



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-  
FEDERAL HOUSING COMMISSIONER

U.S. Department of Housing and Urban Development  
Office of Housing

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**Transmittal** for Handbook No.: **4615.1 REV-1, CHG-1**

Special Attention of:

Director, Office of Hospital Facilities (OHF)  
Director, Client Service Division, OHF  
Director, Special Services Division, OHF  
Participating Mortgagees

Issued: February 7, 2014

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1. This Transmits:

Changes to Handbook 4615.1 REV-1, Hospital Mortgage Insurance Program

**BACKGROUND**

Since Handbook 4615.1 REV-1 was issued on April 18, 2013, program participants and HUD staff members using it have identified changes they believe would improve clarity and consistency with current healthcare and multifamily policies. The Office of Healthcare Programs agreed with most of the suggestions for change.

**CHANGES**

**1. SUBJECT: DEPOSIT ACCOUNT CONTROL AGREEMENTS**

**Handbook guidance related to § 242.17 Commitments.** Replace Paragraph 1 with the following: (Handbook Page 9)

1. \*The mortgagee is responsible for ensuring that Deposit Account Control agreements (DACA)s are in place at closing for all depository accounts that control the mortgagor's operating revenues and expenditures. (Note: DACA are not required for trust accounts such as the Mortgage Reserve Fund.) The mortgagee is also responsible for ensuring that UCC liens are filed and that all collateral for the HUD-insured loan is securitized for the life of the mortgage.\*

***Reason for Change:*** Clarifies that DACA are required only for operating accounts.

## 2. SUBJECT: EQUITY REQUIREMENT FOR SECTION 241 SUPPLEMENTAL LOANS

**Handbook guidance related to § 242.23 Maximum mortgage amounts and cash equity requirements.** Paragraph 4 below is deleted: (Handbook Page 10)

4. ~~\*Applications for mortgage insurance pursuant to Section 241 must provide 10% of the Total Estimated Project Cost in cash as a minimum equity contribution in addition to meeting all of the other requirements under Section 242.\*~~

### **Appendix 3, Applicant's Guide – Pre-Application, Required Documentation for a Preliminary Review – Section 241 Mortgage Insurance.**

**Section C, Statutory Eligibility Criteria, Loan-to-Value Requirement (LTV).** On Page 21, the following sentence is deleted:

~~\*In addition to meeting the LTV requirement, applicants for Section 241 mortgage insurance must provide 10 percent of the Total Estimated Project Cost in cash as a minimum equity contribution.\*~~

**Section D, Equity Contribution and Working Capital.** On Page 22, the last sentence in the first paragraph is deleted:

~~\*An equity contribution of 10 percent of the mortgage amount is required to be eligible for mortgage insurance through Section 241.\*~~

Replace the three deletions above with the following:

\*Section 241 mortgage amounts, when added to the unpaid principal balance of the outstanding indebtedness relating to the property, may not exceed 90 percent of the estimated replacement cost of the property following completion of the Section 241 project.\*

*Reason for Change: The change is consistent with the Section 241 statute and with established practice in the healthcare and multifamily programs.*

## 3. SUBJECT: HOSPITAL ACQUISITIONS AND PROPERTY PURCHASES

**Handbook guidance related to § 242.23 Maximum mortgage amounts and cash equity requirements.** The text in paragraph 8 below is deleted: (Handbook Page 11)

8. ~~\*For any project that includes the purchase of land and any improvements thereon, or the acquisition of a hospital, the mortgage shall include the lesser of 90 percent of the actual purchase price of the land and any improvements thereon, or 90 percent of HUD's estimate of the sum of the fair market value of such land and the replacement cost of improvements thereon.\*~~

This language is replaced by the following:

8. \*For any loan that is limited to the purchase of land and any improvements thereon, or the acquisition of a hospital, the mortgage shall not exceed the lesser of 90 percent of the actual purchase price of the land and any improvements thereon, or 90 percent of HUD's estimate of the sum of the market value of such land and the replacement cost of improvements thereon. For loans involving purchase of property or hospital acquisition that also include rehabilitation, see the regulations at 242.23(a)(3). For Section 223(f) loans involving purchase of property, also follow the regulations at 242.23(a)(3). For hospital acquisitions under Section 223(f), see the regulations at 242.23(b)(2). For Section 241 loans that include property purchase or refinancing in connection with the financing of a proposed construction project, the mortgage may include only the lesser of (a) HUD's estimate of the fair market value of such land and improvements prior to substantial rehabilitation or (b) the purchase price (or capital debt to be refinanced) as appropriate, plus other allowable costs. Valuation of land and existing improvements should follow guidance found in Appendices 4 and 5, Supplement 10 – Appraisal Preparation Guidelines. Note: Costs of purchase, acquisition, and rehabilitation are understood to include associated soft costs that are normally allowable in Section 242 loans.\*

*Reason for Change:* The original language was limited to projects involving purchase of land and improvements thereon or acquisition of a hospital, with no rehabilitation. The regulatory language in Section 242.23 referenced in the revision addresses projects that involve purchase of land and improvements thereon or acquisition of a hospital, and also include rehabilitation.

#### 4. **SUBJECT: EQUITY CONTRIBUTION NOTIFICATION TO HUD**

**Handbook guidance related to § 242.46 Insured advances—building loan agreement.**

Paragraph 1 below is deleted. Paragraph 2 becomes Paragraph 1 and Paragraph 3 becomes Paragraph 2. (Handbook Page 14)

- ~~\*1. No later than ten days prior to the scheduled date of initial endorsement, the applicant hospital must provide evidence to HUD that equity held in cash is included in a restricted fund or account and/or a Letter of Credit to be used for equity is in place.\*~~

*Reason for Change:* Because mortgagees have the responsibility for ensuring that the equity contribution is available at initial endorsement, as provided in Section 242.49 of the regulations, the 10-day notification to HUD imposes an unnecessary administrative burden on the applicant hospital.

#### 5. **SUBJECT: INTEREST RATE FOR SECONDARY FINANCING**

**Handbook guidance related to § 242.77 Liens.**

The text in paragraph 3 (below) is deleted. (Handbook Page 18)

3. ~~\*If secondary financing is supplied by a federal, state, or local government instrumentality, it should be at a lower rate than the HUD-insured mortgage.\*~~

This language is replaced by the following:

3. \*If secondary financing is supplied by a federal, state, or local government instrumentality for a project that will be financed with an FHA-insured loan, it should be at a lower rate than the FHA-insured mortgage.\*

***Reason for Change:** The requirement that secondary financing be at a lower rate applies only at the time of loan origination. It does not apply to any secondary financing that may be put in place during the life of the original loan.*

## **6. SUBJECT: USE OF LETTERS OF CREDIT FOR INITIAL OPERATING CAPITAL OF FOR-PROFIT HOSPITALS**

**Appendix 3 – Pre-Application Guide – Start-Up Hospital Supplement - Initial Operating Capital = to HUD Requirements (Page 37).** Delete the second sentence,

~~\*Letters of credit are usually not an option for for-profit hospitals.\*~~

This language is replaced by the following:

\*If a letter of credit is used, it cannot be backed by the mortgagor or the mortgagor's property and it must be irrevocable. The letter of credit must be issued by, or the liquid assets escrow must be placed with, a financial institution that:

- Has assets of not less than \$1,000,000,000;
- Is organized under the laws of the United States or a state thereof and is regulated and examined by the Comptroller of the Currency, the Federal Deposit Insurance Corporation, or the Federal Reserve Board; and
- Has a long-term bank deposit rating of A-1 or better by Moody's Investor Service or A+ or better by Standard and Poor's.\*

***Reason for Change:** The regulations [242.49(b)] state that the mortgagee shall be responsible to HUD for collection under the letter of credit. For this reason, for-profit mortgagors pose no higher risk than nonprofit mortgagors with respect to the letter of credit. The replacement language is a statement of existing policy as a reminder to participants. Also, this change makes Section 242 consistent with Section 232 policy.*

