

# Guidance on Faircloth to RAD Conversions

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## Introduction

This guidance document is written for public housing authorities (PHAs) who have expressed interest in the following:

- Using the Office of Public Housing Investments (OPHI) Mixed-Finance<sup>1</sup> program to develop new public housing units from their available [Faircloth Authority](#); **and**
- Converting the assistance from public housing to Section 8 through the Rental Assistance Demonstration (RAD) program once the units have been entered into the PIH Information Center (PIC) after construction completion.

This conversion type is referred to as a “Faircloth to RAD” conversion. There are three phases in the process of developing and converting these units: (1) Pre-Development; (2) Construction; and (3) Conversion to Permanent Financing.

Exhibit A presents the key steps in the Faircloth to RAD conversion process. The annotations, depicted by a numbered box to the left of this guide, reference the key steps depicted in Exhibit A of this guide.

This guide is specific to Mixed-Finance Development under 24 CFR 905.604. Additional guidance on how to approach Faircloth to RAD conversions that opt to use conventional development, turnkey development, acquisition, or force account labor (see 24 CFR 905.600(b)) is forthcoming.

## Process Description

### 1. Pre-Development

**1** The Faircloth to RAD conversion process begins with the PHA’s request for the Notice of Anticipated RAD Rents (NARR), thereby communicating its interest in developing and converting units from its available Faircloth authority to the Office of Recapitalization (Recap). This inquiry is made through the RAD Resource Desk ([www.radresource.net](http://www.radresource.net)) by selecting the “Faircloth Conversion” option and providing HUD with specific information, requested in the RAD Resource Desk, needed to calculate what the RAD rents for the project will be at the time of conversion. Please note that if the specific project characteristics used to calculate the RAD rents change by or before the PHA submits its Mixed-Finance Development Proposal (MFDP)<sup>2</sup>, the PHA will need to provide updated information for HUD to calculate revised rents.

In addition to requesting the NARR, the PHA must reserve conversion authority under RAD so that when the project is issued a Date of Funding Availability (DOFA) the PHA can be assured that there is availability under the statutory cap of public housing units that can be converted under RAD (currently set at 455,000 units). Conversion authority can be reserved for the units being developed through one of the following three options:

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<sup>1,2</sup> Please refer to [https://www.hud.gov/program\\_offices/public\\_indian\\_housing/programs/ph/hope6/mfph](https://www.hud.gov/program_offices/public_indian_housing/programs/ph/hope6/mfph) for information on the Mixed-Finance program and to access MFDP template.

- **Option 1:** If the PHA has as an existing RAD Portfolio Award, then the PHA should select the option, in the RAD Resource Desk, to add the units to its portfolio award to cover the RAD conversion of the planned projects containing the Development Units.
- **Option 2:** If the PHA does not have a RAD Portfolio Award, then a PHA can secure conversion authority by submitting a RAD Portfolio Application<sup>3</sup>, as outlined in Section 1.9.C of the RAD Notice.
- **Option 3:** A PHA that does not meet the criteria in Section 1.9.C for a Portfolio Award (“PHA A”) because it has no other public housing properties may partner with another PHA (“PHA B”) who has an existing Portfolio Award. PHA A would submit a request to the RAD Resource Desk to update PHA B’s Portfolio Award to include the PHA A’s Development Units, thereby reserving authority under the RAD unit cap for PHA A. PHA B should note for HUD that a specified number of units are reserved on behalf of PHA A. The units will be removed from PHA B’s Portfolio Award when a CHAP is issued to PHA A.

2 Once HUD has calculated the RAD rents and conversion authority is secured, HUD will issue a NARR, which contains the estimated RAD rents. The RAD rents stated in the NARR can be used by the PHA to underwrite the project and should be reflected in the PHA’s MFDP that is submitted to OPHI. Please note that, as with all RAD conversions, a PHA has certain flexibilities under Section 1.6.B.5 and 1.7.A.5 to make modifications to the rents, including through rent bundling and using MTW flexibility.

