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February 26, 2020

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Addressing Quality of Care Issues in Application

As noted in the December 18, 2019 Email Blast ([here](https://www.hud.gov/sites/dfiles/Housing/documents/DecEmailBlast12182019.docx)), failure to analyze and address ongoing survey/quality of care issues was one of the areas in FY 2019 in which additional lender due diligence was needed on some transactions.  Quality of care should be thoroughly addressed in the Lender Narrative, a key component of which is the Risk Management Program section.

An analysis of a facility’s implementation of recently effective CMS requirements is highly relevant to addressing quality of care issues. In particular, the Quality Assurance and Performance Improvement (QAPI) plan requirement section of the *CMS Medicare and Medicaid Programs; Reform of Requirements for Long-Term Care Facilities* 10/4/2016 final rule ([here](https://www.federalregister.gov/documents/2016/10/04/2016-23503/medicare-and-medicaid-programs-reform-of-requirements-for-long-term-care-facilities)) became effective on November 29, 2019. This rule requires all Medicare and Medicaid funded LTC facilities to develop, implement, and maintain an effective comprehensive, data-driven QAPI program that focuses on systems and outcomes.  The final rule also includes requirements for Training, Compliance and Ethics, and Infection Control.

As noted in Handbook 4232.1, Section II, Chapter 8.8 ([here](https://www.hud.gov/sites/documents/42321S2C8HSGH.PDF)), “The Lender is responsible for reviewing the qualifications of the proposed Operator and/or Management Agent to assess their ability to operate the project effectively and in compliance with ORCF requirements.”  QAPI plans may impact staffing and staffing levels can heavily impact overall star ratings. When evaluating the operator’s capacity, Lenders should thus consider whether staffing levels, experience and roles are commensurate with the QAPI requirements and any needs identified in the QAPI plans.

(Quality of Care was also the subject of Email Blasts on 12/19/2018 [here](https://www.hud.gov/sites/dfiles/Housing/documents/DecEmailBlast12192018.docx) and 2/29/16 [here](https://www.hud.gov/sites/documents/FebEmailBlast022316.docx).)

***Keywords:*** *Quality of Care, Risk Management Programs*

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Guidance on Operating Lease Escalators

Lease payment escalators included in the operating leases with third-party operators are an important operational risk factor. As such, Lenders should analyze this risk as part of the Lease Payment Analysis for the applicable underwriting Lender Narrative. In that regard, Handbook 4232.1, Section II, Chapter 8.6 ([here](https://www.hud.gov/sites/documents/42321s2c8HSGH.pdf)) and excerpted below, outlines the basic ORCF Operating Lease Requirements, (as further detailed in forms HUD 91116-ORCF and 91116-ORCF). As the handbook emphasizes, the lease payments must be sufficient to “*(1) enable the Borrower to meet debt service and impound requirements and* (2) enable the Operator to properly maintain the project and cover operating expenses.”

When a facility’s performance is placing the facility at financial or other operational risk, notification and action plan requirements apply. Form HUD 93334-ORCF, Servicer’s Risk Notification to HUD of Risks to Healthcare Project and Action Plan for Remedy ([here](https://www.hud.gov/sites/dfiles/OCHCO/documents/93334_orcf.docx)) and form HUD 93335-ORCF, Operator’s Notification to HUD of Threats to Permits and Approvals ([here](https://www.hud.gov/sites/dfiles/OCHCO/documents/93335_orcf.docx)) outline requirements for addressing situations where the financial viability of the facility is at substantial and imminent risk.  Any consideration of bankruptcy or of efforts to renegotiate substantive lease terms trigger the formal notification and action plan requirements, and the servicing Lender in such instances should be timely in engaging the assigned Account Executive.

***Keywords:****Operating Leases**, Operator and Management Agent Analysis, Asset Management, Financial Operations, State Risk*

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Appraisal Reminders

ORCF Appraisers would like to remind Lenders of the following when submitting appraisals with their applications:

