



OFFICE OF HEALTHCARE PROGRAMS



Office of Hospital Facilities Lender Training

Virtual Presentation

September 22, 2020

Opening Remarks

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- Welcome to 2020 OHF Lender Training
- Opening remarks by:

Roger Lukoff

Deputy Assistant Secretary for the Office of Healthcare Programs

Geoffrey Papsco

Director, Office of Hospital Facilities



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Overview of the 242 Portfolio

Mr. Geoffrey Papsco
Director
Office of Hospital Facilities



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Overview

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- **Office of Healthcare Programs (OHP) consists of:**
 - Office of Hospital Facilities
 - Office of Residential Care Facilities
 - Office of Architecture and Engineering (support office)
- **OHP's mortgage insurance programs enable affordable financing of healthcare facilities:**
 - Section 242 Mortgage Insurance for Hospitals
 - Section 232 Mortgage Insurance for Nursing Homes, Assisted Living Facilities, Board & Care Homes



**Buffalo grazing outside Rio Grande Hospital
Del Norte, CO**

History of FHA's Office of Healthcare Programs

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Hollywood Presbyterian
Medical Center
Los Angeles, CA

- Section 242 of the National Housing Act was enacted by Congress in 1968:
 - To support capital financing for urgently-needed hospitals and encourage lending for needed hospital projects.
- Section 232 of the National Housing Act was established by Congress in 1959:
 - To support the critical care needs of a vulnerable aging population in residential care facilities across the country.

Role of FHA in Helping Private Lenders Serve the Healthcare Market

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- FHA facilitates the construction and refinancing of healthcare facilities through private lenders
- Without FHA mortgage insurance, lenders would not lend to most of the facilities that have FHA loans, or would only do so at prohibitively high interest rates
- Without FHA, results would be:
 - Fewer facilities built, modernized, or refinanced, limiting access to hospital care
 - Higher operating costs for facilities that chose high rates



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Office of Healthcare Programs: What We Do

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- Enable the affordable financing of needed healthcare facilities
- Strengthen communities - healthcare facilities are economic engines
 - Nationwide, hospitals employ approx. **7.0 million people** and generate a total revenue of over **one trillion U.S. dollars.**

*Statistics based on data as of 11/8/18, <https://www.statista.com/topics/1074/hospitals/>

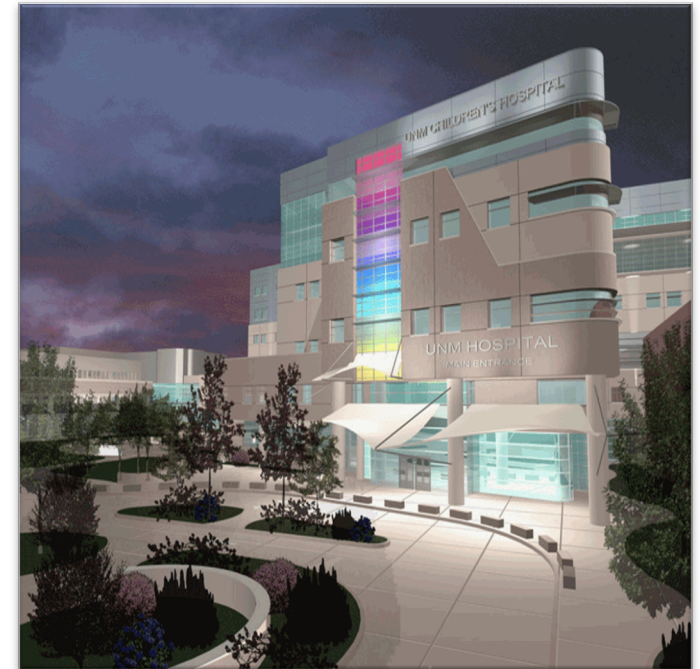


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Office of Hospital Facilities Highly Specialized Staff

- **An office of 27 professionals with expertise in and a single focus on the financing and operations of hospital facilities**