3 When the PHA is close to submitting their MFDP, the PHA should request a preliminary conversion call through the RAD Resource Desk. Upon receiving this request, the assigned Transaction Manager (TM) from Recap will then schedule a call with the PHA and other relevant stakeholders, including OPHI. The preliminary conversion call will discuss the following agenda items:

- The Faircloth to RAD conversion process
- The construction delivery and occupancy plans, specifically whether all units will be completed at once or whether units will be delivered for occupancy over time (e.g., on a building-by-building basis)
- Permanent financing terms and the timing of the RAD conversion relative to construction completion and the take-out of the construction loan by permanent financing
- Housing Assistance Payments (HAP) contract funding during the first year after completion of construction

4 To expedite processing, Recap has established streamlined requirements for Faircloth to RAD conversions. Essentially, a PHA will update the Resource Desk with only the RAD Financing Plan documents that are not covered within the MFDP, consisting of the following:

1. The Conversion Overview, including a description of the proposed RAD ownership structure
2. Selection of Program Platform: Project Based Vouchers or Project Based Rental Assistance
3. Certification of Board Approval of the RAD Conversion
4. Operating Pro Forma

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<sup>3</sup> This application can be accessed on the Resource Desk by selecting the “Apply” icon and then clicking on the “RAD Portfolio Application” hyperlink which will download an Excel spreadsheet that must be completed by the PHA.

5. Approved Significant Amendment to PHA Plan and, if applicable, the Approval of the MTW Agreement
6. Initial Year Funding Tool

Because OPHI is underwriting the development of the project as public housing and because the conversion of assistance under RAD will not occur until the project has been constructed, HUD will underwrite the RAD conversion as a no-debt conversion without any construction. Therefore, all development activity should be reflected in the MFDP's discussion of sources and uses of funds, even if the expenditures may occur after the date of the RAD conversion. The Transaction Log is not required at this time because Recap expects that all costs known at this stage of the process will be reflected in the Mixed Finance Development Proposal and the RAD "Sources and Uses" of funds would not have any transaction costs.

5 If OPHI approves the PHA's MFDP, Recap will, in conjunction with the Mixed-Finance Approval Letter, issue a RAD Conversion Conditional Approval (RCCA), along with a draft RAD Conversion Commitment (RCC). The draft RCC will stipulate the conditions upon which the PHA is receiving conditional approval and outline the steps that need to be completed for the PHA to effectively convert through RAD. Upon receipt OPHI's Mixed-Finance Approval, the PHA will proceed towards closing the transaction (construction financing closing) under the standard Mixed-Finance development processes. No additional RAD steps, or Recap approvals, are required between issuance of the RCCA and construction closing.

The Mixed-Finance construction closing process includes, but is not limited, to the preparation of the following "evidentiary" documents:

- Regulatory & Operating Agreement (R&O),
- Declaration of Restrictive Covenants (DORC),
- Mixed-Finance Annual Contributions Contract (ACC) Amendment, and
- Admissions & Continued Occupancy Plan (ACOP).

During the Mixed-Finance construction closing process, the PHA also submits to HUD, as applicable, the first mortgage and subordinate mortgage loan documents, the ownership entity partnership agreement/operating agreement, the ground lease, construction documents, and all other documents for the real estate development transaction. The bulleted documents listed above are unique to public housing and will be terminated/moot at the time of the RAD conversion (see templates referenced in Section 3 of this document). As a result, these documents are expected to be effective for only a short time. Therefore, the PHA should draft and negotiate these documents with that limited lifespan in mind. The PHA should also inform the HUD OGC team that the transaction will be converting to RAD once the units are entered into PIC so that the legal documents prepared at the time of the Mixed-Finance construction closing are reviewed with RAD in mind.

## 2. Construction

9 Once the Mixed-Finance transaction is closed, the PHA can begin construction. As the units near construction completion, the PHA should prepare to submit to PIH the documents that onboard the units as public housing under standard Mixed-Finance development processes. The Development Units

must be developed, fit for occupancy, and included within the public housing program pursuant to the requirements of 24 C.F.R. Part 905 Subpart F. When the public housing Field Office verifies the DOFA eligibility, the Field Office will enter the units into PIC, officially classifying them as public housing.