* Sales Comparables - every attempt should be made to find the most recent and similar sales comparables, typically within the same state.  ORCF Appraisal Guidelines require that the sales selected for the Sales Comparison Approach should be those that provide the most relevant and meaningful insight into the property’s value.  When the sales comparables are old, require substantial adjustments, or are not relevant to the appraisal analysis, additional data or explanations may be required and slow down the review process.
* Sales History – please fully analyze the subject's sales history. Failing to do this is a common deficiency. While not a requirement, ORCF considers it a best practice to include the Subject’s sale as a comparable within the Sales Comparison Approach.
* Initial Operating Deficit Escrow Calculation Template - please remember to use the most recent version of the Initial Operating Deficit Escrow Calculation Template (HUD-91128-ORCF), found ([here](https://www.hud.gov/sites/dfiles/OCHCO/documents/91128_orcf.xlsx)). Please do not convert the file into pdf, but submit it in its original Excel format as provided.
* Demand analyses for new construction applications of assisted living, memory care, and independent living - the monthly rents used in the target income calculations should be based on average monthly rents, not minimum rents. In addition, the anticipated care fees should be included in the monthly rent determinations for the target income calculations.
* Decision Circuit - when filling in the Revenue tab, and Historical Expense tab, the columns to the left of the appraisal’s projections (shaded blue) should be filled out with the same time periods that were used in the appraisal. Additional periods not included in the appraisal, such as updated financial periods, should be entered in the “Optional Reporting Periods” columns to the right of the Lender’s Debt Service Coverage projections (shaded yellow).
* Certified Financials - the application needs to include certified financials that match those supplied to the appraiser. Without them, the review appraiser cannot reconcile the history shown in the appraisal to the certified financials. This does not mean that certified financials will not also be required for updated financials that occur after the appraisal.

***Keywords:*** *Appraisals*

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Section 106 Historic Preservation Reviews

Lenders and third-party consultants are reminded of the importance of submitting complete information to the State Historic Preservation Officer (SHPO) for use in the Section 106 consultation. In particular, please ensure that you are specific about the scope of work that is being completed as part of the FHA-insured project, and include a map, photos, and project plans as applicable (Please see Handbook 4232.1, Section II, Chapter 7.E.5).  Please check the SHPO’s website prior to submitting a request for consultation as some states have their own process and submission requirements. While SHPOs have 30 days to review a submission, the submission must be complete and correct or the SHPO may require additional information which can add to the review time.

***Keywords:*** *Section 106, Historic Preservation, SHPO, Application Processing*

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New Environmental Rule Conforming the Acceptable Separation Distance (ASD) Standards for Propane Tanks to Industry Standards

On January 24th, 2020, HUD published a final rule revising 24 CFR Part 51 Subpart C to exempt liquefied petroleum gas or propane (LPG/propane) containers up to 1,000 gallons that comply with industry standard, National Fire Protection Association (NFPA) Code 58 (Liquefied Petroleum Gas Code) (2017).  This final rule is effective on February 24th, 2020 and is available ([here](https://www.govinfo.gov/content/pkg/FR-2020-01-24/pdf/2020-00440.pdf)).  ORCF environmental reviews will incorporate the new standards in the evaluation process for propane aboveground storage tanks (ASTs).

Mortgage insurance applications for projects involving propane ASTs that qualify for the exemption should include evidence of compliance with NFPA 58 in *Section 2: Third-Party Reports*.  Documentation of compliance with NFPA 58, including the NFPA separation distance requirements noted below, will satisfy the Handbook requirements for fire safety conformance letters and ASD calculations.

Copied below is the revision in 24 CFR Part 51.201 which removes propane ASTs from the ASD requirements if they comply with NFPA Code 58 and do not exceed 1,000 gallons water capacity.

“**§ 51.201 Definitions.**

\* \* \* \* \*

*Hazard*—means any stationary container which stores, handles, or processes hazardous substances of an explosive or fire prone nature. The term ‘‘hazard’’ does not include: ….

(5) Containers used to hold liquefied petroleum gas with a volumetric capacity not to exceed 1,000 gallons water capacity, if they comply with National Fire Protection Association (NFPA) 58.”

As stated in the rule’s Supplementary Information, “this rule does not remove all safe distance requirements for LPG containers sited near HUD assisted projects. All tanks exempted from HUD’s ASD requirements under this rule must be fully compliant with NFPA (2017) standards, including NFPA separation distance requirements. Tanks locations must meet a separation distance between the container and important buildings … or line of adjoining property that can be built upon, in accordance with the NFPA 58. Tanks between 125 and 500 gallons must be at least 10 feet apart from important buildings or property lines of adjoining property that can be built upon, while tanks between 501 and 1,000 gallons must be at least 25 feet apart. Under NFPA 58 and this rule’s revision of 24 CFR part 51, tanks under 125 gallons would not require a separation distance”.

HUD’s Office of Environment and Energy has issued Fact Sheet #H1, *Hazardous Operations* ***–*** *FR-6054-F-02 Conforming the* *Acceptable Separation Distance (ASD) Standards for Residential Propane Tanks to Industry Standards*, which is available on HUD Exchange ([here](https://www.hudexchange.info/programs/environmental-review/explosive-and-flammable-facilities/)).

