

Legal Opinion: CIM-0111

Index: 3.600
Subject: Preservation

May 1, 1995

Mr. Richard M. Price
Peabody & Brown
1255 23rd Street, N.W.
Washington, DC 20037

Dear Mr. Price:

Your letter to Michael Flores of the Honolulu, Hawaii Office of the Department of Housing and Urban Development ("HUD") dated January 27, 1995 regarding Maunakea Tower has been referred to our office for reply.

Your letter concerns the eligibility of the above project to participate in the preservation program under the Low-Income Housing Preservation and Resident Homeownership Act of 1990 ("LIHPRHA"), 12 U.S.C. 4101 note, or, in the alternative, the eligibility of the project owner to prepay the mortgage. For the reasons set forth below, we have concluded that the project is not eligible for participation under LIHPRHA. Furthermore, we have concluded that the project owner may not prepay its mortgage at this time. The project mortgage will, however, become eligible for prepayment without the Commissioner's consent on November 25, 1996 pursuant to the HUD regulations in effect on the date the mortgage note was initially endorsed for insurance.

The facts, as understood by our office, are as follows. The project mortgage was insured under Section 221(d)(3) of the National Housing Act with a limited dividend mortgagor. The mortgage note received initial endorsement for insurance on October 10, 1974 and was finally endorsed on November 24, 1976. The project is receiving assistance under Section 8 of the United States Housing Act of 1937 ("Housing Act"), 42 U.S.C. 1437f, but not as a result of a conversion from rent supplement assistance under Section 101 of the Housing and Urban Development Act of 1965 ("HUD Act"), 12 U.S.C. 1701s. The mortgage note contains a prepayment prohibition for the full term of the mortgage.

A project, to be eligible for participation under LIHPRHA, must meet the eligibility requirements of Section 229 of LIHPRHA. The implementing regulations which govern LIHPRHA eligibility are found at 24 CFR Part 248. Pursuant to LIHPRHA, the determination of "eligible low-income housing" is a two-part process. LIHPRHA defines "eligible low-income housing" as:

- "any housing financed by a loan or mortgage-
- (A) that is-
- (i) insured or held by the Secretary under

section 221(d)(3) of the National Housing Act and receiving loan management assistance under section 8 of the United States Housing Act of 1937 due to a conversion from section 101 of the Housing and Urban Development Act of 1965;

(ii) insured or held by the Secretary and bears interest at a rate determined under the proviso of section 221(d)(5) of the National Housing Act;

(iii) insured, assisted, or held by the Secretary or a State or State agency under section 236 of the National Housing Act; or

(iv) held by the Secretary and formerly insured under a program referred to in clause (i), (ii), or (iii); and

(B) that, under regulation or contract in effect before February 5, 1988, is or will within 24 months become eligible for prepayment without prior approval of the Secretary." LIHPRHA section 229(1).

While the project meets the second part of the eligibility test of Section 229(1)(B), it does not meet the first part under Section 229(1)(A)(i). The project mortgage is receiving assistance under Section 8 of the Housing Act, but not due to a conversion from assistance under Section 101 of the HUD Act as required by the statute. Therefore, the project is not eligible for assistance under LIHPRHA.

The HUD regulations that govern the mortgage insurance contract for the project are those which were in effect on the date the mortgage note was initially endorsed for insurance, October 10, 1974. The regulations which govern mortgages insured under Section 221(d)(3) are found at 24 CFR Part 221. Prepayment privileges are contained at 24 CFR section 221.524. Section 221.524(a) provides in relevant part that a mortgage may be prepaid without the Commissioner's prior consent:

"(ii) Where the mortgagor is a limited distribution type, which is not receiving payments from the Commissioner under a rent supplement contract executed pursuant to the provisions of sections 5.1 et seq. of this title, and where the prepayment occurs after the expiration of 20 years from the date of final endorsement of the mortgage." 24 CFR section 221.524(a)(1)(ii) (1974) (emphasis added).

The above regulatory section requires that the mortgagor be a limited distribution type, that the project not be receiving rent supplement assistance, and that 20 years have elapsed since the mortgage note was finally endorsed for insurance before the mortgage is prepaid. The project owner is a "limited distribution type." Moreover, the project is not receiving rent supplement assistance. The mortgage note, however, was not finally endorsed until November 24, 1976, thus the 20-year time period from the date of final endorsement will not expire until November 24, 1996. Therefore, the project mortgage is not yet eligible for prepayment without HUD's consent pursuant to

Section 221.524(a). It will, however, become eligible for prepayment without HUD's prior consent on November 25, 1996.

The prepayment prohibition in the note does not change the result of the above analysis. In this case the governing regulations, 24 CFR Part 221, and the mortgage note language are in direct conflict. You are correct that in such cases the regulations supersede contrary language in the note. The preamble and interim rules for LIHPRHA reflect the HUD policy that where there is a conflict between HUD regulations and mortgage note language, the regulations will govern. Furthermore, footnote 4 above reflects that the endorsement panel on the mortgage note provides that the regulations in effect on October 10, 1974 govern the contract of mortgage insurance. This position was expressed in the context of LIHPRHA at 56 Fed. Reg. 20262, 20267 (May 2, 1991) as follows:

"Likewise, if the applicable program regulations at section 221.524 or section 236.30 allow prepayment at the expiration of 20 years after final endorsement, but the mortgage note prohibits prepayment without HUD's consent for the full term of the mortgage, HUD would construe the regulation as superseding the prepayment prohibition in the mortgage note."

Therefore, despite the language in the note prohibiting prepayment, the project mortgage will become eligible for prepayment without prior HUD consent on November 25, 1996, which is after 20 years from the date of final endorsement, November 24, 1976.

In view of the foregoing, we conclude that the project is not eligible for participation under LIHPRHA because the project is not receiving Section 8 assistance due to a conversion from rent supplement assistance as required by the statute. We also conclude that the project mortgage is not eligible for prepayment without HUD's consent, but will become eligible under the applicable regulations on November 25, 1996, despite language in the mortgage note prohibiting prepayment.

I hope this letter has resolved your questions in this matter. If you have any further questions, please contact Athena Katcheves at (202) 708-3667.

Sincerely,

/s/David R. Cooper for

John J. Daly
Associate General Counsel
Office of Insured Housing