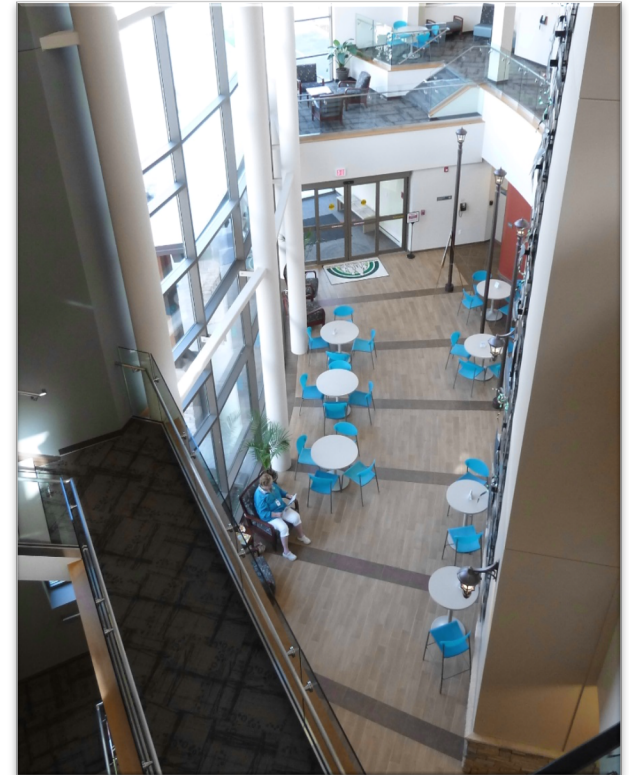


University of New Mexico Hospital
Albuquerque, NM

Qualifications of OHF Program Staff

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- Former Health Care Executives
- Former Business (Lending, Finance, etc.) Executives
- Professional Society Fellows
- Former State Finance Authority Executives
- Majority of Staff Possess Graduate Degrees, including:
 - PhDs, Juris Doctors, MBAs, MHAs
- Certified Public Accountants
- Registered/Licensed Nurses



Interior of Coquille Valley Hospital
Coquille, OR

➤ Comprised of two divisions:

- Underwriting Division
 - Functions include all underwriting activities involved in the review and processing of Section 242 mortgage insurance applications, client assistance, and staff training.
- Asset Management Division
 - Functions include portfolio management, client assistance, default prevention, and risk management.



Baton Rouge General Hospital
Baton Rouge, LA

Hospitals that Use FHA

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➤ **FHA serves all types of hospitals nationwide**



Matagorda Regional Medical Center
Bay City, TX

- Acute care hospitals
- Rural and Critical Access Hospitals (CAHs)
- Large urban teaching hospitals
- University hospitals
- Not-for-profit, for-profit, and government-owned hospitals

➤ **Enables urgently-needed hospitals underserved by the private capital market to obtain access to capital.**

Attractive Program Features

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New York-Presbyterian
New York, NY

- No maximum loan amount
- Loan-to-value up to 90%
- Loan term up to 25 years
- Fixed annual premiums
- Section 241 supplemental loans
- 223(a)7 and 223(f) refinancing options for hospitals

Current 242 Portfolio

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- 65 hospitals presently in the insured 242 portfolio, totaling 87 active loans*
- \$6.0 billion in unpaid principal balances (UPB) in the current 242 portfolio*
- Facilities located in 29 states and Puerto Rico*



Kirby Medical Center
Monticello, IL

*Statistics based on data as of 6/30/20



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Office of Hospital Facilities Lender Training

HUD Headquarters
Brooke-Mondale Auditorium

September 22, 2020



Underwriting Overview – Program Eligibility Requirements and the Underwriting Process

Ms. Shelley McCracken-Rania, CPA, MBA
Senior Financial Analyst
Office of Hospital Facilities



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Underwriting Division Outline

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



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Hospital Mortgage Insurance Programs

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➤ 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.



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➤ Statute – Section 242 of the National Housing Act

- 12 U.S.C. 1715z–7
 - https://www.hud.gov/sites/documents/SEC242_STATUTE.PDF
- 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=tr ue&n=pt24.2.242&r=PART>
- Handbook - 4615.1
 - https://www.hud.gov/program_offices/administration/hudclips/handbooks/hsg/4615.1

Statutory Eligibility Criteria

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➤ **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)



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Statutory Eligibility Criteria (Cont.)

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➤ 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



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Regulatory Eligibility Criteria

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- **§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



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Regulatory Eligibility Criteria (Cont.)

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➤ §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

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➤ §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



➤ **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

➤ Pre-Application

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

➤ Application Process

➤ Pre-Screening Tool

- https://portal.hud.gov/hudportal/HUD?src=/federal_housing_administration/healthcare_facilities/section_242/Prescreening242

➤ 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

➤ 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

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➤ 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



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- **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**

➤ **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

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➤ 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



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Hospital Program Production (FY15 – FY20 (YTD)) ²¹

➤ **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

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Medians for FY 2015 to 2020 (YTD) Commitments			
	223(f)	223(a)(7)	241
Number of Commitments	9	6	10
Total Revenue	\$264,742,000	\$59,409,559	\$406,875,768
Mortgage Amount	\$47,642,200	\$50,976,000	\$58,062,000
Operating Margin	0.5%	0.2%	3.0%
Total Margin	1.0%	1.3%	4.7%
Debt Service Coverage	2.0	1.9	3.0
Days Cash on Hand	109.3	58.2	70.7
LTD to Capitalization	35.8%	65.9%	52.1%
Loan to Value	68.9%	86.9%	71.7%
Mortgage Amount/Revenue	45.3%	88.9%	42.3%



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Metrics Analysis – Takeaway Points

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- 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



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Median Processing Times (FY15-20 projects)

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- **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).



