

OFFICE OF HOSPITAL FACILITIES  
2017 LENDER TRAINING

# FHA SECTION 242 MORTGAGE INSURANCE FOR HOSPITALS

HUD HEADQUARTERS  
BROOKE-MONDALE AUDITORIUM  
JUNE 14, 2017



# Mortgagee Letter 2016-23

Lender Responsibilities in Servicing  
Section 242 Loans



## MORTGAGEE LETTER 2016-23

### Effective Date:

- December 1, 2016. This Mortgagee Letter supersedes Mortgagee Letter 2015-19.

### Purpose:

- Provide, in a checklist format, a summary of important servicing responsibilities of Lenders of Record holding Section 242 hospital loans.
- The servicing of Section 242 loans is performed either by the Lender of Record ("Lender") or by another HUD-approved lender acting as Agent for the Lender. In either case, interactions with the borrower put the Lender in a position to monitor the borrower's financial well-being and to share critical information and concerns with HUD.

## MORTGAGEE LETTER 2016-23

### Initial Endorsement

#### ❖ Each time a commitment is issued

- 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

## MORTGAGEE LETTER 2016-23

### Construction Phase

#### ❖ Ongoing

- Escrows & Deposits
- Monitor insurance policies and surety bonds
- Letters of credit
- Perform Lender Servicer Tasks as described in OHF Handbook

#### ❖ 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

## MORTGAGEE LETTER 2016-23

### 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.

## MORTGAGEE LETTER 2016-23

### Construction Phase (cont.)

#### ❖ Loan for new construction or Substantial Rehab

- Monitor the disbursements of capitalized interest and advise HUD 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, and causing final endorsement to occur.

## MORTGAGEE LETTER 2016-23

### 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

## MORTGAGEE LETTER 2016-23

### 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.

## MORTGAGEE LETTER 2016-23

### 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.

## MORTGAGEE LETTER 2016-23

### Permanent Loan Servicing – Periodic Monitoring (cont)

#### ❖ Quarterly (Monthly for Credit Watch/Priority Watch accounts)

- Discussion 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.

#### ❖ Persistent decline in financial performance

- Discussions with OHF to consider whether the services of a turnaround consultant should be employed.

## MORTGAGEE LETTER 2016-23

### 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 to start HUD review process.
  - Provide an updated title policy to HUD as needed.

## MORTGAGEE LETTER 2016-23

### Event-Driven Risk Management (cont)

#### Lender Becomes Aware of:

##### ❖ 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

##### ❖ 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

## MORTGAGEE LETTER 2016-23

### 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

- Review and approve/disapprove loan documents
- HUD-92322-OHF- Intercreditor Agreement (ICA) for 242 program
- If approved, submit to OHF AE along with Borrower's request

## MORTGAGEE LETTER 2016-23

### Event Driven Risk Management (cont)

#### Lender Becomes Aware of (cont):

##### ❖ Delinquent mortgage payments

- Notify OHF AE. Report through MDDR system as required.
- 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.

##### ❖ Vacating or condemnation of project

- Notify HUD AE

## MORTGAGEE LETTER 2016-23

### 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

#### ❖ Lender Elects to Assign Mortgage to HUD

- Continue to bill for and accept payments until mortgage is assigned in Secretary's name

## MORTGAGEE LETTER 2016-23

### 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.

## MORTGAGEE LETTER 2016-23

### 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

If you have any questions or concerns regarding this Mortgagee Letter, please contact Kathryn Killeen at 202-402-3119 ([kathryn.e.killeen@hud.gov](mailto:kathryn.e.killeen@hud.gov)).

Persons with hearing or speech impairments may access this number via TDD/TTY by calling 1-800-877-8339.



# Office of Architecture and Engineering

Robin Senator RA, Director



## WHO IS OAE?

- The Office of Architecture and Engineering (OAE) is responsible for the architectural-engineering technical oversight for FHA-242/241 design and construction projects and FHA 242/223f or 223A refinancing projects. Once a project passes the preliminary financial review and receives a favorable determination, OAE is asked to assign a Project Manager for a particular FHA-242 project.
- OAE works in conjunction with the assigned HUD OHF Account Executive all through the various phases of the project--from the conceptual stage, through the application stage, the commitment and initial endorsement stages, construction and through to the close out of construction.
- OAE also provides Construction Asset Management for OHF.
  - Renovations or additions on insured properties. Updated 4128's.
  - Physical inspections as required on insured properties or new acquisitions.



## SERVICES PROVIDED BY OAE

- Pre-Application Phase
  - OAE attends Pre-Application meeting at HUD headquarters to examine extent of construction in the potential client's loan.
  - OAE advises on acceptable forms of contract and other regulations per loan type criteria, and advises on required construction documentation, to best position hospital for complete loan package.
  - OAE can meet separately with hospital's design and construction team to advise further on an optimal loan application from a construction point of view.

## SERVICES PROVIDED BY OAE

- Application Phase
  - OAE reviews application for completeness with regard to construction, legal, environmental and budgetary documentation.
  - OAE participates in Initial Site Visit with OHP/OHF Customer Service Team (CST).
    - OAE attends meetings with Hospital, Lender and CST.
    - OAE performs Physical Inspection of Properties to be included in the mortgage insurance and prepares a site visit report for the Account Executive.
    - OAE meets with Design Team to review proposed project.

## SERVICES PROVIDED BY OAE

- Application Phase (Continued)
  - For construction projects-OAE discusses with applicant, and their design and construction consultants:
    - “Left Side” of HUD-92013-OHF Application for Hospital Project Mortgage Insurance (Lines C1-C9) related to design/construction budget).
    - HUD Acceptable forms of contract (Construction Management, Design Build, and Lump Sum).
    - Prevailing wage requirements (if any); retainage, bonding, damages and dispute resolution requirements, so all parties are clear on process.
    - Early construction start options allowed by HUD.
      - site preparation work
      - pre-commitment work
      - early start

## EARLY CONSTRUCTION START OPTIONS

- Site Preparation Work
  - The Hospital has usually had a pre application review and been invited to submit an application. They may not be ready to submit but want to do some work prior. The Lender submits a request to OAE and copies the CST. It can be asbestos removal and demolition of a building, site work but not actual construction. OAE will need to review:
    - Construction contract or Construction Management Agreement with GMP for this work.
    - Performance and Payment Bonds.
    - Construction documents or site drawings or other documentation of what is entailed.
    - Phase One Environmental as OAE will prepare a form HUD-94128-OHF (HEROS) before work can proceed.
    - Paperwork for the 2530's needs to be submitted and approval received.
    - OAE will then issue a letter allowing work to proceed.