8

The PHA is also responsible for notifying Recap as construction of the units are nearing construction completion. The timing to approach Recap is at the PHA's discretion, but 60 days before the DOFA is strongly encouraged if the PHA wants to minimize the time that it will operate the units under public housing requirements. At this stage in the process, as described in the RCCA, the PHA must upload/update the following on the RAD Resource Desk:

- Construction Completion Update – contains the PHA's certification that the completed project is consistent with the terms specified in the RCCA. The PHA should include any work to be done after the date of the RAD conversion which was not reflected in the MFDP or subsequent OPHI approvals. The PHA should also inform Recap of any financing liens to be created post-RAD conversion so that they may be reviewed, approved, and identified as HUD-approved liens in the Additional Provisions exhibit of the RCC. PHAs may not place additional liens on a RAD converted property without HUD approval and this pre-approval will ensure a smooth subsequent closing of the lien.
- Attachments to the Construction Completion Update – explains and documents material changes from the transaction structure as previously approved by Recap, if necessary.
- Resource Desk Transaction Log – The Transaction Log will be pre-populated to reflect \$0 Sources and \$0 Uses as all costs identified at the time of the Mixed Finance Development Approval will be reflected in the Mixed Finance sources and uses. With the Construction Completion Update, provide updates to the Transaction Log to include to any changes to the sources and uses that are not reflected in prior OPHI approvals, if necessary.

Once the documents and updates identified above, as applicable, are submitted to Recap, Recap will review to confirm that the transaction remains consistent with RAD requirements. Recap will then assign a Closing Coordinator and OGC will assign counsel to bring the RAD conversion to completion. The PHA may begin uploading the RAD closing documents to the RAD Resource Desk. The list of necessary closing documents is available on the RAD Resource Desk. As noted above, many of these documents can be negotiated at the time of the construction closing if the PHA chooses. Uploading documents at this time is strongly encouraged as it will permit the Recap and OGC team to begin reviewing the closing documents to prepare for RAD closing. This will minimize the time operating under public housing requirements and the time it takes to complete the RAD closing.

### 3. Conversion to Permanent Financing

Once the PHA has notified Recap that construction is nearing completion and Recap has approved the Construction Completion Update and other documents, as applicable, Recap will coordinate with PIH to track when the units are established as public housing by being entered into PIC. Once the units are in PIC, Recap will issue the Commitment to Enter into a Housing Assistance Payments Contract (CHAP) and RCC simultaneously, as the Financing Plan was previously reviewed and approved during the Pre-Development period, described in Section 1. The RAD conversion can then proceed to final RAD closing reviews.

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### 3.1 RAD Closing

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The RAD closing process for Faircloth to RAD conversions is the same as all other RAD conversions. The closing process generally takes approximately 60 days, which can begin when the PHA uploads a complete package of closing documents. The PHA may upload the closing documents before the units are in PIC (as noted above) or after issuance of the RCC. RAD Closing can only occur after HUD approves all documents. The PHA team should familiarize themselves, prior to CHAP issuance, with the following guidance documents available on the Resource Desk:

- [Overview of the RAD Closing Process for PHAs](#)
- RAD Closing Checklist & Overview – [PBRA](#)<sup>4</sup>/[PBV](#)

Additionally, also available on the Resource Desk, the following three templates relevant for projects developed through the Mixed Finance program are applicable for Closing of Faircloth to RAD conversions:

13

1. [Mixed Finance – Release from Declaration of Restrictive Covenants](#)
2. [Mixed Finance – Termination of ACC](#)
3. [Mixed Finance – Termination of Regulatory & Operating Agreement](#)

### 3.2 Funding in the Conversion Year

For the remainder of the first Calendar Year in which a HAP Contract is effective (the “year of conversion”), Operating Funds and Capital Funds will be obligated to the PHA for the Covered Project at the level of public housing subsidy which that project is eligible to receive regardless of the initial contract rent amount (stated in the NARR) or Operating Cost Adjustment Factor. These are the funds that the project will rely on for the balance of the calendar year. New public housing projects are funded in the following way:

- 1) PHAs must follow Operating Fund processing guidance<sup>5</sup> to initiate funding for new projects. Please note that each year the Operating Fund establishes a new project submission deadline, typically in the early summer of each year. Projects that meet DOFA after this date and/or that fail to provide the Operating Fund submissions by this date will not receive Operating Funds in the year of conversion.
- 2) The public housing Capital Fund provides funding to PHAs each year based on public housing units in PIC on the Capital Fund certification date in the prior calendar year. As such, PHAs do not receive funding for new projects in the year that they come on-line in PIC.