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Office of Hospital Facilities Lender Training

Virtual Training Session
September 22nd and 24th

HOSPITAL

OHF “Best Practices” for Asset Management

- **Reminder: As the saying goes “When you have seen one Regulatory Agreement, you have seen one Regulatory Agreement” as there have been many changes to the Reg Agreements over the life of the program.**
- **Therefore it is extremely critical to review the Regulatory Agreement for your respective borrower.**

Best Practices for Asset Management

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- Sometimes issues with the Reg Agreement are reported “after the fact”.
- Examples include, but are not limited to:
 - Distribution of Assets to Affiliate
 - Additional Indebtedness
 - After-acquired property
 - Collateral Release
 - Board Report of Business Plan section
 - Remodeling and renovations to collateral

➤ Compliance Monitoring and Reporting:

- Need to understand Borrower's Compliance Monitoring.
- HUD and the Lender should work together to identify:
 - Who in the Borrower's organization monitors regular compliance with the HUD Regulatory Agreement and other legal documents
 - Examples include Compliance officer; CFO; others in the C-suite
 - Frequency of compliance monitoring and reporting by Borrower's Management and the Board
 - Who in the Borrower's organization is responsible for contacting OHF for modifications and renovations to FHA-insured collateral.

➤ Regulatory Agreement – Filing of financial statements:

- Per Reg 242.58:
 - Quarterly unaudited financials must be submitted within 40 days following the end of each quarter (or 40 days after month end if requested by HUD)
 - This also applies to fourth quarter unaudited financials.
 - Note that the reg wording does not allow for extensions on interims.
- Board Certified financials within 120 days following the close of the FYE (if the audit has not yet been filed with HUD) and at such times as HUD may designate on a case-by-case basis.
 - “On a case-by-case basis” allows HUD to provide extensions, if appropriate.
 - Requires written request from borrower with reason for 30-day extension and filing date. Must be received in advance of filing deadline.
 - 30 day is maximum extension that can be provided but borrowers can request additional extensions beyond that with good cause.

➤ Regulatory Agreement – Filing of financial statements

■ Regulatory Agreement:

- ✓ New Regulatory Agreement: Requires Borrower to provide financial information to both HUD and the Lender.
- ✓ Old Regulatory Agreements:
 - Borrower not required to share information with the Lender and HUD cannot forward/share information provided by the Borrower to outside parties, including the Lender.
 - Borrower must provide Lender with annual audited financial statements in accordance with Handbook 4350.4, Chapter 2-10.f.2 (MF Housing: Loan Administration: Responsibilities of Mortgage Servicing) and GNMA requirements where applicable.

➤ Regulatory Agreement – Timely filing of financial statements:

- Late filing of financials.
 - Potential red flag for operational or accounting issues.
 - Continual lateness may require action by Enforcement.
- Occasionally HUD will receive a request from a Borrower to provide a letter that there will be no Enforcement actions if financial statements are late.
 - Reminder - OHF cannot write letters dealing with Enforcement issues or actions.

➤ **Regulatory Agreement – Collateral Releases:**

§ 242.62 Releases of lien:

- The mortgagor shall not sell, dispose of, transfer, or permit to be encumbered any security property without the prior approval of the lender and Commissioner, subject to thresholds or such other standards as HUD may establish for the approval requirement.
- Where there is a partial release of lien, the lender must make a determination, subject to prior review and approval by HUD, that the remaining or replacement property subject to the first lien provides adequate security for the remaining principal indebtedness.

Note that year end audits may be a source of information with regards to property sales requiring HUD and Lender review “after the fact”.

➤ Regulatory Agreement – Collateral Releases (cont)

- If a Borrower is requesting a release of real property that serves as collateral for the HUD-insured loan:
 - Need the Lender's decision prior to HUD's letter being issued.
 - Unless otherwise approved by HUD, sales proceeds are to be placed in an escrow (new HUD escrow form forthcoming).
 - Unless otherwise approved by HUD, escrowed funds may only be used for improvements to collateral.
 - Draws from the escrow to be approved by both HUD and Lender.
 - OAE involvement required when necessary.

- **Regulatory Agreement – “Business Plan” section:**
 - Needs to be reviewed carefully, especially in light of COVID-19 impact and potential accounting restatements.
 - Note that Business Plan sections vary for specific borrowers and this section may not be found in the older Regulatory Agreements.
 - Typical key features:
 - Notes frequency of Board Review of financial statements.
 - Financial triggers that require Board Report to OHF and timelines
 - Describes steps, options and timing available to HUD to require a turnaround plan, etc.
 - Latest version of Reg Agreement (2017) requires that Borrower send information and reports to both HUD and the Lender.

➤ “Business Plan” section (continued):

- Report: When certain conditions exist, the Board is to submit a written “Report” to OHF on the steps being taken to improve the Borrower’s operations. Typical conditions include:
 - Operating loss equal to or greater than 1%
 - Net income less than zero
 - MRF not fully funded in accordance with schedule
 - These are typical examples – please review your Borrower’s Regulatory Agreement for the conditions.