## EARLY CONSTRUCTION START OPTIONS

- Pre-Commitment Work
  - The Hospital can submit a request to perform pre-commitment work after an application is submitted but before they receive commitment. This can include construction work but must be complete before closing. It could be ordering steel or other long lead items, excavation, foundation work, etc. OAE reviews same documents as for site preparation plus receives a signed "Representations and Warranties." This requires approval by OHP DAS as well.
- Early Commencement of Work (Early Start)
  - This is construction work that starts after commitment but before initial closing. Often due to weather conditions foundation and steel work need to be started early. Lender submits form HUD-92415-OHF Request for Permission to Commence Construction Prior to Initial Endorsement for Mortgage Insurance.

## SERVICES PROVIDED BY OAE

- Application Phase (Continued)
  - OAE makes Recommendation to OHF to Proceed to Commitment:
    - OAE approved drawings and specifications .
    - Firm fixed Construction Cost- Fully executed construction contract (lump sum HUD-92442-OHF or Construction Management Agreement with GMP or Design-Build).
    - Executed Owner-Architect Agreement with Fixed Fee.
    - Approved HUD-92013-OHF.
    - Environmental Review Approval prepared by OAE using HEROS. *(HUD Environmental Review Online System).*

## SERVICES PROVIDED BY OAE

- Application Phase (continued)
  - OAE makes Recommendation to OHF that Project Proceed to Initial Endorsement:
    - Current certified or draft metes and bounds survey of all properties included in the mortgage.
    - Evidence of Zoning Compliance
    - Building Permit(s).
    - Engineer's Sub-surface Report
    - Assurance of Utility Services

## SERVICES PROVIDED BY OAE

- **Pre-Construction Phase** (After Commitment and/or Recommendation to proceed to Initial Endorsement prior to Closing):
  - Perform final inspection of pre-commitment work (if any).
  - Final Approval For Early Commencement of Work (HUD-92415-OHF) if requested.
  - Review Initial Advance for hard costs to be paid at Initial Closing.
  - Review final certified site surveys.
  - Prepare letter for HUD Attorney stating items reviewed and approved for Initial Closing by OAE.
  - OAE conducts pre-construction conference with loan servicer to educate hospital/construction team on correct advance procedures to keep construction cash flow and timeline within loan and hospital business continuity parameters.

## SERVICES PROVIDED BY OAE

- Construction Phase:
  - Conduct bi-monthly site visits and prepare site visit report.
  - Review Monthly HUD-92403-OHF Application for Insurance of Advance of Mortgage Proceeds and/or HUD-92464-OHF Request for Approval of Escrow Funds-Hospital/Section 242.
    - HUD-92448-OHF Contractor's Requisition Project Mortgages (Line C1)
    - Architect's and Consultant Fees
    - Other Construction Related Hard Costs
  - Discuss and review any upcoming change orders.
    - OAE is authorized to approve change orders up to \$250,000.
    - Change orders above \$250,000 require approval by OHF and OAE makes a recommendation to Account Executive.
  - Review line item budget transfer requests and make recommendation to OHF.

## SERVICES PROVIDED BY OAE

- Post Construction Phase:
  - 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.
    - Lien Waivers.
    - As Built ALTA Site Survey



## OAE CAPITAL ASSET MANAGEMENT

- HUD FHA 242 Regulatory Agreement requires review of additional construction and renovation projects on mortgage collateral properties. Hospitals also need to be kept in good repair.
  - Reporting of Capital Projects to Lenders, OHF Account Executives and OAE Project Managers by Hospitals.
  - HUD 4128 Environmental Review now required.

# NEW HUD ENVIRONMENTAL REVIEW REQUIREMENTS

- CPD is responsible for Compliance with all Environmental Regulations throughout HUD.
- They have issued Guidance for all HUD Reviewers, including OAE, on what qualifies as Maintenance which does not require Environmental Review.
  - Maintenance activities slow or halt deterioration of a building and do not materially add to its value or adapt it to new uses.
  - Sometimes, maintenance of a building feature or system requires periodic replacement of individual component parts that are subject to normal wear and tear.
  - While maintenance is often budgeted as an operating expense, and repairs and rehabilitation are treated as capital expenses, it is the nature of the activity itself, not its budget category that determines whether it qualifies as maintenance for environmental review purposes.

# NEW HUD ENVIRONMENTAL REVIEW REQUIREMENTS

- All proposed work, that does not qualify as maintenance under this notice, would need to go through an environmental evaluation and OAE would need to prepare a 4128 review in HEROS. The scope of an environmental review relates to the nature and extent of the rehabilitation activities.
  - **For environmental review purposes,**
    - Deferred maintenance that has resulted in a need for extensive repairs and rehabilitation does not qualify as maintenance.
    - If items that would otherwise be considered maintenance are done as part of an extensive remodeling or renovation of a building that amounts to rehabilitation, the entire job is considered rehabilitation.
    - Depending on the extent of damage, activities performed after a disaster event will typically not be considered maintenance.
  - **Possible impacts could be;**
    - Related to historic preservations issues (for example, change the appearance of the building) and;
    - Issues with landscaping or new construction/renovations around updated floodplains and wetlands. For example, FEMA has been updating their maps and we see some significant changes in recently impacted areas (super-storm Sandy etc.).

# Office of Hospital Facilities: Review of Closing and Transactional Documents

## OHF DOCUMENT REVIEW - BACKGROUND

- Goal: Develop documents specific to OHF/242 program to support closing and program processes.
- Documents can be found on HUDClips

## OHF DOCUMENT REVIEW

- Effective Date:
  - ❖ Effective for any commitments issued after Oct 1, 2016.
  - ❖ Documents are "good until 8/31/2019".