## **7. SUBJECT: LIMITATION ON INITIAL ADVANCE FOR PURCHASE PRICE**

**Appendix 4, Applicant's Guide, and Appendix 5, Applicant's Guide – Critical Access Hospitals.** In Supplement 2, HUD 92013 Instructions, Line C.12 – Interest, **Page 2-5**, Estimated initial draw amount listing, the following language is deleted:

- 1) ~~\*90% of the lesser of (i) HUD's estimate of the sum of the fair market value of the existing land and the replacement cost of existing improvements for land, property and equipment to be purchased or (ii) the purchase price of the land, property and equipment to be purchased. (C.31 and D.3)\*~~

This language is replaced by the following:

- 1) \*Funds needed for the purchase of property, not to exceed the lesser of (i) HUD's estimate of the sum of the fair market value of the existing land and the replacement cost of existing improvements for land, property and equipment to be purchased or (ii) the purchase price of the land, property and equipment to be purchased. (C.31 and D.3)\*

*Reason for Change: The regulations at 242.7 and 242.23 establish a maximum loan-to-value of 90 percent. This maximum applies to the entire loan, but not to individual components of the loan such as property purchased for the project.*

## **8. SUBJECT: CAPITALIZATION OF MORTGAGE INSURANCE PREMIUM.**

**Appendix 4, Applicant's Guide, and Appendix 5, Applicant's Guide – Critical Access Hospitals.** In Supplement 2, HUD 92013 Instructions, **Pages 2-5 to 2-6**, Line C.15 – Mortgage Insurance Premium, the following language is deleted:

~~\*The Mortgage Insurance Premium that may be paid from Loan funds is limited to the cut-off date which may be up to 60 days past the date of substantial completion. The formula to calculate the MIP that maybe included on line C.15 is basically: (Insured Loan Amount) X (annual rate for MIP) X (number of months in the construction period / 12) rounded down to the nearest whole dollar. This amount is then tested for 223(a)(7) status and if so reduced for the lower rate in the first year.\*~~

This language is replaced by the following:

\*When applying for insurance of advances, the Mortgage Insurance Premium that may be capitalized in the loan may equal up to 1 year of MIP payments for each year or partial year of the construction period. However, at final endorsement of the loan, the amount of MIP that can actually be paid with loan proceeds will be limited to MIP actually owed as of the cost certification cutoff date, which may be up to 60 days past the substantial completion date of the project.\*

*Reason for Change: With this change, Section 242 will be consistent with the other healthcare and multifamily programs in its treatment of MIP, and the process will be administratively simpler than the process currently described in the handbook.*

**9. SUBJECT: LEASED PROPERTY**

**Appendix 4, Applicant’s Guide, and Appendix 5, Applicant’s Guide – Critical Access Hospitals.** In Supplement 2, HUD 92013 Instructions, **Page 2-12**, Line E-1 – Information on Leased Property, Paragraph b), the following language is deleted:

~~\*99 if the lease will be for a minimum term of (i) 99 years following initial endorsement or (ii) 50 years with an option for the Mortgagor to renew the lease for an additional 49 years following initial endorsement.\*~~

This language is replaced by the following:

\*99 if the property is held under a lease (i) having a period of not less than 99 years which is renewable or (ii) having a period of not less than 50 years to run from the date the mortgage is executed with an option for the Mortgagor to renew the lease for an additional 49 years following its initial 50-year term.\*

*Reason for Change: The current language related to ground leases does not accurately reflect what is in the statute (Section 207 of the NHA).*

**10. SUBJECT: TYPE OF APPRAISAL**

**Appendix 4, Applicant’s Guide, and Appendix 5, Applicant’s Guide – Critical Access Hospitals, Supplement 10, Appraisal Preparation Guidelines, Page 10-3.**

Delete the content in the “Type of Appraisal” section and replace it with the following:

**TYPE OF APPRAISAL**

\*For each appraisal, HUD requires a “Replacement Cost” estimate and a “Market Value” estimate prepared according to USPAP guidelines. The two valuations should be separate and distinct valuations and be presented within the appraisal supplied to HUD.