➤ “Business Plan” section (continued):

■ Report

- There is no standard OHF template for the Board “Report”. This is a written Report from the Board which should include the information required by the Regulatory Agreement.
- The deadlines for submission of the Report are outlined in the Regulatory Agreement, typically 30 days after the Board review. If unable to meet the deadline, the Borrower needs to submit a request for an extension for no more than 30 days.

➤ “Business Plan” section (continued):

- If the Report deadline is missed or the Report is inadequate, the Regulatory Agreement describes steps, options and timing available to HUD to require a turnaround plan, etc.
- OHF and Lender to work closely together on addressing key issues to monitor the performance issues detailed in the Board’s report.

- **Turnover in Borrower Management or Board Members:**
 - Previous Participation (2530s)
 - If requested, HUD can provide a Regulatory Agreement review with Borrower, Lender and OHF.

➤ Mortgage Reserve Fund (MRF) Issues:

- HUD has limited discretion for MRF usage as defined in the MRF Agreements. Acceptable uses may include:
 - To prevent or cure default under the FHA-insured mortgage.
 - To pay for a management consultant to implement a turnaround plan to prevent a default with respect to the FHA-insured mortgage.
 - To apply for any other purposes that HUD may determine reduces its insurance liabilities as insurer of the mortgage.

➤ Mortgage Reserve Fund (MRF) Issues:

- Process: All distributions from the MRF are at HUD's discretion with HUD providing written direction to the Borrower and MRF Trustee (and Lender when necessary).
 - In the event of Bankruptcy, default or a claim, reference is made to the MRF Trust Agreement for next steps.
- If Borrower makes a request to use the MRF for debt service or for a consultant to prevent a default:
 - All MRF requests from the Borrower need to include a plan to replenish the MRF to the required minimum balance.
 - Requires a higher level of internal FHA review
- The MRF is not to be confused with an R4R in the 232 program.

➤ Other Issues:

- Attorneys for either Borrower or Lender
 - OHF must include an attorney from OGC on a call or in a meeting if there are other attorneys present.
 - If Borrower or Lender schedules a meeting with OHF and includes their attorneys, OGC (HHQ or Field Counsel) must also be included.
 - No exceptions.

Mortgagee Letter 2016-23

Mortgagee Letter 2016-23: Lender Responsibilities in Servicing Section 242 Loans

- <https://www.hud.gov/sites/documents/16-23ML.PDF>
- Checklist format of a summary of important servicing responsibilities of Lenders of Record holding Section 242 hospital loans.
- Covers Initial Endorsement, Construction Phase, Final Endorsement, Loan Servicing & Monitoring and Event-Driven Risk Management.

Initial Endorsement

- Each time a commitment is issued, Lender to:
 - Review documents
 - Coordinate with all parties to assist in fulfilling conditions for Initial Endorsement
 - Confirm DACAs are in place
 - Assist Borrower with preparing HUD 92403-OHF, Application for Insurance of Advance of Mortgage Proceeds

<https://www.hud.gov/sites/documents/92403.PDF>

Construction Phase - Lender Responsibilities

- Ongoing
 - Escrows & Deposits
 - Monitor insurance policies and surety bonds
 - Letters of Credit
 - Perform Lender Servicer Tasks as described in OHF Handbook
https://www.hud.gov/program_offices/administration/hudclips/handbooks/hsg/4615.1
- Hospital Requests Advance
 - Review for completeness and submit to HUD for approval
- Approved advance received from HUD
 - Obtain evidence that title is clear; arrange funding
 - Obtain title insurance endorsement increasing coverage to the total of all advances
 - Release approved funds to hospital

Construction Phase (cont.)

- Change Order, Line Item Change or Change of Scope Request
 - Determine if change is acceptable to hospital, architect and HUD
 - Verify source of payment for change and availability of funds for payment
 - Approve/disapprove the change and forward to OAE
- Request for Mortgage Increase
 - Review Request to determine if loan is in balance in accordance with BLA and if provision has been made for payment of any fees required.
 - Contact AE – will need HUD consent
- Monthly Requisition Meeting w/ OAE, Architect and CM
 - Attend, as needed, to review work progress
 - Always attend preconstruction conference and meetings at end of project to discuss close out procedures.

Construction Phase (cont.)

- Loan for new construction or Substantial Rehab
 - Monitor the disbursements of capitalized interest and advise OHF AE if failure to disburse capitalized interest will cause a default in a note payment.

- Each Final Endorsement
 - Assist in Cost Certification Process
 - Request Borrower to execute and deliver all required FHA documents and to fund all escrows and deposits required by FHA for final endorsement.
 - Coordinate with OHF to assist Borrower in fulfilling all conditions for final endorsement.