***Keywords:*** *Environmental,* *Propane, NFPA, ASD*

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Submitting Environmental Reviews to ORCF in HEROS

Environmental reviews that are prepared by third-party consultants in the HUD Environmental Review Online System (HEROS) may now be voluntarily submitted to ORCF for Section 232 mortgage insurance applications. ORCF will use HEROS submissions for assistance with processing of its environmental reviews; however, ORCF remains responsible for independently evaluating the information supplied in HEROS, supplementing that information as needed, and making the required environmental findings.

The HEROS review should be assigned to ORCF at the time of, or shortly before, the application’s submission to HUD. In addition, HEROS reviews that have been prepared for applications that are currently in the ORCF processing queue may be submitted at this time.

Upon approval by the Lender, the consultant should submit the HEROS review to ORCF by using the “Assign Review” feature and then selecting Wayne Harris as the assignee. ***Please do not contact Wayne Harris regarding HEROS; his name is only used to store the HEROS submissions until an environmental reviewer is assigned to the project.*** Questions regarding HEROS should be submitted to LeanThinking@hud.gov.

Consultants should enter the name of the facility and the FHA Project Number in the “Project Name” field on the Initial Screen (1105) in HEROS. For example, 111-22999-ABC Project. Providing the FHA number with the project’s name allows ORCF to quickly identify the subject of the HEROS review.

A download of the HEROS environmental review record (ERR) should be included in the mortgage insurance application in *Section 2: Third-Party Reports*. The HEROS exhibit should be named “Other-**HEROS ERR**” to identify its content. Please note that a HEROS submission does not replace or eliminate any application exhibits. All applicable environmental exhibits will continue to be submitted with the mortgage insurance application in accordance with the current practice.

Guidance for ORCF stakeholders using HEROS is available online at ORCF’s Environmental Resource website ([here](https://www.hud.gov/federal_housing_administration/healthcare_facilities/residential_care/environmental_resources)).

Lenders and stakeholders are also encouraged to access the ORCF Lender's Environmental Checklist ([here](https://www.hud.gov/sites/documents/223f_EnvChecklist.xlsx)) for additional environmental guidance.

***Keywords:*** *Environmental, HEROS*

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LEAN Thinking Communication With Loan Applications

Lenders are encouraged to include any Lean Thinking responses within their applications for FHA Mortgage Insurance. The LeanThinking@hud.gov mail box is available for pre-submission questions that are specific to a project, and/or general questions which have may have applicability to a project that is being contemplated for submission. In the event that a LeanThinking inquiry results in guidance under one of these scenarios, Lenders are asked to submit a complete record of the inquiry/response within the Communication folder of their applications. This includes any request(s) for early Environmental Consultation. Inclusion of this information within the application will help ORCF streamline processing and may save considerable time by avoiding duplicative efforts.

Although Lenders should include the Lean Thinking email exchange for ready reference, we do note that, as stated at the bottom of each Lean Thinking response:

A Lean Thinking response is based on the limited and preliminary information submitted by the inquirer specific to a particular matter.  The response is thus limited to that particular matter and/or transaction and *is itself preliminary*.  A Lean Thinking response shall not be construed as an approval of a submission; all submissions must meet ORCF underwriting criteria, and approval of the topic discussed above is only a portion of the overall review process that must be approved.  Lean Thinking cannot be used in lieu of prescribed waiver or exception procedures, and any firm application accompanied by a Lean Thinking response will always be subject to underwriting and final approval.

***Keywords:*** *Lean Thinking, Environmental, Application Processing*

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FHA Number Requests

Please note that the 232FHARequest@hud.gov email box is no longer being monitored and emails submitted to this mailbox will not receive a response.  All FHA Number Requests should be submitted through the HUD 232 Healthcare Portal ([here](https://www.hud232portal.com/)) for processing.

If you are having issues submitting your FHA Number Request or Application, please submit a Help Desk Ticket ([here](http://www.hud232portal.com)) for assistance.

If you are following up on the status of an FHA Number Request, please contact LeanThinking rather than reaching out to individual ORCF staff. LeanThinking will route the inquiries to the appropriate ORCF staff members and coordinate the response.  Please note that Lenders are encouraged to request FHA Numbers early in the application preparation process to accommodate application submission timing deadlines, as periods of high volume or processing of Help Desk Tickets can require additional time for processing.