For the purpose of calculating the statutory maximum Loan-To-Value, HUD will consider the Replacement Cost valuation. However, HUD may limit LTV after consideration of the creditworthiness of the applicant and the Market Value estimate.

NOTE: Section 242 uses a Market Value appraisal when selling or disposing of an asset, as in the case of calculating adequacy of collateral for a release of lien.\*

*Reason for Change: The prior language was unnecessarily long and confused some readers.*

## **11. SUBJECT: MORTGAGE RESERVE FUND**

### **Appendix 4, Applicant's Guide, and Appendix 5, Applicant's Guide – Critical Access Hospitals, Supplement 13, Page 1, Mortgage Reserve Fund.**

Delete the lead-in narrative under the title **SUPPLEMENT 13 –MORTGAGE RESERVE FUND** in each of the Applicant's Guides and replace it with the following:

\*The Mortgage Reserve Fund (MRF) is a reserve fund to provide monies in a client hospital's financial emergency to cure or prevent a default, engage a consultant, implement a turnaround plan, or take other measures to deal with the financial emergency. Prior approval by HUD is required for these expenditures. Required fund balances of the MRF are tied directly to the debt service payments for the FHA-insured mortgage. The MRF will be held as a trust fund by the mortgagee of record or a trustee acceptable to the mortgagee and HUD. Mortgagors are required to make contributions to the MRF on a quarterly basis, unless the mortgagor receives cost-based reimbursement, in which case monthly contributions are required.

Unless OHF determines that the mortgagor's credit profile warrants an alternative schedule, the MRF for 25 year mortgage terms will be constructed to achieve a minimum balance equal to 12 months and 24 months of FHA-insured mortgage debt service at 5 and 10 years, respectively, from the commencement of amortization. Minimum year-end balance expectations are calculated by simple arithmetic, with 2.4 months' worth of FHA insured mortgage debt service accruing at every annual anniversary of commencement of amortization, for the first 10 years. Minimum year-end balance for the following 5 years remains at 24 months of FHA insured mortgage debt service, and distributions without HUD approval are prohibited.

Unless a mortgagor is placed on OHF's Credit or Priority Watch list, in the distribution phase (years 16-25), distributions are permitted without HUD approval subject to a minimum yearly anniversary balance that drops 2.4 months' worth of FHA insured mortgage debt service until reaching zero in year 25. For facilities on Credit or Priority Watch Lists, OHF approval is always required for MRF distributions. For shorter term mortgages and 223(a)(7) mortgages with extended amortization, OHF adjusts this schedule accordingly. Upon termination of insurance, the balance of the MRF shall be returned to the mortgagor, provided that all obligations to HUD have been met.

The MRF agreement is provided for your information on the following pages. Contact your account executive to obtain a mortgage reserve fund schedule.

**Also see §242.14 Mortgage reserve fund and Handbook guidance related to §242.14 Mortgage reserve fund (MRF).\***

***Reason for Change:** Currently there are two different narratives – one for standard acute care hospitals and another for Critical Access Hospitals – suggesting that there are differences in the rules for the MRF, when in fact the two narratives are saying the same things in different words. One narrative applying to both types of hospital avoids confusion.*

## 12. SUBJECT: SECTION 223(A)(7) CONSTRUCTION COMPONENT

**Appendix 6 – Section 223(a)(7) Refinancing, Page 1.** Delete the text under the Construction Component section and replace with the following:

### 1. Construction Component

\*The proceeds of a loan insured under Section 223(a)(7) may include “costs, as determined by HUD, of improvements, upgrading, or additions required to be made to the property” (*see 24 CFR 242.91(a)(1)(ii)*). HUD expects that Section 223(a)(7) authority will be used primarily for refinancing the existing Section 242-insured loan in order to lower the hospital’s debt service expense. Further, HUD expects that any construction activities financed via Section 223(a)(7) will relate to urgently needed modifications to the property, discussed below.