Permanent Loan Servicing – Administrative Functions

- Ongoing
 - Insurance
 - Escrow Analysis at least annually
 - Maintain current and complete mortgage loan files

- Monthly/Annually
 - Collect monthly mortgage payments
 - Prepare and distribute monthly mortgage loan statement and annual statement of account
 - Remit MIP payments

Permanent Loan Servicing – Periodic Monitoring

- Ongoing
 - Monitor Letters of Credit if any
 - Verify that the project has required Fidelity Bond Coverage.
 - ✓ Reference 242 Handbook 4615.1 REV-1 Appendix 7 for insurance requirements.
- Annually
 - Deposit Account Control Agreements (DACAs).
 - Confirm all UCC filings are continued every 5 years and all personalty for the HUD-insured loan is securitized for the life of mortgage.

Permanent Loan Servicing – Periodic Monitoring (cont)

- Quarterly/Annually (Monthly for Credit Watch/Priority Watch accounts)
 - Review annual audited financials, interim statements and actual-to-budget variance reports.
 - Identify signs/trends of financial weakening.
 - ✓ Discuss with OHF Account Executive.
 - ✓ Identify items for follow up in quarterly meetings with hospital CFO.
- Regulatory Agreement:
 - ✓ New Regulatory Agreement: Requires Borrower to provide financial information to both HUD and Lender.
 - ✓ Old Regulatory Agreements:
 - Borrower not required in all cases to share information with the Lender and HUD cannot forward/share information provided by the Borrower to outside parties, including the Lender.
 - Borrower must provide Lender with annual audited financial statements in accordance with Handbook 4350.4, Chapter 2-10.f.2 (MF Housing: Loan Administration: Responsibilities of Mortgage Servicing) and GNMA requirements where applicable.

Permanent Loan Servicing – Periodic Monitoring (cont)

- Quarterly (Monthly for Credit Watch/Priority Watch accounts and other identified accounts)
 - Set up periodic discussions with Borrower CFO to review financial performance.
 - Discussion should include the assigned OHF AE.
 - Identify and discuss changes in the Borrower's business plans and operations.
 - During pandemic, recommended reaching out to borrowers to review operations, cash flow and ability to service debt. If a borrower is facing challenges, reach out to the OHF AE.
- Persistent decline in financial performance
 - Discussions with OHF to consider whether the services of a turnaround consultant should be employed.

Event-Driven Risk Management

- Requests from Borrower: Lender is to review and submit recommendation to OHF AE for the following requests:
 - Modify the note and mortgage
 - Transfer of physical assets (TPA)
 - Partial release of liens
 - Permit secondary financing
- Lender requests a loan mod; refi under 223(a)(7) or 223(f); or supplemental loan under 241
 - Contact OHF AE and the 242 Underwriting Director to start HUD review process.
 - Provide an updated title policy to HUD as needed.

Event-Driven Risk Management (cont)

Lender Becomes Aware of:

- Delinquent mortgage payments
 - Notify OHF AE. Report through MDDR system as required.
 - Note – be sure to send a copy of the MDDR filing directly to the AE
 - Work with borrower and management to determine cause of delinquency.
 - Request a report from management describing how delinquency will be resolved.
 - Monitor mortgage payments and keep AE informed of status of loan and circumstances causing delinquency.
- Missed lease payment (for Borrowers with lease arrangements)
 - Notify AE and work with AE, borrower and operator to find out reason for missed payment
 - Request plan from management to avoid missed payments in the future

Event Driven Risk Management (cont)

Lender Becomes Aware of (cont):

- Vacating or condemnation of project
 - Notify HUD AE

- Notification of termination of any insurance
 - Work with AE and request management to provide an explanation of the termination and actions being taken to ensure that necessary is in place.
 - Reference to Handbook 4615.1 Rev-1 Appendix 7 for insurance requirements

- Default on an Accounts Receivable (AR) Loan
 - Work with AE, discuss with borrower why default occurred and request plan from borrower to deal with this event and prevent future defaults

Event-Driven Risk Management (cont)

Lender Becomes Aware of:

- Unauthorized Distribution
 - Request a plan from management to deal with event and to strengthen controls

- Borrower wants to add or amend an AR line of Credit
 - Borrower to send request to both Lender and OHF
 - Lender to review and render decision prior to OHF's decision.
 - HUD-92322-OHF- Intercreditor Agreement (ICA) for 242 program <https://www.hud.gov/sites/documents/92322-OHF.PDF>

Event Driven Risk Management (cont)

- Borrower stops making mortgage payments
 - Work closely with assigned OHF AE and HUD Turnaround Team
 - Request an action plan from the Borrower to return loan back to Performing status
 - Track progress of Action Plan
 - Report through MDDR system as required.
 - Note – be sure to send a copy of the MDDR filing directly to the AE.
- Lender Elects to Assign Mortgage to HUD
 - Continue to bill for and accept payments until mortgage is assigned in Secretary's name
 - Reference to Section 207.258 on the steps required of the Lender/Servicer for assignments.