## OHF DOCUMENT REVIEW

- Process:
  - ❖ Used existing 232 documents as start point
  - ❖ Some documents removed
  - ❖ Certain form numbers were renamed in the revised collection to reflect a consistent naming convention
    - All OHF forms now have the HUD-9 prefix

## OHF DOCS - NEW FORMS

- HUD-91070-OHF – Consolidated Certifications Borrower
  - New form that consolidates many certifications into one form (ex – prior versions of the HUD-41901, HUD-92010, Byrd Amendment Certifications, etc.)
- HUD-92466-OHF – Regulatory Agreement
  - To be covered in more detail later

## OHF DOCS - NEW FORMS

- HUD-92476-OHF – Escrow Agreement for Deferred Work
  - Escrow language modified to cover funds for deferred work
- HUD-92476A-OHF – Escrow Agreement for Limited Rehabilitation
  - Escrow language modified to cover 223(f) loans

## Figure 1. Insurance Upon Completion Process and Documents 223(f) or 223(a)(7) Project with Rehabilitation or Repairs

PRELIMINARY → PRE-ENDORSEMENT → ENDORSEMENT → REHAB/REPAIRS → COST CERTIFICATION → ESCROW CLOSEOUT

Replacement  
Cost  
and Maximum  
Insurable  
Mortgage  
Worksheet

Borrower's  
Certificate of  
Known Costs  
HUD-92205-OHF

Escrow Agreement  
for Limited  
Rehabilitation  
or Deferred Work  
HUD-92476A-OHF  
or  
92476-OHF

Commitment  
Letter Insure  
Upon Completion

Request Approval of  
Escrow Advance  
HUD-92464-OHF

Borrower's  
Certification **Partial**  
Completion  
HUD-92117-OHF

Request for Approval of  
Final Escrow Advance  
HUD-92464-OHF

Borrower's Certification  
**Full** Completion  
HUD-92117-OHF

Borrower's Cert.  
of Actual Cost  
HUD-92330-OHF

Contractor's Cert.  
of Actual Cost  
HUD-92330A-OHF

- Remaining Borrower's Cash Equity Returned
- Cost Savings Remain in Escrow For Capital Costs or Funding MRF
- After All Remaining Funds Are Spent, Escrow Account is Closed

## OHF DOCS - NEW FORMS BASED ON 232 DOCS

- HUD-92322-OHF – Intercreditor Agreement
  - To be covered in more detail later
- HUD-92441-OHF – Building Loan Agreement
  - Includes provisions for various expenses involved in 242 transactions, off-site improvements and 242 construction contracts.

## OHF DOCS - NEW FORMS BASED ON 232 DOCS

### HUD-92434-OHF – Lender's Certificate

- Removed Administrative Fees provision;
- added disclosure of GNMA extension fee provision and deleted provision noting that Borrower has collected amounts to cover extension fees;
- changed the time for submission of application for insurance of advances;
- various updates to conform to the handbook;
- added a provision on escrows and deleted unitary loan provision.

# UNDERWRITING WORKSHOP FOR NEW LENDERS



# UNDERWRITING DIVISION OUTLINE

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



**Delta Regional Medical Center  
Greenville, MS**

# HOSPITAL MORTGAGE INSURANCE PROGRAMS

## ➤ Insurance Types Available

- §242: For hospitals not currently in the FHA portfolio seeking financing for new construction projects or substantial rehabilitation (may include mortgage proceeds for existing debt refinance – up to 80% of the loan amount).
- §223(f): For hospitals 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).
- §241: For hospitals already in the FHA portfolio seeking financing for new construction projects, substantial rehabilitation, or additions.
- §223(a)(7): For hospitals already in the FHA portfolio seeking to refinance existing FHA loans.
- Interest Rate Reduction: For hospitals already in the FHA portfolio seeking interest rate reductions on existing FHA loans, without increasing UPB or the term of the existing loan.



## PROGRAM GUIDANCE

- Statute – Section 242 of the National Housing Act
  - ❖ 12 U.S.C. 1715z–7
  - ❖ [https://portal.hud.gov/hudportal/HUD?src=/federal\\_housing\\_administration/healthcare\\_facilities/section\\_242/additional\\_resources](https://portal.hud.gov/hudportal/HUD?src=/federal_housing_administration/healthcare_facilities/section_242/additional_resources)
- Regulation – Hospital Mortgage Insurance Program
  - ❖ 24 CFR Part 242
  - ❖ <https://www.gpo.gov/fdsys/pkg/FR-2013-02-05/pdf/2013-02404.pdf>
- Handbook
  - ❖ 4615.1
  - ❖ <https://portal.hud.gov/hudportal/documents/huddoc?id=46151HSGH.pdf>

## STATUTORY ELIGIBILITY CRITERIA

- Loan-to-Value Requirement
  - ❖ Maximum LTV for Section 242, 241, 223(f) programs = 90%
  - ❖ Based on net book value of property, plant, and equipment
  - ❖ Appraisals may be used to meet the LTV requirement
- First Lien
  - ❖ The HUD-insured lender must have a first lien position on real estate
  - ❖ HUD requires that the Lender also have a first lien on revenues, accounts receivable, etc.

# STATUTORY ELIGIBILITY CRITERIA

## *CONTINUED*

- 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 in-house sources
- Patient Day Requirement
  - ❖ Acute care patient days must be greater than 50% of total patient days
  - ❖ Non-acute patient days include skilled nursing, rehabilitation, psychiatric, and other services

## REGULATORY ELIGIBILITY CRITERIA

- §242.16 - Historical Operating Margin Requirement
  - ❖ The 3-year aggregate Operating Margin must exceed 0%.
- §242.16 - Historical Debt Service Coverage Ratio Requirement
  - ❖ The 3-year average debt service coverage must exceed 1.25x (1.4x for Section 223f).
- §242.72 - Owner/Operator
  - ❖ Owner/Operator structures not allowed
  - ❖ Borrower must also operate the entity

# REGULATORY ELIGIBILITY CRITERIA

## *CONTINUED*

- §242.8, §242.64, Collateral Requirements
  - ❖ All critical pieces of the property, operations must be captured as collateral
  - ❖ “Fully functioning hospital”
- §242.4 - Capital Purchases
  - ❖ Mortgage Proceeds must be used for capital purchases
- §242.11 - Compliance with State and Federal Regulations
  - ❖ If under investigation, it must be disclosed to HUD and evaluated

## OTHER REGULATORY HIGHLIGHTS

- §242.14 – Mortgage reserve fund (MRF)
  - ❖ Each mortgagee after closing or after construction is complete, must establish a MRF.
    - Same for all hospitals
    - At 5 years, must have deposited 12 months of debt service
    - At 10 years, must have deposited 24 months of debt service