- a. HUD’s Office of Architecture and Engineering shall review any proposed improvements, upgrading, or additions to be made to the hospital structure. HUD will approve for inclusion in the insured mortgage only those construction activities that are necessary to correct defects that pose a risk of imminent disruption to hospital operations; threaten the life and safety of building occupants; cause the hospital to be in violation of state or local codes; or threaten to cause serious financial harm to the hospital if not corrected in the short term. Construction activities that could be prioritized for completion at a later time are not eligible for financing by the insured mortgage.
- b. If the proposed construction component (or total hard costs) would equal 20 percent or more of the mortgage amount, HUD cannot consider the use of Section 223(a)(7) for refinancing and construction combined. The refinancing and the construction project may be accomplished in one of two ways: (1) A new Section 242 loan may be used to refinance the existing loan and to finance the construction project, or (2) two loans may be used – a 223(a)(7) for the refinancing and a 241 for the construction project.
- c. If the proposed construction component (or total hard costs) would equal less than 20 percent of the mortgage amount, it may be included in a Section 223(a)(7) loan, provided the conditions in sub-paragraph 1a. above are met.
- d. If there is a construction component, the application must indicate if insurance of advances will be required or if the costs of the construction component will be borne by the mortgagor and included in the final mortgage loan (insurance upon completion). HUD expects that insurance of advances will be needed in rare cases, if at all.\*

***Reason for Change:*** *It was not the intent of Congress to allow the Section 223(a)(7) refinancing program to be used for construction (other than urgently needed modifications required to keep the facility operational). Otherwise, HUD does not have the authority to insure construction loans under Section 223(a)(7).*

### 13. CONSTRUCTION GUIDE CLARIFICATIONS

**Appendix 8 – Construction Guide.** The following changes have been made to the Construction Guide:

**Part I 1.b. Page 1, Typical Steps in OAE Review.** Eighth bullet has been modified:

- Must have current certified metes and bounds survey of all properties included in the mortgage with legal description and legal opinion stating that the legal description submitted reflecting the certified land survey is the property included in the FHA-242 project \*and whether it is owned in fee simple or has a leasehold interest, etc. Note: A draft survey will suffice until just prior to the closing date upon which OAE will review and approve the finalized certified survey.\*

*Reason for Change: Having a current certified survey much time prior to initial endorsement has been problematic since mortgagors are receiving HUD's comments up to and on the closing date. The requirement of having a certified survey at a significant time prior to initial endorsement creates significant delays in getting to closing. This increases the cost to hospitals. Therefore in the interest of saving time and money, OAE will review a draft and will be issued a certified survey just prior to the closing.*

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**Part I 1.b. Pages 1 and 2, Typical Steps in OAE Review.** Several bullets have been enhanced by plus symbols (+). A note has been added to the end of the bullets as follows:

\*Note: These are typical requirements for an FHA-242 project. Check with the OAE Project Manager for the necessity of those items marked with a plus symbol (+) for Section 223(a)7, 241 or 223(f) loans as some may not be necessary in all cases.\*

*Reason for Change: For refinance loans, many requirements are not applicable or are modified for refinancing loans depending upon the characteristics of the proposed project. For the sake of clarity, we have noted that the list is for a typical FHA-242 project and have noted that in those cases marked with a plus symbol, the individual requirement may or may not be applicable and needs to be worked out on an individual project basis with the applicant and OAE.*

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**Part I 2.b. Page 3, Construction standards and minimum requirements.** The fifth sentence is modified as follows:

HUD Form 92442 is required to be utilized for lump sum construction contracts \*as modified for Section 242 requirements (including the FHA-242 retainage and liquidated damage requirements).\*

**Part I Item 2.e.(3), Page 6.** The last sentence is modified as follows:

If a design-build construction contract is anticipated, \*the HUD acceptable form of agreement must be modified to meet the Section 242 requirements.\*

*Reason for Changes: HUD Form for lump sum contract and AIA Form for design-build by themselves cannot be utilized since they do not exactly meet the FHA-242 requirements and need to be modified. Adding the extra clause helps to manage contractor expectations by providing more detailed guidance.*

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**Part I Item 2.d.(1) Page 4, First Stage-Schematics.** The seventh sentence has been modified as follows:

The Owner's Representative (required on all construction projects) \*if contracted independently,\* must submit his/her contract with the Owner for OAE review and approval.