Event Driven Risk Management (cont)

Lender Becomes Aware of (cont):

- Borrower files for Bankruptcy
 - File appropriate documents to assure that Lender's interest as first lienholder is protected and the security preserved.
 - Obtain an order recognizing Lender's entitlement to the revenues and restricting use of the revenues in accordance with the rules governing cash collateral.
 - Remind Borrower that project assets may not be used to pay attorney fees for legal services in connection with the bankruptcy without HUD approval.
 - Provide HUD with copies of any notice of default; noncompliance from regulatory authorities regarding the hospital's license, CON, or provider agreements.

Event Driven Risk Management (cont)

When Lender Becomes Aware of any of the Event- Driven risks:

- ✓ Notify the OHF Account Executive immediately.
- ✓ If not available, contact the OHF Director of Asset Management or Director of the HUD Turnaround Team.
- ✓ Communication is Critical!

Mortgagee Letter 2016-23

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Office of Hospital Facilities Lender Training

Virtual Training Session
September 22nd and 24th

HOSPITAL

Overview of the Construction, Limited Rehabilitation, and Critical Repair Processes

- **The “construction” process is different for**
 - 2-endorsement deals (typically 242 and 241 construction projects), where there is an Initial and a Final Endorsement
 - And 1-endorsement deals (223(f) and 223(a)(7))
- **The terminology is also different**
 - 242 and 241 allows for “Construction”
 - 223(f) allows for “Limited Rehabilitation”
 - 223(a)(7) allows for “Critical Repairs”

➤ Definitions §242.1

- *Construction* means the creation of a new or replacement hospital facility, the substantial rehabilitation of an existing facility, or the limited rehabilitation of an existing facility. The cost of acquiring new or replacement equipment may be included in the cost of construction.

➤ Definitions §242.1

- *Limited rehabilitation* means additions, expansion, remodeling, renovation, modernization, repair, and alteration of existing buildings, including acquisition of new or replacement equipment, in cases where the hard costs of construction and equipment are less than 20 percent of the mortgage amount.

➤ And for 223(a)(7) §242.91

- *Critical Repairs* – as determined by HUD, the improvements, upgrades or additions REQUIRED to be made to the property

We will cover:

- Initial Budgets
- Construction or Escrow Draw Requests
- Change Orders
- Line Item Transfers
- Project Closeout
- Cost Certification

Initial Budget Process:

- The HUD-92013-OHF
 - <https://www.hud.gov/sites/documents/92013-OHF.PDF>
- And for 223(f) Limited Rehabilitation:
 - Escrow Form HUD-92476A-OHF
 - <https://www.hud.gov/sites/documents/92476A-OHF.PDF>
- And for 223(a)(7) critical repairs
 - Escrow Form HUD-92476-OHF
 - <https://www.hud.gov/sites/documents/92476-OHF.PDF>

Initial Budget Process:

- Equipment list ([Handbook](#)) – applies to all commitment types
 - Applicants must submit an itemized list of major medical equipment broken out by broad categories. This list must be classified as follows:
 - Equipment to be purchased from mortgage proceeds
 - Equipment to be purchased with other funds
 - Leased equipment
 - For replacement hospitals, the net book value of property to be transferred to the new building(s), and plans for the existing site
 - For each category provide total cost by department
 - For the Application, consolidate the equipment list to broad categories and pieces of major equipment with costs in excess of \$700,000. A complete listing will still be required for closing and cost certification

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Construction Draws - (242 and 241)

➤ **See Handbook 4615.1 Rev-1, Appendix 8, Section 1-15**

➤ Draw Request package includes:

- AIA G702-Application and Certificate for Payment signed by the Architect and Contractor
- Form HUD-92448-OHF-Contractor's Requisition signed by the Contractor and Architect
- Form HUD-92403-OHF-Application for Insurance of Advance of Mortgage Proceeds signed by the Borrower and Lender, along with supporting documentation:
 - All detailed receipts and invoices to support the requested draw
 - All payment authorizations to support the requested draw
 - The above should be identified and in the same order as the cost categories on the 92403 and correlate with the line items in the final HUD-92013-OHF



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Construction Draws - (242 and 241)

- Mortgagor/Borrower submits two complete (currently electronic) draw packages to the Lender
- Lender performs a full review of the complete draw packages for adherence to the HUD approved project scope and HUD regulations and policies. This includes:
 - All receipts, invoices, and payment authorizations ensuring the amounts and line items on the HUD-92403-OHF are correct
 - Change orders and line item transfers
 - Remaining line item balances
 - Identification of the amounts to be drawn from the mortgage proceeds and mortgagor's equity/cash
 - Completion of the form HUD-92403-OHF
 - Request issuance of mortgage insurance of the requested amount, if applicable
- Lender submits the two completed packages to HUD OAE and OHF