## PROGRAM FEES

- Application (One-Time) Fees
  - ❖ Application fee (0.15% of the mortgage amount)
  - ❖ Commitment fee (0.15% of the mortgage amount)
  - ❖ Inspection fee (ranges from 0.1% to 0.5% of the mortgage amount, depending on the Section of the Act)
- Ongoing (Annual) Fees - MIP
  - ❖ Ranges from 55 bps (223a7) to 70 bps (242), with first-year exceptions

## PROCESS OVERVIEW

Pre-Application

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

Application

- Application
- Underwriting Review
- Commitment

# PRE-APPLICATION PROCESS

## Pre-Application

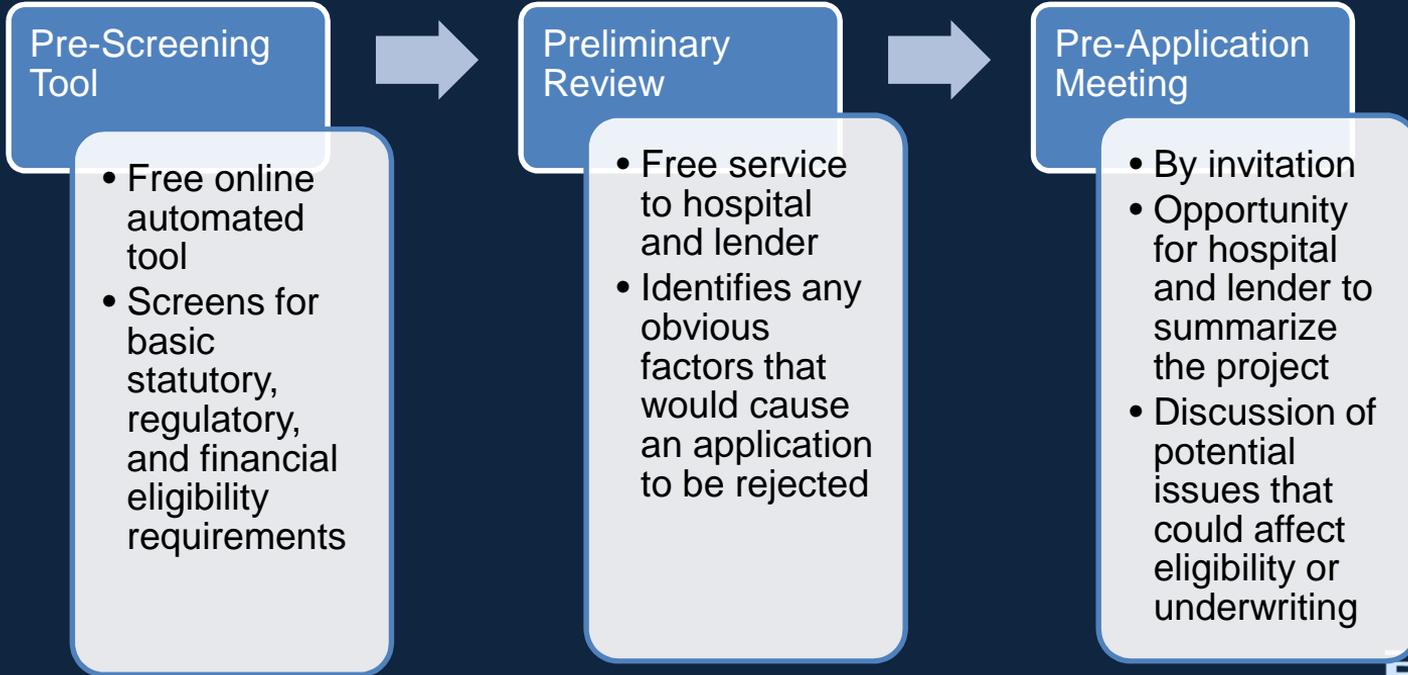
- Pre-Screening Tool
- Preliminary Review
- Pre-Application Meeting

## Application

- Application
- Underwriting Review
- Commitment

# PRE-APPLICATION PROCESS

*CONTINUED*



# PRE-APPLICATION OVERVIEW

## PRE-SCREEN AND PRELIMINARY REVIEW

- Pre-Screening Tool
  - ❖ [https://portal.hud.gov/hudportal/HUD?src=/federal\\_housing\\_administration/healthcare\\_facilities/section\\_242/Prescreening242](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

# PRE-APPLICATION OVERVIEW

## PRELIMINARY REVIEW

- Preliminary Review Submission Contents
  - ❖ Preliminary Review Template
  - ❖ Audited financial statements
  - ❖ Utilization statistics
  - ❖ Project description
  - ❖ Organizational chart/collateral discussion
- OHF Review
  - ❖ Review of eligibility
  - ❖ Credit review

## PRE-APPLICATION OVERVIEW PRELIMINARY REVIEW

- Credit/Programmatic Review
  - ❖ Financial Statement review
  - ❖ Ratio analysis
  - ❖ Proforma
  - ❖ Market Review
  - ❖ Unique Factors
- Process – Underwriter review, followed by brief committee review
- Goal: Provide feedback to lender in 2 weeks

# PRE-APPLICATION PROCESS OVERVIEW

## PRE-APPLICATION MEETING

- What is the purpose of the Pre-Application Meeting
  - ❖ Discuss issues identified during the Preliminary Review
  - ❖ Overview of the Hospital and its project
- In-person meeting is optional for certain proposals (some 223(f) and 241 loans)
- Following the meeting, OHF staff meets and determines next steps

# APPLICATION PROCESS

Pre-Application

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

Application

- Application
- Underwriting Review
- Commitment

# APPLICATION PROCESS

*CONTINUED*

## Application

- Development by lender and hospital
- Submission to HUD
- Fees paid

## Underwriting Review

- Assign Client Service Team (CST)
- Conduct detailed review
- Develop recommendation

## Commitment

- If the hospital and project meet FHA's requirements and the FHA Commissioner approves the application, a commitment for mortgage insurance is issued

# UNDERWRITING PROCESS OVERVIEW

## APPLICATION PROCESS

- Application Requirements/Development
  - ❖ **Volume 1**
    - Application form (sources and uses)
    - Information on the Board Members, Executives
    - “Check-the-box” requirements
  - ❖ **Volume 2**
    - Financial Statements and budget
    - Forecast
    - Insurance and contracts
  - ❖ **Volume 3**
    - Architectural and Engineering documents

