



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410-8000

OFFICE OF MULTIFAMILY HOUSING ASSISTANCE RESTRUCTURING

MEMORANDUM TO: PAEs
OMHAR Staff

FROM: April LeClair Chang, Senior Underwriter

DATE: February 6, 2003

SUBJECT: Clearing of Payables At The M2M Closing

The following procedures expand upon the requirements in our May 15, 2002 broadcast guidance on underwriting and provide a more formal process for identifying, approving, and clearing payables prior to a M2M closing. This memo also provides a new policy for transactions that leave M2M with an Action Other Than Closing (AOTC) and subsequently return to M2M.

Purpose. A primary purpose of the M2M program is to produce financially sound transactions. After the M2M closing, transactions should have sufficient funds to pay reasonable, ongoing expenses as well as debt service, IPF, etc. However, M2M underwriting does *not* anticipate that closed transactions would also have to pay off *other* obligations that have been previously amassed by the property. Therefore, M2M policy requires that all Excess Obligations (as defined in the attached) be paid off in conjunction with the M2M closing, to assure that property finances are not destabilized as a result of attempting to pay them after closing. See the attached Instructions and Forms of Certification for the information to be provided by owners, how Excess Obligations will be determined, and how they will be addressed.

Implementation. The certifications must be completed for all transactions that do not have Restructuring Commitments issued by the date of this memo. If this creates a hardship in any transaction, the Portfolio Director may waive the requirement at any time during the next two months. We would not expect waivers to be necessary thereafter.

Owner Investment. As with other M2M transaction costs, the normal owner investment is 20%, and this investment is eligible for Capital Recovery Payments (CRPs). However:

- **For any transactions that were completed PRIOR to the date of this memo** with an AOTC at the owner's decision, but that return to M2M, the owner will pay 20% of acceptable Excess Obligations, and this will not be eligible for CRPs.
- **For any transactions that are completed AFTER the date of this memo** with an AOTC at the owner's decision, and that return to M2M, the owner will pay 40% of acceptable Excess Obligations, and this will not be eligible for CRPs.
- **All arms-length TPAs** will be excluded from the policies in the two preceding paragraphs. The purchaser will pay 20% of acceptable Excess Obligations, and that investment will be eligible for Capital Recovery Payments.

Attachments: Instructions and Forms of Certification

INSTRUCTIONS FOR CERTIFICATIONS CONCERNING ACCOUNTS PAYABLE

Initial Certification For Restructuring Commitment. The owner will complete one of the two attached certifications so that an estimate of the amounts to be cleared can be included in the Restructuring Commitment. The PAE will transmit the certification to the Multifamily Hub or Program Center for review and a determination whether the obligations are acceptable. Form A is for properties that have a history of positive Surplus Cash; Form B is for all other properties.

Final Certification For Closing. The owner will certify again, just prior to the M2M closing. If needed, the PAE will consult with the Hub or Program Center concerning any material new payables added since the initial certification.

‘As Of’ Date For Certifications. The PAE and owner will agree on an ‘as of’ date for each certification, appropriate for the owner’s accounting system and as recent as practicable.

Supporting Information. Owners should provide supporting information (such as invoice copies and information supporting the reasonableness of the amount paid) for any obligations that might be questioned.

Amount of Excess Obligations To Be Cleared. The PAE will require that all Excess Obligations be cleared. “Excess Obligations” means obligations (from Attachments A and B to the certification) in excess of available assets (from Attachments C and D to the certification). Typically, the most recent obligations will be offset against available assets. If the status of an obligation as “excess” is disputed, HUD’s determination shall be final. Excess obligations acceptable to HUD will be cleared as transaction costs of the M2M closing. **Obligations not acceptable to HUD must be paid by the owner, from non-project funds, and without regard to whether such obligations are “excess.” The PAE and OMHAR will not schedule the M2M closing until these unacceptable obligations have been paid off.**

Items Generally Not Acceptable As Transaction Costs. The Multifamily Hub or Program Center has full discretion to accept or not accept obligations. Owners should, however, expect that the following types of obligations generally will not be allowed as transaction costs:

- Entity expenses (including owner costs related to Mark-to-Market).
- Expenses that cannot be documented to the satisfaction of the Hub or Program Center.
- Amounts in excess of what is typical and customary for similar properties in the area in which the property is located.
- Items that were approved to be funded in other ways (for example, items for which a rent increase was previously approved).
- Mortgage delinquencies (unless approved by the PAE).
- Delinquent Reserve deposits (unless approved by the PAE).
- Deficient escrow accounts (these are normally brought current at the M2M closing).
- Under-funding of the Security Deposit account.

FORM A OF OWNER CERTIFICATION RE: ACCOUNTS PAYABLE

[PAE name and address]

[date]

[OMHAR Portfolio Director name and address]

Dear PAE and OMHAR:

Re: [name of project, FHA number, city, state] (the "Project")
Owner's Certification Regarding Accounts Payable

This certification is given in connection with the planned Mark-to-Market ("M2M") restructuring of the Project, [reflected in / to be reflected in] a Restructuring Commitment by and between [name of ownership entity] (the "Owner") and HUD's Office of Multifamily Housing Assistance Restructuring ("OMHAR"). The Owner hereby certifies that:

1. The information contained herein is true and correct. The person whose signature appears below is duly authorized to make this certification on behalf of the Owner and has reviewed all relevant books and records of the Project. The Owner understands that the PAE and OMHAR will rely upon the accuracy of this certification in developing and approving the M2M restructuring of the Project. In the event any statement in this certification is no longer correct or complete, the Owner agrees to immediately issue an amended certification.
2. The most recently issued audited financial statements of the Project reflected positive Surplus Cash.
3. The Owner believes that, if the Project were to issue audited financial statements as of the date of this certification, such statements would reflect positive Surplus Cash.