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Construction Draws - (242 and 241)

- OAE performs a (currently virtual) site visit to verify the work contained in the draw request and completes a Site Visit Report for OHF
- NOTE: OAE reviews and verifies construction related items within requests and provides approval or disapproval on construction related items. This includes construction aspects related to certain equipment.
- OHF reviews the draw packages and site visit report from OAE and prepares a transmittal letter to the Lender identifying any adjustments and specifying the approved draw amounts.
- OHF Director issues the transmittal letter, along with copies of the 92403 and 92448
- Lender processes the disbursement of funds, mortgage insurance, and title policy date-down



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Limited Rehabilitation and Critical Repair Escrow Draws - (223(f) and 223(a)(7))

- The process is similar though the documents are different:
- Lender submits either **HUD-92476A-OHF for Limited Rehab** or **HUD-92476-OHF for Repairs**, along with the **HUD-92117-OHF Borrower's Certification of Full or Partial Completion of Project to OAE/OHF**
- Lender and OAE perform their respective reviews of the submission
- OAE performs a (currently virtual) site visit to verify the work contained in the draw request and completes a Site Visit Report for OHF
- OHF reviews the escrow draw packages and site visit report from OAE and prepares a transmittal letter to the Lender identifying any adjustments and specifying the approved draw amounts.
- OHF Director issues the transmittal letter, along with copies of either the **HUD-92476A-OHF for Limited Rehab** or **HUD-92476-OHF for Repairs**
- Lender processes the disbursement of funds

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Construction Change Orders - (242 and 241)

- Mortgagor/Borrower submits a written request to OAE and Lender stating the requested change, where funds will come from to support the change, and be on AIA change order forms or in a similar format. Requests need to be submitted separately from draw requests
- Lender reviews the request for adherence to HUD regulations, policies, and the sufficiency of the Owner's Contingency balance. Then provides written approval/disapproval to OAE
- OAE reviews the request and Lender decision and
 - If the amount of the change order is less than \$250,000, approves or disapproves the change order.
 - If the amount of the change order is greater than \$250,000, provides memorandum to OHF with recommendation and the amount of the change order
 - Note: Requests that have insufficient Owner's Contingency funds will not be approved
- Once approved, the Lender/Borrower can requisition for payment of change order work
- See Handbook 2615.1 Rev-1 Appendix 8



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Construction Change Orders - (223(f) and 223(a)(7))

- Most Limited Rehabilitation and Critical Repair projects will likely not have major change order requests. However, for larger projects, the process is similar to traditional two endorsement deals:
- Mortgagor/Borrower submits a written request to OAE and Lender stating the requested change, where funds will come from to support the change, and be on AIA change order forms or in a similar format. Requests need to be submitted separately from draw requests
- Lender reviews the request for adherence to HUD regulations, policies, and the sufficiency of the Owner's Contingency balance. Then provides written approval/disapproval to OAE
- OAE reviews the request and Lender decision and provides a memorandum to OHF regarding OAE decision and amount of change order. Requests that have insufficient Owner's Contingency funds will not be approved
- For change orders above \$250,000, and/or those requiring a Line Item Transfer, OHF also reviews the request and OAE recommendation and issues a letter to the Mortgagor/Borrower
- Once approved, the Lender/Borrower can requisition for payment of C.O. work



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Line Item Transfers- (242 and 241)

- Lender may request a transfer of funds from one line item on the approved HUD-92013-OHF to another when the category funds are coming from is complete or near completion
- Lender submits a written request to OAE and OHF clearly identifying:
 - The line item funds will be transferred from
 - The line item funds will be transferred to
 - The balances of the line items both before and after the transfer
 - The basis for the line item transfer
 - The overall resulting budget line items pre and post the requested adjustment
- OAE reviews the request related to the construction aspect of the project and provides a recommendation memorandum to OHF
- OHF reviews the request and issues a decision letter to the Lender
- NOTE: Change orders debiting Contingency funds, if approved, do not require a LIT request/approval



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Line Item Transfers- (223(f) and 223(a)(7))

- Single endorsement deals typically do not have Line Item Transfer requests, since the total mortgage amount is released at initial endorsement (and/or escrowed)
- However, major scope changes and budgetary changes, if needed, should be communicated via the escrow draw process and formally approved by OAE and OHF.
- More detail will be forthcoming in our next Handbook revision



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Project Closeout Process – 242 and 241 - OAE

- Conduct Final Inspection and prepare report.
- Review and recommend approval of retainage reduction/punch list completion.
- Review and recommend approval of final HUD loan endorsement
- Review Certificate of Actual Cost
 - HUD-92330-OHF (Borrower)
 - HUD-92330A-OHF (Contractor)
- Final Certificate of Occupancy.
- As Built ALTA Site Survey
- AIA Form G704-Certificate of Substantial Completion
- AIA Form G706-Certificate of Release of Liens
- AIA Form G707-Consent of Surety to Final Payment
- Architect's and Contractor's final Certificate for Payment
- Architect's letter asserting compliance with State Department of Health or Authority w/ Jurisdiction
- Certification all change orders have been included in the Final Certificate for Payment