# UNDERWRITING PROCESS OVERVIEW

## APPLICATION PROCESS (CONT'D)

- Steps in the Application Process
  - ❖ 1. Application Receipt and Completeness Review
  - ❖ 2. Underwriting Questions
  - ❖ 3. OHF Site Visit
  - ❖ 4. Covenant review and discussion
  - ❖ 5. Previous Participation (2530) review
  - ❖ 6. Architectural/Engineering /Environmental Review
  - ❖ 7. Credit Report development
  - ❖ 8. Credit Committee Review
  - ❖ 9. Approvals- (ORM, OGC, FHA Commissioner)

# PRE-APPLICATION AND APPLICATION PROCESSING TIMES (GOALS)

- 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)

# Office of Hospital Facilities Regulatory Agreement

## OHF DOCUMENT REVIEW – NEW CONCEPTS -REGULATORY AGREEMENT (“RA”)

- Overview of key concepts and definitions
  - ❖ Definitions section in back of RA
- Concepts and terms:
  - ❖ Use of “Borrower” and “Lender” versus “Mortgagor” and “Mortgagee” in old RA.
  - ❖ Program Obligations

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section II.4 – Lender's Certificate

- Reference to new 242 documents, as applicable
  - ❖ Lender Certificate (HUD-92434-OHF)
  - ❖ Request for Endorsement of Credit Instrument & Certificate of Lender, Borrower & General Contractor (HUD-92455-OHF)
    - Documents already used in 232 programs
    - Lender Certification of HUD Program Obligations
    - Discloses fees, expenses and escrows

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### SECTION II.8. CONDITIONS TO BE SATISFIED DURING AND FOLLOWING CONSTRUCTION.

(a) Section 242 and 241:

- (i) **Application of Cost Savings.** Any Cost Savings identified during the cost certification process shall be used to reduce the principal amount of the Note and Borrower's cash equity contribution proportionally, in accordance with Program Obligations unless the Borrower elects to have a greater portion of the Cost Savings used to reduce the principal amount of the Note.
- (ii) **Submission of construction and performance review report.** Between initial endorsement and final endorsement, the Borrower shall furnish HUD with a report, within forty (40) days of the close of each quarter, addressing:
  1. The progress of construction;
  2. Adherence to the construction budget and the projected schedule; and
  3. Unanticipated issues encountered during construction (including Project scope change, change orders, and/or cost overruns), and how the issues will be resolved.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section II.8. CONDITIONS TO BE SATISFIED DURING AND FOLLOWING CONSTRUCTION.

#### (a) Section 242 and 241 (cont):

#### (iii) Completion of final endorsement

1. Borrower shall complete final endorsement within 180 days from commencement of amortization of the construction note.
2. If Borrower does **not** complete final endorsement within 180 days from commencement of amortization of the construction note, then Borrower may, in advance of the completion of the 180-day period, request from HUD one or more extensions in increments of 90 days. Extension requests must include a Board-approved timetable outlining tasks and dates necessary to achieve final endorsement.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section II.8. CONDITIONS TO BE SATISFIED DURING AND FOLLOWING CONSTRUCTION

(b) Section 223(f) and 223(a)(7) Projects [when construction is part of the refinance]

- (i) **Application of Cost Savings.** Any Cost Savings identified shall be used in accordance with the provisions of the Escrow Agreement for Limited Rehabilitation or Escrow Agreement for Deferred Work.
- (ii) **Submission of construction and performance review report.** Between initial/final endorsement and completion of the work, the Board shall furnish HUD with a report, within forty (40) days of the close of each quarter, addressing:
  1. The progress of construction;
  2. Adherence to the construction budget and the projected schedule; and
  3. Unanticipated issues encountered during construction (including Project scope change, change orders, and/or cost overruns), and how the issues will be resolved.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section II.8. CONDITIONS TO BE SATISFIED DURING AND FOLLOWING CONSTRUCTION

(b) Section 223(f) and 223(a)(7) Projects [when construction is part of the refinance] (cont)

#### iii. Completion of supplemental cost certification, if required,

1. Borrower shall complete supplemental cost certification within 180 days from the Completion Date as required in the Escrow Agreement for Limited Rehabilitation or Escrow Agreement for Deferred Project Work.
2. If Borrower does not complete supplemental cost certification within 180 days from the Completion Date, then Borrower may, in advance of the completion of the 180-day period, request from HUD one or more extensions in increments of 90 days. Extension requests must include a Board-approved timetable outlining tasks and dates necessary to achieve supplemental cost certification.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.11 – Property and Operations; Encumbrances

- ❖ Receipts deposited in accordance with Program Obligations
- ❖ Use FDIC insured or brokerage account
- ❖ Satisfy liens
- ❖ Notify HUD and Lender of receivership/bankruptcy
- ❖ Maintain insurances
- ❖ Notify HUD and Lender of condemnation
- ❖ Notify HUD and Lender of litigation not covered by insurance

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.12: Finances and Financial Records

- ❖ Accurately record the activities of the Borrower and the Project.
- ❖ Maintain accounts, records and reports for the Borrower and Project separate from other entities.
- ❖ Segregate income and funds of the Project from any business or activity not related to the Project.
- ❖ Funds of the Project can only be used for the Project, with the exception of Surplus Cash.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

- Sec III.13: Financial Reports
  - ❖ Now applies to Borrower and Affiliates included in Regulatory Agreement.
  - ❖ Financial reports provided to HUD and Lender.
  - ❖ No change in due dates:
    - Monthly & quarterly: 40 days after month- or quarter-end.
    - For-profit: 120 days for audited financial statements (AFS).
    - Not-for-profit and governmental: 120 days for board-certified statements (if applicable) and 9 months for AFS.
  - ❖ Board-approved annual budget prior to start of F/Y.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.17 – Transactions with Affiliates

- Definition of Affiliate (Section 242.1 of the Regulation)
  - ❖ *Affiliate* means a person or entity which, directly or indirectly, either controls or has the power to control or exert significant influence on the other, or a person and entity both controlled by a third person or entity, which may be a parent entity...
- Affiliate position and performance may be critical during the underwriting process
- Affiliates that pledge assets to the HUD-insured lender are listed in Exhibit B.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.17 – Transactions with Affiliates

- Section 17 (a)
  - ❖ Arms-length transactions between affiliates do not require HUD approval
  - ❖ A transaction is arms length if the cost of the property or service provided is no less than the lower of (a) the market value, or (2) the fully allocated cost to the Borrower
  - ❖ Non-arms length transactions with Affiliates listed in Exhibit B do not require HUD approval
- Section 17 (b)
  - ❖ Payment for any good or service provided by the Borrower to an Affiliate must be received within 90 days of providing such service
  - ❖ Affiliates listed in Exhibit B are not bound by this requirement