*Reason for Change: There was ambiguity as to whether this party must be hired as an independent consultant or not. While HUD does require an Owner's Representative on all its construction projects, the Owner's Representative may be from the Owner's in-house staff or may be hired as an independent consultant. If the independent consultant is hired, OAE will need to review that contract. If the Owner's Representative is a member of the in-house hospital staff such a contract will not be required. The clause offers clarity to the statement.*

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**Part I Item 2.e.(3) Page 6, Form of owner-contractor agreement.** The second sentence is revised to state:

\*If a construction manager contract is anticipated, a Part B Construction Contract noted in Appendix 8 –Exhibit 4 must be utilized.\*

*Reason for Change: OAE Handbook 2.4 no longer exists.*

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**Part I Item 2.e. Page 7, Mandatory Requirements to be Specified** has been renumbered to Part I Item \*2.f.\*

*Reason for Change: Typographic error.*

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**Part I Item 2.e.(3) [revised to 2.f.(3)] Page 8, Wage determination applicability.** A last sentence has been added to paragraph (b):

\*This is applicable to all HUD FHA-242 construction contracts.\*

**Part I Item 7. Page 11, LABOR STANDARDS.** Add:

\*Also, see Part 1, Item 2.f. Mandatory Requirements to be Specified\*

**Part II Item 2.i(8), Page 8, Pre-Bid Conference.** The third sentence has been modified as follows:

The requirements of Executive Order 11246, Equal Employment Opportunity (EEO), and Federal Labor Standards \*(See Part 1, Section 7)\*, should be emphasized at the pre-bid conference.

**Part II Item 3.d. PREPARING CONSTRUCTION MANAGEMENT AGREEMENTS – HUD Provisions for Labor Standards and Equal Employment Opportunity, Page 13.** Add the last sentence:

\*See Part 1, Section 2.f.(2) Labor Standards.\*

*Reason for Changes: These statements help clarify that all of these requirements apply to all construction contracts since there appears to have been ambiguity regarding this issue.*

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**Part I Item 2.e.(4) [revised to 2.f.(4)] Page 9, General conditions.** Paragraph (b) has been modified as follows:

(b) Representatives of the Secretary, HUD, \*the Lender,\* the State agency and the local authority shall have access to the work site.

Paragraph (d), item 3 (**Page 9**) has been modified to read:

3. Property damage, \*i.e. Builder’s Risk (\$100,000/\$300,000);\*

*Reason for Change: It is critical that the Lender have access to the construction work site as well as the other parties. Builder’s Risk Insurance needed to be added as it is a requirement for Initial Endorsement.*

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**Part I Item 8. Page 12, CHANGE ORDERS.** The second sentence has been revised to read,

Request for approval of change orders during a construction project must come directly from the Owner, \*copying the Lender,\* ...

After the last sentence, add a sentence to read,

\*The Lender must approve all change orders as well.\*

*Reason for Change: The Lender must be totally involved in the change order review and approval process to be consistent with the Building Loan Agreement.*

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**Part I Item 9. Page 12, SUBSTANTIAL COMPLETION DATE.** The section is revised to read,

\*The date of substantial completion is established by the owner, the architect, the contractor and OAE. After substantial completion, the borrower must submit a cost certification. These costs will be reviewed by HUD/OAE.\*

*Reason for Change: The paragraph needed clarification and needed to be written in a more logical manner to allow for a more orderly project closeout.*

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**Part I Item 10. Pages 12 and 13, OAE FINAL INSPECTION.** In paragraph (a), revise the last word in the sentence from “~~applicant~~” to \*owner\*. In paragraph (b), also revise “~~applicant~~” to \*owner\*.

**Part 1 Item 11. Page 13, EQUIPMENT.** In paragraph (a), the word “~~applicant~~” has been replaced with \*owner\*.

*Reason for Change: In the industry, the as-built drawings go to the owner. The use of the word “applicant” as was originally written would imply the as-built drawings would go to the Lender since they are the “applicant” on the HUD-92013 form and this would be inappropriate.*

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**Part 1 Item 11. Page 13, INCOMPLETE ON-SITE AND OFF-SITE FACILITIES.** In the first sentence, change the word “~~mortgagee~~” to \*Lender\*.

