Office of Hospital Facilities
Lender Training

HUD Headquarters
Brooke-Mondale Auditorium

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Underwriting Overview – Program Eligibility Requirements and the Underwriting Process

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Underwriting Division Outline

- Hospital Mortgage Insurance Programs
- Statutory/Regulatory eligibility requirements
- Pre-Application and Application Processes
Hospital Mortgage Insurance Programs

**Insurance Types Available:**

- **§242:** For hospitals *not* currently in the FHA portfolio seeking financing for new construction projects or substantial rehabilitation (may include mortgage proceeds for existing debt refinance – up to 80% of the loan amount).

- **§223(f):** For hospitals either *not* currently in the FHA portfolio seeking to refinance existing capital debt (may include mortgage proceeds for capital improvements – up to 20% of the loan amount) or, in limited cases, for hospitals already in the FHA portfolio.

- **§241:** For hospitals already in the FHA portfolio seeking financing for new construction projects, substantial rehabilitation, or additions.

- **§223(a)(7):** For hospitals already in the FHA portfolio seeking to refinance existing FHA loans.

- **Interest Rate Reduction:** For hospitals already in the FHA portfolio seeking interest rate reductions on existing FHA loans, without increasing UPB or the term of the existing loan.
Program Guidance

➢ Statute – Section 242 of the National Housing Act
  ▪ 12 U.S.C. 1715z–7

➢ Regulation - Hospital Mortgage Insurance Program - 24 CFR Part 242
  ▪ [https://www.ecfr.gov/cgi-bin/retrieveECFR?gp=1&SID=0d6edd1462c5c07502e67d556895bc0e&ty=HTML&h=L&mc=true&n=pt24.2.242&r=PART](https://www.ecfr.gov/cgi-bin/retrieveECFR?gp=1&SID=0d6edd1462c5c07502e67d556895bc0e&ty=HTML&h=L&mc=true&n=pt24.2.242&r=PART)

➢ Handbook - 4615.1
  ▪ [https://www.hud.gov/program_offices/administration/hudclips/handbooks/hsgh/4615.1](https://www.hud.gov/program_offices/administration/hudclips/handbooks/hsgh/4615.1)
Statutory Eligibility Criteria

- **Loan-to-Value Requirement**
  - Maximum LTV for Section 242, 241, 223(f) programs = 90%
  - Based on net book value of property, plant, and equipment
  - Appraisals may be used to meet the LTV requirement

- **First Lien**
  - The FHA-insured lender must have a first lien position on real estate
  - FHA requires that the Lender also have a first lien on revenues and accounts receivable (unless approved in writing by HUD)
Market Need

- Per language in the Statute: “The purpose of this section is to assist the provision of urgently needed hospitals...”
- OHF performs a market need review, based on data provided by the hospital and other in-house sources

Patient Day Requirement

- Acute care patient days must be greater than 50% of total patient days
- Non-acute patient days include rehabilitation, psychiatric, and other services listed in the statute
Regulatory Eligibility Criteria

- §242.16 - Historical Operating Margin Requirement
  - The 3-year aggregate Operating Margin must exceed 0%.

- §242.16 - Historical Debt Service Coverage Ratio Requirement
  - The 3-year average Debt Service Coverage Ratio must exceed 1.25x (1.4x for Section 223f).

- §242.72 - Owner/Operator
  - The Owner must also be the facility operator
§242.8, §242.64, Collateral Requirements

- All critical pieces of the property and operations must be captured as collateral

§242.4 - Capital Purchases

- Mortgage Proceeds must be used for capital purchases, or to refinance loans originally used to purchase capital

§242.11 - Compliance with State and Federal Regulations

- If under investigation, it must be disclosed to HUD and evaluated
Other Regulatory Highlights

**§242.14 – Mortgage reserve fund (MRF)**

- An MRF must be funded after loan closing (223f) or construction completion (242, 241)
  - Standard Requirements:
    - At 5 years, the Borrower must have deposited 12 months of debt service
    - At 10 years, must have deposited 24 months of debt service
Program Fees

- **Application (One-Time) Fees**
  - Application fee (0.15% of the mortgage amount)
  - Commitment fee (0.15% of the mortgage amount)
  - Inspection fee (ranges from 0.1% to 0.5% of the mortgage amount, depending on the Section of the Act and hard costs included in the mortgage)

- **Ongoing (Annual) Fees - MIP**
  - Ranges from 55 bps (223a7) to 70 bps (242), with first-year exceptions
Process Overview

- Pre-Application
  - Pre-Screening Tool
  - Preliminary Review
  - Pre-Application Meeting

- Application Process
Pre-Application / Pre-Screen and Preliminary Review

- **Pre-Screening Tool**

- **What is the purpose of the Preliminary Review**
  - Evaluate hospitals against minimum eligibility requirements