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.18 – Distribution of Assets

- Section 18 (a), (b), (c)
  - ❖ Establishes the conditions and thresholds that a Borrower must meet in order to distribute assets
  - ❖ Conditions: Final endorsement has occurred, Borrower is current on payments, MRF is fully-funded, taxes and payroll contributions are deposited as required
  - ❖ Thresholds – Debt service coverage, Days in A/R, Average Payment Period, Current Ratio, Days Cash on Hand, Net assets
  - ❖ Limitation on distributions based on net income and equity financing ratio
- Section 18 (d)
  - ❖ Certification requirement
- Section 18 (f)
  - ❖ Affiliates listed in Exhibit B are not bound by this requirement

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report

#### ❖ 19(a): Board review and report

- Board must review financial statements (F/S) at least twice a year.
  - As applicable, review must include, at a minimum:
    - » Audited F/S;
    - » 6-month interim F/S;
    - » Board-certified F/S, if applicable.
- Includes F/S of Borrower and Affiliates included in RA.
- Board review must occur by the F/S submission due date, or earlier as stipulated in RA.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report (Con't)

#### ❖ 19(a): Board review and report (Con't)

- Board must provide written report (Report) to HUD and Lender within 30 days of review if any of the following conditions exist:
  - Loss from operations that is at least one percent of Total Operating Revenue;
  - Net income less than zero; or,
  - MRF is not fully funded in accordance with MRF schedule.
  
- Report must include actions to be taken to improve Borrower's financial operations.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report (Con't)

#### ❖ 19(b)/(c): Business plan

- Upon receipt of Report (or expiration of required timeframe to submit Report), HUD may request a Business Plan.
- Business Plan (and any updates) will include:
  - Analysis of issues leading to negative financial results.
  - A turnaround plan detailing actions to be taken to address the issues.
  - Projections of cost savings/revenue increases from implementation of the actions and related timetables.
  - Financial forecast for at least 12 months.
  - An approval resolution by the Board.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

- Sec III.19 – Business Plan/Consultant's Report (Con't)
  - ❖ 19(b)/(c): Business plan (Con't)
    - Business Plan is due within 60 days of HUD's request.
    - Annual update of Business Plan required until certain financial parameters are met for 2 consecutive years based on AFS:
      - Positive net income; and
      - Loss from operations is no greater than 1% of total operating revenue.
    - Business Plan update shall be submitted to HUD and Lender with annual budget.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report (Con't)

#### ❖ 19(d): Review Consultant

- HUD may require engagement of Review Consultant.
- Review Consultant will review and report on the following:
  - Business Plan (if any);
  - Borrower's operational and financial issues;
  - Recommendations for corrective action; and
  - Other items identified by HUD.
- Scope, milestones and timeframe of review and report must be approved by HUD.
- Status updates must be provided to HUD and Lender.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report (Con't)

#### ❖ 19(e): Independent Consultant

- HUD may require engagement of Independent Consultant.
- Independent Consultant will review and report on the following:
  - Governance and organizational structure;
  - Management;
  - Recommendations for corrective action; and
  - Other items identified by HUD.
- Scope, milestones and timeframe of review and report must be approved by HUD
- Status updates must be provided to HUD and Lender.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.19 – Business Plan/Consultant's Report (Con't)

#### ❖ 19(f): Implementation plan

- Plan to implement Review/Independent Consultant's recommendations shall be submitted to HUD/Lender.
  - Using format detailed for the Business Plan; and
  - Submission within agreed-upon timeframe.

#### ❖ 19(g): Use of MRF

- HUD may direct that the MRF be used to pay for the services required under this section.
  - Including implementation of Consultant's recommendations.
- HUD must approve the related contract(s).
- MRF funds used shall be replenished based on a revised MRF schedule issued by HUD.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.20 – Additional Indebtedness and Leasing:

- Long-term
  - ❖ Secured versus unsecured
  - ❖ Conditions for Notification versus HUD approval
- Unsecured Short Term Debt, with the exception of lines of credit
  - ❖ Conditions for Notification versus HUD approval
- Short term debt in the form of a line of credit
  - ❖ Secured by Patient Accounts Receivable
  - ❖ 242 Intercreditor Agreement executed by Borrower, Lender & Short Term debt lender and approved by HUD.
  - ❖ To be covered in more detail in ICA discussion
- Limitation on Total Debt Service Payments
- Reporting Requirements

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.23 – Comparison of Financial Forecast to Actual Results for the Forecast Periods

#### ❖ If projections were provided with Borrower's application:

- Borrower shall provide an analysis of actual performance compared with the projection within 120 days following the end of each F/Y for which a projection was prepared.
- Written explanation of any material deviations from the projection when compared with actual shall accompany the submission of the Borrower's analysis.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.24 – Changes in Reimbursement

- ❖ If there is a change in any payor reimbursement or contract that results in:
  - A decrease in total operating revenue of at least 3%; or
  - A net loss; then -
- ❖ Borrower must report to HUD assessment of impact within 30 days of the enactment of such a change.
- ❖ Borrower must submit a Board-approved action plan to HUD that addresses the mitigation of the related impact within 60 days of the assessment report.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section III.25 – After-Acquired Property

- After-Acquired Property (definition):
  - ❖ Property (both real property and personalty) purchased or acquired by the Borrower after initial endorsement, or after initial/final endorsement, as applicable, of the Note.
- All After-Acquired Property shall be added to the Mortgaged Property, unless HUD agrees, in writing, that certain After-Acquired Property may be excused from this requirement, or if such After-Acquired Property is used to secure Additional Debt (as allowed in Section 20).
- Borrower shall promptly execute, record, and deliver the necessary documents required by HUD and Lender to encumber said property as additional security for the Note.
- Survey and Phase I for Environmentals.