***Keywords:*** *Application Processing*

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Reminder - CMS Provider Number

Please ensure that the CMS Provider Number is entered correctly on the contact sheet in the application (e.g. Exhibit 1-6 for a 223F application). ORCF has seen a number of submissions with the incorrect number entered. Please note, the CMS Provider Number is always six digits and that some begin with a zero (if you have a five-digit number, the zero may be missing). Providing the correct CMS Provider Number will avoid delays in processing your application.

***Keywords:*** *Application Processing*

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ORCF Asset Management Risk Monitoring Routine

As part of our continuous effort to enhance and standardize the notification and mitigation of circumstances that could impair the value of the FHA-insured security in Section 232 facilities, ORCF Asset Management will be implementing a standard risk monitoring routine in the coming months, consistent with existing Borrower/Operator requirements and Lender servicing requirements.

As a reminder, all Operators are required by 24 CFR Section 232.1015 to provide to HUD and the Lender/Servicer prompt notification of circumstances placing the value of the FHA-insured security at risk. Although this provision applies to Operators of any Section 232 facility (regardless of the of the version of the Regulatory Agreement the Operator has executed), the requirement is further set forth in the Borrower Regulatory Agreement (92466-ORCF). Handbook 4232.1, Section III, Asset Management, Chapter 3.10 further prescribes that a Project is required to notify both HUD and the Lender when there are threats to the Project’s permits and approvals.

Effective October 3, 2019, Lender/Servicers, Borrowers, and Operators are required to use the Operator’s and/or Borrower’s Notification to HUD of Threats to Permits and Approval (HUD-93335-ORCF), ([here](https://www.hud.gov/sites/dfiles/Housing/documents/93335N_orcf.docx)), and The Servicer’s Notification to HUD of Risks to Healthcare Projects and Action Plan for Remedy (HUD-93334-ORCF) ([here](https://www.hud.gov/sites/dfiles/Housing/documents/93334N_orcf.docx)) when notifying relevant parties of risks to the FHA-insured security and for communicating action plans for remedy. Consistent with these publications, issues requiring action plans include, but are not limited to:

* Delinquent or defaulted mortgage payments
* A debt service coverage ratio below 1.0
* Special Focus Facility (SFF) designation
* Licensed Nursing Facility survey findings higher than a “G” level citation
* REAC inspections (single score below 30 or consecutive scores below 60)
* Missing Financial Reports

The information required by ORCF when risks to the FHA-insured security are present can be found in Handbook 4232.1, Section III, Chapter 3.10 and Chapter 4.4, and the information is further delineated in HUD-93334-ORCF ([here](https://www.hud.gov/sites/dfiles/Housing/documents/93334N_orcf.docx)). As detailed therein, ORCF requires the establishment of a corrective action plan for improving deficiencies and remedying the identified risk condition(s).  Consistent with HUD-93334-ORCF, ORCF expects that servicing Lenders will work with their clients to ensure the following are addressed:

* A description of the risk and discussion of its effect on the Project.
* An analysis of the root cause of the financial risk factor(s) (i.e., is a low DSCR due to low census, labor market, staff turnover, and/or unexpected expenses, etc.?).
* A description of the action plan to be implemented (e.g., marketing plan, expense management plan, risk management plan, etc.) and the identified goals and areas in need of improvement.  The Lender should be sure that the plan and the goals align with the root cause analysis.  For example:
	+ An action plan implementing cost saving measures would be included for a Project with increasing operating expenses.
	+ An action plan implementing a marketing plan to expand Medicare referral sources would be expected for a Project with declining revenues, declining resident days, and declining average daily rate (ADR).
* Each identified goal/step of the action plan is measurable (e.g., increase census by 10%).
* Each goal has a timeline (target completion date).
* The action plan includes a set time when the Borrower or Operator will follow-up with the Lender and provide a status report.
* Monitor and inform HUD on a recurring basis (monthly, quarterly, as determined by the timelines/target completion dates) whether the plan is on schedule or not, and if not, have the Operator/Borrower reevaluate and provide amended action steps, target completion dates, as appropriate.

In the coming months, ORCF Asset Management will communicate with stakeholders about improved processes to better position Lenders and their clients to timely meet the expectations summarized above.