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Project Closeout Process – 242 and 241 - OHF

- Review/Accept OAE recommendation for project closeout
- Review Certificates of Actual Cost
 - HUD-92330-OHF (Borrower)
 - HUD-92330A-OHF (Contractor)
- Review Final Equipment list
- Issue HUD-92580 Maximum Insurable Mortgage based on acceptability of submissions
- Work with OGC/Borrower/Lender to schedule closing



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Project Closeout Process – Differences for 223(f) and 223(a)(7)

- Depending on the size of the project, the documents to be submitted to OAE and OHF can vary.
- For single endorsement commitments where the amount attributed to Limited Rehabilitation or Critical Repairs exceed \$5,000,000, audited cost certification documents from at least the mortgagor will be required.
- Note, however, there is no potentiality of a mortgage size reduction as a result of the cost certification process.
- For projects under \$5M, submission of HUD-92117-OHF – Certification of Full or Partial Completion of Project (along with the Escrow draw requests) will suffice



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Cost Certification Process (242 and 241)

- Establishes the Maximum Insured Mortgage Amount
- Parties involved:
 - Mortgagor/Borrower
 - Lender
 - Independent auditor
 - Contractor
 - HUD's Office of Architecture and Engineering (OAE)
 - HUD's Office of Hospital Facilities (OHF)



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Cost Certification Process (242 and 241)

- **Mortgagor/Borrower Responsibilities:**
 - Establishes the Substantial Completion date with the Architect, Contractor, and OAE (HB 4470.2 REV-1, Ch 2)
 - Completes HUD Form 92330-OHF (HB 4470.2 REV-1, Ch 4)
 - Obtains Independent CPA audit opinion on final costs
 - Submits HUD Form 92330-OHF inclusive of CPA audit; Certificate of Occupancy/Completion; Final Equipment List; and any additional supporting documentation to OAE, OHF, and Lender

Cost Certification Process (242 and 241)

■ Contractor Responsibilities:

- Establishes the Substantial Completion date with the Architect, Contractor, and OAE (HB 4470.2 REV-1, Ch 2)
- Completes HUD Form 92330A-OHF (HB 4470.2 REV-1, Ch 5)
- Obtains Independent CPA audit opinion on final costs
- Submits HUD Form 92330A-OHF inclusive of CPA audit; any additional requested supporting documentation to OAE, OHF, and Lender

Cost Certification Process (242 and 241)

- **Independent Auditor Responsibilities:**
 - Certified Public Accountants (CPA), engaged by Contractor and Mortgagor respectively, prepares the HUD-92330A-OHF and HUD-92330-OHF, along with supplemental supporting documents and schedules, in accordance with professional standards of practice HUD Guidance
 - Provides OAE and OHF with an express opinion
 - See official HUD forms for guidance and references

Cost Certification Process (242 and 241)

- **Lender Responsibilities:**
 - Should facilitate / coordinate submission of the cost certification and project close out documents between parties
 - Review submissions for adhered to HUD regulations and policies
 - Monitor the project budgets and address discrepancies between budget and actual costs incurred

Cost Certification Process (242 and 241)

- HUD Office of Architecture and Engineering
 - Reviews the construction related aspects of the HUD-92330-A-OHF and HUD-92330-OHF and supporting documentation
 - Initiates OHF process by recommending project close out / movement to final endorsement

Cost Certification Process (242 and 241)

- **HUD Office of Hospital Facilities**
 - Reviews all Line Item Transfers and final project budgets to ensure consistency was maintained across the project timeline
 - Reviews all aspects (hard and soft costs) of the HUD-92330-A-OHF and HUD-92330-OHF and supporting documentation in order to establish a maximum insurable mortgage
 - Reviews equipment list for adherence to HUD guidelines
 - **Issues HUD-2580 Maximum Insurable Mortgage**
 - **Schedules Final Endorsement closing with Office of General Counsel, Lender, Borrower**

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Cost Certification Process Differences for 223(f) and 223(a)(7)

- No reduction in mortgage
- Attestation from CPA using HUD-92330-OHF from mortgagor only required for projects over \$5M*
- Attestation from CPA using HUD-92330-A-OHF from Contractor only required for contracts over \$5M*
- No maximum insurable mortgage issuance
- Savings or 'disallowed' costs could result in an escrow deposit
- Projects under \$5M are attested to via the Escrow Draw process and HUD-92117-OHF described previously

*unless identity of interest exists between parties



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Process Graphic for 223(f) & 223(a)(7)

Figure 1 - Insurance on Completion Process and Documents – 223(f) or 223(a)(7) Project with Rehabilitation or Repairs