## IV – PROJECT MANAGEMENT

### Section 26. Preservation, Management & Maintenance of the Mortgaged Property

#### ❖ Borrower

- a) shall not commit or permit Waste,
- b) shall not abandon the Mortgaged Property,
- c) shall restore or repair promptly, or cause to be restored or repaired promptly, in a good and workmanlike manner, any damaged part of the Project to the equivalent of its original condition, or such other condition as HUD may approve in writing
  - a) Reference to 36(g) - "Approvals requiring prior written approval by HUD: Remodeling, adding to, subtracting from, constructing or demolishing any part, except as required under Section 26(c)..."
- d) Shall keep, or cause to be kept, the Project in decent, safe sanitary condition and good repair, including the replacement of Personalty and Fixtures with items of equal or better function and quality

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Sec III.28 – Identify of Interest & Conflict of Interest

- ❖ Borrower shall have a policy on identity of interest and conflict of interest.
  - Policy must be compliant with State and Federal requirements.
- ❖ The Borrower shall disclose to HUD any identities of interest and conflicts of interest that are identified under the Borrower's policy.
- ❖ Reference to 24 CFR 242.53(b) on Excluded Contractors
  - 24 CFR 242.53(b) Contracts relating to the construction of the project shall not be made with a general contractor that has an identity of interest, as defined by HUD, with the mortgagor or mortgagee.

## IV – PROJECT MANAGEMENT

### Section 31. Acceptability of Management of Hospital

- ❖ Moves 24 CFR 242.61 of Regulations to Regulatory Agreement
  - Applies to Contract Management, Principals, Key Employees and Board
- ❖ 2530 requirement

### Section 32. Commercial Leases

- ❖ Commercial space leases of the Mortgaged property must be approved by HUD in writing
- ❖ Must include a provision that permits, HUD, any lender-in-possession or any successor organization, at such party's option, to succeed to the interest of the Borrower

### Section 35. Debts of Affiliates

- ❖ Borrower shall not be directly or indirectly responsible for the debts or liabilities of any affiliates without prior written approval of HUD

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Section V.36: ACTIONS REQUIRING PRIOR WRITTEN APPROVAL OF HUD.

#### ❖ Section V.36 (g)

- Remodeling, adding to, subtracting from, constructing or demolishing any part, except as required by HUD under Section 26(c).
- Disposal of obsolete equipment does not require HUD approval if replaced by like items. Minor alterations that do not adversely affect the Mortgaged Property in accordance with Program Obligations does not require HUD approval.

#### ❖ Section V. 36 (n) – Entering into a contract for a merger, reorganization and/or consolidation.

#### ❖ Section V. 36 (o) – Establishing, developing, organizing, becoming the sole member of or acquiring an interest in any corporation, subsidiary or affiliate organization.

#### ❖ Section V 36 (p) – Entering into an interest rate swap or any derivative related to the Note.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### Exhibits to the Regulatory Agreement

- Exhibit A (Legal Description of the Land)
  - ❖ Prepared prior to Closing
- Exhibit B (List of Affiliates)
  - ❖ A list of Affiliates who are pledging assets and/or revenues to the Lender. The Exhibit is refined during the underwriting process and included with the Commitment.
- Exhibit C (Excluded Property)
  - ❖ List of property that is excluded from the Regulatory Agreement and Security Instrument. Exhibit C is refined during the underwriting process and included with the Commitment.

## OHF REGULATORY AGREEMENT ("RA") REVIEW

### EXHIBIT D – Definitions

- ❖ Program Obligations
- ❖ Waste
- ❖ Collateral-related definitions: Project, Mortgaged Property, Land, etc.
- Other sources of definitions
  - ❖ Regulation 242.1
  - ❖ Handbook
  - ❖ Security Instrument

Accounts Receivable Financing:  
Intercreditor Agreement (ICA)  
Section 242 Program  
Form HUD-92322-OHF

# INTERCREDITOR AGREEMENT (ICA) SECTION 242

- ❖ The October 2016 documents included an ICA specifically for the 242 program
  - HUD-92322-OHF – ICA for the 242 program.
- ❖ Reminder: HUD approval – Federal Register, Vol 77. No. 119, page 37249
  - OHP DAS or ADAS approval required “To authorize a portfolio hospital to pledge accounts receivable as collateral for non-FHA indebtedness”
- ❖ ICA is referenced in the Regulatory Agreement in Section 20 (b) for Short-Term Indebtedness

# INTERCREDITOR AGREEMENT (ICA) SECTION 242 – REG AGREEMENT

Reg Agreement Section 20(b)(iii): Additional Indebtedness and Leasing:  
Short Term Debt in the form of a Short Term Line of Credit (LOC) is permitted with prior approval of HUD pursuant to the following:

1. Short term LOC may not have a limit > 15 days of Adjusted Operating Expenses, as reflected on the Most Recent Audited Financial Statements
2. Short Term LOC may be secured by patient accounts receivable, subject to consent by the Lender and HUD
  - The Total amount of the patient accounts receivable used to secure the Short Term LOC cannot be greater than 150% of the Short Term LOC

# INTERCREDITOR AGREEMENT (ICA) SECTION 242 – REG AGREEMENT

Reg Agreement Section 20(b)(iii): Additional Indebtedness and Leasing:  
Short Term Debt in the form of a Short Term Line of Credit (LOC) is permitted with prior approval of HUD pursuant to the following:

3. Total Short Term Debt for the current fiscal year will not exceed 5% of the Average Adjusted Operating Revenue for the three most recent fiscal years based on audited financial statements
4. The combined debt service for all Long Term and Short Term debt in the current fiscal year is not projected to exceed 10% of the average Adjusted Operating Revenue for the three most recent fiscal years based on audited statements

# INTERCREDITOR AGREEMENT (ICA)

## SECTION 242 – REG AGREEMENT

Reg Agreement Section 20(b)(iii): Additional Indebtedness and Leasing: Short Term Debt in the form of a Short Term Line of Credit (LOC)

5. MRF funding is current
6. No condition of default exists under the Reg Agreement or under other debt agreements
7. For All Short-Term Debt that is secured by Borrower's Accounts Receivable, Borrower must obtain an Intercreditor Agreement executed by Borrower, Lender and Short Term Debt Lender which shall be approved by HUD.

# INTERCREDITOR AGREEMENT (ICA)

## SECTION 242

242 ICA based on the most recent 232 ICA. Key changes to 232 ICA:

- ❖ Changed residential care facility language to reflect hospitals
- ❖ Removed language relevant to Owner/Operators and master tenancy/leases that do not apply to 242
- ❖ Includes provisions to cover additional facilities under one loan as many 242 loans cover multiple buildings/facilities
- ❖ Changed "impositions" in 232 documents to "current mortgage costs" in 242 documents.
  - Current Mortgage Costs equals the sum of all principal and interest under the FHA-insured Loan Documents and taxes and insurance due and owing with respect to the Hospital for such month.

