing loan.  
544            Each month, regional center/satellite office directors receive an automated  
545            report for those amortizing flexible subsidy loans that have been delinquent  
546            for over 30 days. The reports include pertinent information regarding the  
547            delinquent principal and interest amounts for each delinquent loan for the  
548            previous month.

549            2) The account executive responsible for the delinquent loan listed on the report  
550            must send a delinquency letter ([Exhibit 4.4-10](#)) by certified mail, with a return  
551            receipt requested, to notify the owner of the loan delinquency within five  
552            business days of receiving the OCFO's report. The delinquency letter  
553            instructs the owner to bring the loan current within 30 days or to contact the  
554            account executive to discuss what options are available if the owner cannot  
555            do so. The delinquency letter also informs the owner that it is HUD's policy to  
556            begin collection proceedings on any flexible subsidy loan that is not brought  
557            current within 90 days of delinquency.

558            F. Owner Responsibilities

559            1) If the owner cannot bring the loan current upon receipt of the delinquency  
560            letter, the owner should contact their HUD account executive immediately to  
561            discuss repayment. If there is already a repayment plan in place in  
562            accordance with the procedures outlined for an OA loan deferment in the first  
563            part of this chapter, the owner should contact the account executive to  
564            discuss the status of repayment and if any amendments are needed to  
565            ensure timely repayment of the flexible subsidy loan. The owner must ensure  
566            that the flexible subsidy use agreement is recorded in first position, except  
567            when a prior recorded insured loan or other HUD-approved lien has a  
568            recording priority.

569            2) Owners who are unable to repay the delinquent portion of the flexible subsidy  
570            loan within 30 days of the delinquency letter should submit a request for relief  
571            to their appropriate HUD regional center/satellite office within 30 days of  
572            receipt of the delinquency letter.

573            G. Repayment Agreement and HUD Responsibilities

574            1) In some circumstances, HUD may agree to a repayment agreement for  
575            projects where full payment of the delinquent portion of the CI loan may  
576            destabilize the project. For CI loans, repayment plans may only extend to the



- 577            term of the original mortgage (if there is time remaining). Otherwise, the full  
578            loan amount is collected upon mortgage maturity or HUD initiates foreclosure  
579            proceedings to collect monies owed. HUD's regional center/satellite office  
580            must perform a detailed analysis of the owner's request for a repayment  
581            agreement and determine that the project meets the following criteria before  
582            granting approval:
- 583            a) The project owner is in compliance with its business agreements including  
584            the applicable recorded flexible subsidy use agreement, CI note and  
585            mortgage/deed of trust (if applicable), HAP contract, mortgage, loan  
586            agreement, and/or regulatory agreement.
- 587            b) Project management is satisfactory as evidenced by the most recent  
588            MOR.
- 589            c) Rents are at a sustaining level.
- 590            d) The physical condition of the project is satisfactory evidenced by the last  
591            REAC physical inspection score being 60 or above.
- 592            e) The project owner certifies that no additional funds are owed to the federal  
593            government.
- 594            2) Project owners may not take any otherwise allotted distribution until this debt  
595            is paid in full. Allowable distributions from surplus cash, as that term is  
596            defined in any surviving HUD business agreement, due to the owner is  
597            applied to the debt until the loan is current. Any surplus cash used to bring the  
598            loan current is not cumulative. Therefore, the owner may not seek  
599            reimbursement for funds expended.
- 600            3) Repayment agreements must be in writing and have a fixed monthly payment  
601            amount that allows for full payment of the delinquent portion of the flexible  
602            subsidy loan no later than 12 months from the date the repayment agreement  
603            is made. Requests for extensions beyond this 12-month time frame are  
604            considered on a case-by-case basis. The repayment agreement must include  
605            a confession of judgment for the entire amount of the flexible subsidy loan, so  
606            that, in the event of a default under the repayment agreement, HUD may, at its  
607            discretion, confess judgment and create a judgment lien against the project. If  
608            the repayment agreement matures in more than three years, approval by the  
609            Director of OAMPO is required.
- 610            4) A copy of the executed repayment agreement must be submitted to the  
611            financial operations analyst in the OCFO's Accounting, Monitoring and  
612            Analysis Division Payment Branch and to the Director of OAMPO, both in  
613            Headquarters.

614            5) If the project owner cannot meet the above criteria for a repayment  
615            agreement, the regional center/satellite office director may consider other  
616            repayment options on a case-by-case basis.

617            6) The regional center/satellite office ensures that all information regarding the  
618            flexible subsidy loan delinquency is reflected in iREMS.

619            H. Enforcement

620            1) If the owner does not bring the loan current or contact the account executive  
621            to discuss repayment options within 30 days of the date the delinquency letter  
622            was issued, the regional center/satellite office director issues a declaration of  
623            default by registered or certified mail with a return receipt requested. The  
624            declaration of default informs the owner of actions HUD may take 30 days  
625            after the issuance of the letter, including but not limited to:

626            a) referring the delinquent debt to FHA's Financial Operations Center (FOC)  
627            for debt collection;

628            b) flagging the owner in HUD's Active Partners Performance System (APPS);

629            c) denial of a distribution from surplus cash, as defined in HUD's business  
630            agreements, as long as the owner has a delinquent flexible subsidy loan;

631            d) allocating residual receipts funds to pay off the debt; and/or

632            e) reporting the delinquency to CAIVRS.

633            2) For CI Loans, HUD may begin foreclosure proceedings in accordance with  
634            the mortgage/deed of trust. If the CI mortgage is not recorded upon maturity  
635            of the project's first mortgage, the CI mortgage is recorded, and when the CI  
636            note becomes due by its terms, HUD may commence foreclosure  
637            proceedings to sell the project in order to repay the CI note if the loan is not  
638            paid in full.

639            3) HUD may also pursue other enforcement actions such as limited denial of  
640            participation (LDP) in certain HUD programs or debarment or suspension  
641            from government programs if the owner does not bring the loan current and  
642            HUD determines that the default was the result of any deliberate or voluntary  
643            action on the part of the borrower.  
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Exhibits 4.4-2 – 4.4-8 Use Agreements-

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