To calculate funding in the year of conversion, all RAD conversions require the PHA to submit the [Initial Year Funding Tool](#) as part of the Financing Plan to ensure that all parties understand funding available. This tool is also submitted in final form at RAD Closing. It is the Initial Year Funding Tool that establishes the subsidy that the PHA will receive in the year of conversion and not the terms set forth in the R&O. As such, developers and PHAs should take this and Capital fund timing considerations into account when considering the planned construction of the project and in creating their budget. For example, the

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<sup>4</sup> For PBRA conversions, HUD Asset Management requires that the property and owner information is entered into APPS and that the Management Certification is completed. Please refer to the Resource Desk “Submitting the Financing Plan” section of the Document Library to access ‘2530 Guidance for RAD Transactions’ and ‘2530 MF Development Compliance and Credit Requirements’ for more information.

<sup>5</sup> See <https://www.hud.gov/sites/dfiles/PIH/documents/pih2021-04.pdf> for Calendar Year 2021 guidance

development team may wish to consider establishing a year-of-conversion reserve to supplement the public housing funding and provide the project with the normal RAD rent revenue, particularly if the permanent loan conversion requires stabilized occupancy for a period of time that would be impacted by the lack of capital funds in the year of conversion. On January 1 following the HAP effective date, HAP based on the RAD rents will begin.

Any permanent loan conversion could occur before, simultaneous with, or after the RAD conversion. Any lenders will need to subordinate their loans to the RAD Use Agreement, and OGC will need to review the draft subordination agreement(s), associated with the loans, that would be signed at closing.

### 3.3 Resident Considerations if Units are Leased as Public Housing

Once the units are in PIC, the PHA can choose whether to begin leasing the units as public housing under public housing rules or to wait and lease only after RAD conversion, when the units are under the Section 8 program. If the units are delivered for occupancy over time (e.g., on a building-by-building basis) and have multiple DOFA dates, the RAD conversion can only occur after all units exist as public housing.

If units are leased as public housing, the PHA must consider the resident engagement requirements under the RAD Notice that are applicable given when the residents begin occupancy relative to where the transaction is in the RAD conversion process. The PHA must take the following additional steps:

- On move-in, inform the residents in writing of the pending RAD conversion through issuance of the [RAD Information Notice](#) (RIN), which may be modified to fit the circumstances.
- If units are built on a building-by-building basis, the CHAP and RCC are not issued until the last building has established a DOFA date in PIC. As mentioned above, the PHA has the option to begin leasing as public housing as the units come on-line in the PIC system or wait till after the RAD conversion. In this scenario, where residents are moving in prior to issuance of the RCC, the PHA must conduct all resident engagement activities required during the period between submission of the Financing Plan and issuance of the RCC.<sup>6</sup>
- If residents move in after issuance of the RCC but before the RAD conversion, conduct all resident engagement activities required following issuance of the RCC.
- Include documentation of the Resident Meetings and Comments in the Conversion Overview or in the RAD Closing document submission.
- Enter into new Section 8 leases with the tenants prior to RAD Closing or activate the transition from public housing to Section 8 leases if the tenants signed lease forms contemplating the transition.

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<sup>6</sup> For purposes of resident engagement in the new construction context, the NARR shall be treated as the equivalent of the CHAP. As the units are entirely new – developed based on Faircloth authority – there are no residents in occupancy pre-application, or prior to the Concept Call, or between the Concept Call and the Financing Plan submission. If the public housing development is an acquisition of an occupied structure, as opposed to new construction, additional resident engagement processes would apply.

# Faircloth to RAD Conversion Process