- **How does it benefit Lenders and HUD?**
  - There are no fees associated with the Prelim process
  - Identify Statutory/Regulatory/Credit barriers
  - Identify areas of focus for the Pre-Application Meeting and application underwriting
Pre-Application Overview / Preliminary Review

➢ Preliminary Review Submission Contents
  - Preliminary Review Template
  - Audited financial statements
  - Utilization statistics
  - Project description
  - Organizational chart/collateral discussion
  - Other items listed in Appendix 3 of the Handbook (Pre-Applicant’s Guide)

➢ OHF Review
  - Review of eligibility
  - Credit review
Pre-Application Overview / Preliminary Review

- Credit/Programmatic Review
  - Financial Statement review
  - Market Review
  - Regulatory/Policy Review
  - Other Unique Issues

- Process – Underwriter review, followed by brief committee review

- Goal: Provide feedback to lender in 2 weeks
What is the purpose of the Pre-Application Meeting

- Discuss issues identified during the Preliminary Review
- Overview of the Hospital and its project

Following the meeting, OHF staff meets and determines next steps
Underwriting Process Overview / Application

➤ Application Requirements/Development

- Volume 1
  - Application form (sources and uses)
  - Information on the Board Members, Executives
  - Other requirements

- Volume 2
  - Financial Statements and budget
  - Forecast (if applicable)
  - Other Requirements

- Volume 3
  - Architectural and Engineering documents
Steps in the Application Process

1. Application Receipt and Completeness Review
2. Underwriting Questions
3. OHF Site Visit
4. Previous Participation (2530) review
5. Architectural/Engineering/Environmental Review
6. Credit Report development
7. Credit Committee Review
8. Approvals (if applicable) – Deputy Assistant Secretary of OHP, Office of Risk Management
Process Processing Times

- **Preliminary Review**
  - 10 business days for Sections 242, 241, 223(f)

- **Application Completeness Review**
  - 10 business days for Sections 242, 241, 223(f)

- **Application Review**
  - 120 business days for Section 242 and 241
  - 90 business days for Section 223(f)
  - 30 days for Section 223(a)(7)
Underwriting Transaction Metrics

Mr. Paul Giaudrone
Director of Underwriting
Office of Hospital Facilities
Hospital Program Production (FY15 – FY20 (YTD))

- 25 successful applications
- $2.28 Billion
  - 10 Section 241 loans totaling $1.0B
  - 6 Section 223(a)(7) loans (including 1 portfolio hospital 223(f) loan) totaling $515M
  - 9 Section 223(f) loans totaling $754M
## OHF Commitment Metrics

### Medians for FY 2015 to 2020 (YTD) Commitments

<table>
<thead>
<tr>
<th>Metric</th>
<th>223(f)</th>
<th>223(a)(7)</th>
<th>241</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Commitments</td>
<td>9</td>
<td>6</td>
<td>10</td>
</tr>
<tr>
<td>Total Revenue</td>
<td>$264,742,000</td>
<td>$59,409,559</td>
<td>$406,875,768</td>
</tr>
<tr>
<td>Mortgage Amount</td>
<td>$47,642,200</td>
<td>$50,976,000</td>
<td>$58,062,000</td>
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<tr>
<td>Operating Margin</td>
<td>0.5%</td>
<td>0.2%</td>
<td>3.0%</td>
</tr>
<tr>
<td>Total Margin</td>
<td>1.0%</td>
<td>1.3%</td>
<td>4.7%</td>
</tr>
<tr>
<td>Debt Service Coverage</td>
<td>2.0</td>
<td>1.9</td>
<td>3.0</td>
</tr>
<tr>
<td>Days Cash on Hand</td>
<td>109.3</td>
<td>58.2</td>
<td>70.7</td>
</tr>
<tr>
<td>LTD to Capitalization</td>
<td>35.8%</td>
<td>65.9%</td>
<td>52.1%</td>
</tr>
<tr>
<td>Loan to Value</td>
<td>68.9%</td>
<td>86.9%</td>
<td>71.7%</td>
</tr>
<tr>
<td>Mortgage Amount/Revenue</td>
<td>45.3%</td>
<td>88.9%</td>
<td>42.3%</td>
</tr>
</tbody>
</table>
Metrics Analysis – Takeaway Points

- OHF looks for a combination of strengths in broad metric areas (liquidity, leverage, profitability).
- “Deal Killers” (for 242 and 223(f) in particular) – very low or negative net assets, very low days cash on hand (<10 days), Mortgage/Revenue ratio > 1.0, going concern opinion
- Disclaimer – all projects are different, and evaluated on their individual merits
Median Processing Times (FY15-20 projects)

- Preliminary Reviews – 21 days (ranged from 5 to 85 days).
- Prelim Review Letter to Pre-App Meeting – 39 days (ranged from 19 days to 113 days).
- Pre-App Meeting to Complete Application – 126 days (ranged from 32 to 290 days).
- Application Complete to Commitment – 84 days (ranged from 27 to 225 days).