***Keywords:*** *Risk Notification, Documents*

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Revised Asset Management Checklists Pursuant to Healthcare Portal Updates

As a follow up to the Asset Management Healthcare Portal Training sessions held during the week of February 10, 2020, all checklists for Asset Management transactions have been revised to reflect the naming conventions to be utilized for submissions to the Healthcare Portal.  Each of the revised checklists contains instructional information regarding use of the numerical code identifiers (**highlighted in green**)for each of the exhibits in the checklist.  These highlighted numbers are important codes that “guide” the Portal system to recognize the type of transaction submitted, section number of the checklist, and the identity of the document.  **Failure to use the updated Asset Management checklists and their corresponding naming conventions will cause the Healthcare Portal to reject the submitted transactional document and may subsequently result in a rejection of the entire transaction submission.**

***Keywords:*** *Asset Management Checklist, 232 Healthcare Portal*

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FROM THE CLOSING CORNER

Last Minute Issues Prior to Closing – Procedures for Newly Discovered Litigation

As a reminder, as stated in the August 28, 2013, February 27, 2014, and December 21, 2016 Email Blasts, to help to avoid delays in closing Section 232 projects, ORCF is restating procedures for newly discovered litigation.

ORCF no longer collects litigation searches (except where required by the Attorney’s Opinion as an Exhibit).  Please note that the Attorney’s Opinion form requires the attorney signing it to opine that, to such attorney’s knowledge, based on the Docket Searches and the Attorney’s Opinion Certification, there is no litigation or other claim pending before any court or administrative or other governmental body against the Borrower or General Partner/Managing Member, Operator or the Project except as has been disclosed in Exhibit F to the Opinion.

**Please keep in mind the following timeframes:**

1. **Searches:**  Searches should be run and analyzed by the Lender ***no earlier than 30 days before closing and no later than 10 business days before closing***.
2. ***Newly Discovered Litigation?******No later than 5 business days prior to the scheduled closing***, Lenders must disclose to HUD any newly discovered litigation (“newly” meaning not previously disclosed to ORCF in the application process), the Lender must also address the following:
3. Name and discussion of each newly discovered lawsuit, including estimated potential liability;
4. Whether each newly discovered lawsuit is of the type covered by insurance or whether the lawsuit is for a claim not covered by insurance;
5. The amount of liability insurance available to cover each newly discovered lawsuit and other pending claims and judgments and the estimated potential liability for such other lawsuits/judgments; and
6. Identify who bears the cost of defense of each newly discovered lawsuit and whether the insurance company is participating in the defense.
7. ***An opinion from the Lender’s Underwriter that the litigation is mitigated (e.g. covered by insurance) and will have no material impact on the project or underwriting.***

Any issues will need to be cleared by ORCF and HUD’s Office of General Counsel prior to closing. Prompt disclosure to HUD of newly discovered litigation will minimize the risks of delays in closing.

***Keywords:*** *Litigation/Docket Searches, Closings*

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Reminder for Section 232 New Construction Contracts

Please remember that ORCF’s policy for Retainage Reduction Riders attached to executed HUD Construction Contracts must be in accordance with Healthcare’s policy found in Handbook 4232.1, Section II, Chapter 10.15.D. This section, which reads, in part:

*“…the existing standard of 10% retainage will be required only until* ***90%*** *completion. After 90% completion, the requirement will be 5% retainage until* ***100%*** *completion and 2.5% retainage until the loan reaches Final Closing.”*

Please note that this is different than current HUD Office of Multifamily Housing Programs policy. Multifamily Housing Riders will not be accepted.

***Keywords:*** *Retainage Reduction Rider*

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Past Lean 232 Updates are [available online](http://portal.hud.gov/hudportal/HUD?src=/federal_housing_administration/healthcare_facilities/residential_care/mail_blast_index).

Have questions about the Lean 232 Program? Please contact LeanThinking@hud.gov.

For more information on the Lean 232 Program, check out: <http://www.hud.gov/healthcare>.

Have your loan servicing colleagues joined our email list? The Email Blasts contain information relevant to them as well. You might suggest they [Join here](http://portal.hud.gov/hudportal/HUD?src=/subscribe/signup&listname=Lean%20232%20Updates&list=LEAN-232-UPDATES-L).

We hope that you will want to continue receiving information from HUD. We safeguard our lists and do not rent, sell, or permit the use of our lists by others, at any time, for any reason. If you wish to be taken off this mail list, please [go here](http://portal.hud.gov/hudportal/HUD?src=/subscribe/signup&listname=Lean%20232%20Updates&list=LEAN-232-UPDATES-L).

*Lean 232* is a publication of the Federal Housing Administration (FHA) Office of Healthcare Programs, U.S. Department of Housing and Urban Development, 451 7th Street, SE, Washington, DC 20410.

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