Owner represents and warrants that this certification is correct and complete, and that no changes have been made to the wording of the standard form of certification promulgated by OMHAR. Owner agrees that failure to certify correctly and completely is a breach of the Restructuring Commitment. Owner agrees that, in addition to any other penalties and remedies available to HUD, failure to certify correctly and completely is a failure to materially comply with requirements of the Multifamily Assisted Housing Reform and Affordability Act of 1997 as those requirements apply to the Project and, as such, is grounds for acceleration of any Mortgage Restructuring Note and/or Contingent Repayment Note executed pursuant to the Restructuring Commitment.

[name and title of authorized Owner representative]

[date]

FORM B OF OWNER CERTIFICATION RE: ACCOUNTS PAYABLE

[PAE name and address]

[date]

[OMHAR Portfolio Director name and address]

Dear PAE and OMHAR:

Re: [name of project, FHA number, city, state] (the "Project")
Owner's Certification Regarding Accounts Payable

This certification is given in connection with the planned Mark-to-Market ("M2M") restructuring of the Project, [reflected in / to be reflected in] a Restructuring Commitment by and between [name of ownership entity] (the "Owner") and HUD's Office of Multifamily Housing Assistance Restructuring ("OMHAR"). The Owner hereby certifies that, as of [insert 'as of' date for certification]:

1. The information contained herein is true and correct. The person whose signature appears below is duly authorized to make this certification on behalf of the Owner and has reviewed all relevant books and records of the Project. The Owner understands that the PAE and OMHAR will rely upon the accuracy of this certification in developing and approving the M2M restructuring of the Project. In the event any statement in this certification is no longer correct or complete, the Owner agrees to immediately issue an amended certification.
2. Attachment A hereto is a complete list of Accounts Payable of the Project, indicating date incurred, amount, vendor name, general nature of the goods or services purchased, and indicating whether the vendor has any Identity of Interest with any Principal of the ownership entity and/or any Principal of the property management agent. "Accounts Payable" means all items eligible to be reported on HUD/FASS Account 2110 "Accounts Payable – 30 Days." "Identity of Interest" is defined in HUD Handbook 4370.2, Chapter 3, paragraph 3-4, item 17. "Principal" is defined in the Mark-to-Market Operating Procedures Guide, Appendix A.
3. Attachment B hereto is a list of all Other Project Liabilities of the Project. "Other Project Liabilities" means amounts eligible to be reported on HUD/FASS Surplus Cash accounts S1300-080 "Loans and Notes Payable [due within 30 days]", S1300-100 "Accrued Expenses [not escrowed]", 2210 "Prepaid Revenue", or S1300-110 "Other Current Obligations."
4. Attachment C hereto is a complete list of the balances in all cash accounts (including any investment and petty cash accounts) eligible to be reported on HUD/FASS account 1120 "Cash – Operations."
5. Attachment D hereto is a complete disclosure of (a) all applications that have been made by or on behalf of the Project or the Owner for withdrawals from the Project's Reserve for Replacements or Residual Receipts accounts; (b) all Accounts Receivable of the Project (other than from Project tenants); (c) all insurance claims that have been filed on behalf of the Project or the Owner (for which proceeds have yet to be received); and (d) all events that have occurred with respect to the Project or the Owner and for which insurance claims may be filed. "Accounts Receivable" means amounts eligible to be reported on HUD/FASS

Surplus Cash account S1300-030 "Other Cash."

Owner agrees that Accounts Payable and Other Project Liabilities of the Project, incurred prior to the M2M closing date but not referenced in this certification, are not "eligible project expenses" as defined by the Secretary of HUD, shall not be paid from Project funds, and shall be paid promptly by the Owner from Non-Project Funds, except as follows:

- Accounts Payable and Other Project Liabilities for normal monthly recurring costs incurred after the date of this certification, that are consistent with typical monthly amounts incurred previously by the Project and consistent with amounts underwritten by the PAE, may be paid before or after the closing as eligible project expenses.
- Other pre-closing Accounts Payable and Other Project Liabilities may be paid after the date of this certification as eligible project expenses only after HUD issues specific prior written approval.

"Non-Project Funds" means funds of the Owner that are not assets of the Project (other than surplus cash distributable and distributed to the Owner), and that are not proceeds of any loan secured by the Project.

Owner agrees that, if any Accounts Payable or Other Project Liabilities are paid as M2M transaction costs, and if the property has positive Surplus Cash as of its first fiscal year-end following the M2M closing, all such positive Surplus Cash will be treated as having been generated subsequent to the M2M closing, for purposes of the June 27, 2002 memorandum from Beverly Miller, entitled "**Surplus Cash Payments after Mark-to-Market Closing.**"

Owner represents and warrants that this certification is correct and complete, and that no changes have been made to the wording of the standard form of certification promulgated by OMHAR. Owner agrees that failure to certify correctly and completely is a breach of the Restructuring Commitment. Owner agrees that, in addition to any other penalties and remedies available to HUD, failure to certify correctly and completely is a failure to materially comply with requirements of the Multifamily Assisted Housing Reform and Affordability Act of 1997 as those requirements apply to the Project and, as such, is grounds for acceleration of any Mortgage Restructuring Note and/or Contingent Repayment Note executed pursuant to the Restructuring Commitment.

[name and title of authorized Owner representative]

[date]

[list attachments]