## INTERCREDITOR AGREEMENT (ICA) SECTION 242 – KEY DEFINITIONS

- ❖ **1.10 Cap Amount:** Means an amount equal to 150% of the Maximum Commitment Amount, calculated as of the Ceased Funding Date
  - “Cap amount” not found in 232 program.
  - Consistent with 242 Regulatory Agreement
  
- ❖ **1.11 Ceased Funding Definition: Ceased Funding” means either of the following events:**
  - (i) AR Lender has received a request for an Advance under the AR Loan Agreement for which there is sufficient Availability and a period of thirty” (30) calendar days has elapsed since the date of such request, during which time such Advance is not made OR
  - (ii) AR Lender has notified Hospital and/or FHA Lender in writing that it has determined to permanently cease making further Advances under the AR Loan Agreement, in accordance the AR Loan Agreement.
  - Major difference from 232 program – Ceased Funding for 242 does not include “cut off time”. For 232, Cut off time shall be no earlier than 30 days after the Cut off Time Notice has been given.
  
- ❖ **1.12 Ceased Funding Date:** the first date that the AR Lender has Ceased Funding

## INTERCREDITOR AGREEMENT (ICA) SECTION 242 – KEY DEFINITIONS

### ❖ 1.15 FHA Lender Priority Collateral:

- Changed to reflect 242 program hospital assets:
  - shall mean any and all property (whether real, personal or mixed, tangible or intangible) in which FHA Lender and/or HUD is granted liens, encumbrances, security interests and other rights pursuant to any of the FHA Insured Loan Documents, except for the AR Lender Priority Collateral, it being understood that FHA Lender and/or HUD has an “all assets” security interest on the assets of Hospital including but not limited to, to the extent permitted by law, (i) the licenses necessary for the operation of the Facility, (ii) all Medicare and Medicaid/state/county provider agreements for the Facility, (iii) the certificates of need for the Facility, and (iv) Hospital’s furniture, fixtures, equipment, software and inventory directly related to such Facility.
- New language not in 232 ICA: “For purposes of clarity, “FHA Lender Priority Collateral” shall not include any Accounts arising from the delivery of goods and rendering of services at the Facility nor the proceeds thereof until the date on which both of the following have been satisfied: (a) AR Lender has Ceased Funding and (b) AR Lender has received proceeds of Accounts, in cash in an aggregate amount equal to the Cap Amount (or, if earlier, on the date on which the AR Loan Obligations have been Paid in Full).”

# UNDERWRITING OVERVIEW AND RECENT TRANSACTION METRICS

## HOSPITAL VOLUME – FY16 AND FY17

- FY16
  - ❖ 5 Commitments totaling \$947M
  - ❖ 223a7 (2), 223(f) (2), 241 (1)
- FY17 (YTD)
  - ❖ 5 Commitments totaling \$258.7M
  - ❖ 223(f) (3) and 241 (2)

## HOSPITAL VOLUME TRENDS

- Section 242 – preliminary review activity increasing
- Section 223(a)(7) – decrease in activity
- Section 241 – volume consistent since 2010 (1-3 projects per year)
- Pipeline: 9 active applications and pre-applications.

## HOSPITAL PROGRAM PRODUCTION (FY14-17)

- 21 successful applications
- \$1.57 Billion
  - ❖ 8 Section 241 loans (including mortgage increases) totaling \$611.7M
  - ❖ 5 Section 223(a)(7) loans (including 1 portfolio hospital 223(f) loan) totaling \$419.6M
  - ❖ 8 Section 223(f) loans totaling \$538.8M

# OHF COMMITMENT METRICS

## Financial Medians for FY 2014 to 2017 Commitments

	223(f)	223(a)(7)	241
Number of Commitments	8	5	8
Total Revenue	\$165,606,000	\$96,799,597	\$582,032,000
Mortgage Amount	\$38,883,450	\$50,976,000	\$51,712,950
Operating Margin	0.4%	1.1%	2.6%
Total Margin	0.7%	1.3%	3.8%
Debt Service Coverage	1.6	1.9	2.5
Days Cash on Hand	112.3	92.9	48.0
LTD to Capitalization	44.8%	62.7%	59.0%
Loan to Value	71.5%	78.0%	76.6%
Mortgage Amt to Revenue	0.39	0.85	0.15

## TOTAL REVENUES TO MORTGAGE AMOUNT

- HUD portfolio experience shows that the ratio is predictive, particularly for large hospitals
- Smaller hospitals – data is less conclusive
- Helpful when sizing loans

## PRO FORMA ANALYSES

- Pro Forma “Baseline” analysis
- Performed informally at the preliminary review stage
- Analysis performed on operating margin, debt service coverage ratio, as well as leverage ratios
- May generate discussion for the pre-application meeting

## METRICS ANALYSIS – TAKEAWAY POINTS

- OHF looks for a combination of strengths in broad metric areas (liquidity, leverage, profitability). “Strength” means:
  - ❖ Liquidity - DCOH at least 40 or 50 days (HUD will consider average payment period when evaluating cash)
  - ❖ Leverage: LTD/Cap under 70%, low mortgage amount/total revenue
  - ❖ Profitability: Three-year aggregate operating margin > 1-2% (no negative trend)
- “Deal Killers” (for 242 and 223(f) in particular) – very low or negative net assets, very low days cash on hand (<20 days), going concern opinion
- Disclaimer – all projects are different, and evaluated on their individual merits!

## DEAL STRUCTURING

- Composition of the Borrower / 'Carve-Outs'
- Term
- Loan to Value
- Mortgage Reserve Fund (MRF)
  - ❖ Reducing MRF obligation with reduced term

## OTHER UNDERWRITING CONSIDERATIONS

- Need & Competition
- Demographics and Community Support
- Board and Management
- Quality & Value Based Purchasing
- Medical Staff
- Compliance

## MEDIAN PROCESSING TIMES (FY14-17 PROJECTS)

- Preliminary Reviews – 25 days (ranged from 8 to 85 days)
- Preliminary Review Letter to Pre-App Meeting - 49 days (ranged from 13 days to 116 days)
- Pre-App Meeting to Complete Application – 150 days (ranged from 32 to 307 days).
- Application Complete to Commitment - 84 days (ranged from 21 to 189 days)

HOSPITAL

# THANK YOU

Office of Hospital Facilities

1-877-HLTH-FHA

[www.hud.gov/healthcare](http://www.hud.gov/healthcare)