**Part 1 Item 15. Pages 16 through 18, 11-STEP CONSTRUCTION DRAW PROCEDURE, STEPS 2, 3, 5, 10 and 11.** In lieu of the term “~~Mortgagee,~~” the terms \*Lender\* have been utilized.

**Part II Item 1.b. Page 1, Development of the Construction Management Process.** In the first sentence of the second paragraph, the word “~~sponsor~~” has been changed to \*Lender\*.

*Reason for Changes: There was a request to utilize the same word for the mortgagee, lender and mortgage banker throughout the document and lender was chosen for the sake of consistency.*

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**Part 1 Item 13. Page 15, FINAL CONSTRUCTION CLOSEOUT BY OAE.** This section has been revised as follows:

\*As part of the closeout process, OAE will need to complete the OAE Final Report on Construction requiring HUD to process the following documents:

- a. Executed copy of the Certificate of Substantial Completion (AIA Form F704)
- b. Certificate of Release of Liens (AIA Form G706)
- c. Consent of Surety for final Payment (AIA G707)
- d. Architect’s and Contractor’s Final Certificate for Payment
- e. Architect’s letter asserting compliance with the State Department of Health or Authority Having Jurisdiction (AHJ)

- f. Certification that all change orders have been included in d. above.
- g. HUD Form 92330 – Mortgagor’s Certificate of Final Costs with CPA audit opinion attached
- h. Either HUD form 92330-A Contractor’s Certification of Final Costs with CPA audit opinion attached (CM project or lump sum project where identity of interest exists) or Contractor’s letter certifying as to final costs (for design-build and lump sum projects.)
- i. Certificate of Occupancy from approving building authority\*

The last sentence is revised as follows:

\*Final recommendation of OAE approval to close out the construction project is transmitted in writing to the OHF Account Executive assigned to the FHA-242 project.\*

*Reason for Changes: The OAE Final Inspection Report form needed to be separated out from the documentation required directly from the owner to clearly define exactly what needed to come from the owner. Other items were more clearly defined so they would not be considered separate and distinct documents.*

**Part I Item 15. Pages 15 and 17, 11-STEP CONSTRUCTION DRAW PROCEDURE**

**Step 1** is modified as follows, Two original draw packages are prepared by the \*Lender or loan servicer with information gathered from the Hospital, Contractor, and the Project Architect among other parties.\*

**Step 3, Item 2** is modified as follows, \*The designated construction draw processor in the OHF.\*

*Reason for Changes: This clarifies the hierarchy of who prepares, who assists in preparing, and who finally approves the draw packages.*

**Part II Item 1.b. Pages 1 and 2, Development of the Construction Management Process.** The following has been added to the end of the third paragraph:

\*The CM contract may include a statement that states it is only a valid contract subject to a successful FHA-242 Initial Endorsement. In some states execution by both parties starts the clock on a mechanic’s lien and this would compromise HUD’s prime lien position. Therefore, the clause requiring a successful endorsement for it to be valid would not allow the lien clock to start.\*

*Reason for Change: HUD must have signatures from both the owner and the contractor in order to have a fully executed contract for it to be valid. This will guarantee a firm fixed price for a fixed scope of work completely necessary for a commitment and an initial endorsement. The new wording will allow for both HUD and the Owner to meet their individual requirements to proceed with a firm position.*

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**Part II Item 3.a. Page 11, Sample Forms.** Add a second sentence to the second paragraph as follows:

\*HUD will review draft agreements with clearly defined minor modifications and will accept them providing they meet minimum FHA-242 requirements. See part II, Section 1b.\*

*Reason for Change: There needed to be clarification as to whether HUD will accept a contract other than the standard form.*

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**Part II Item 3.f. Page 14, Retained Percentage.** In the second paragraph, the second sentence is revised to state:

\*Upon written approval of HUD, the Lender, the Surety, the Architect and the Owner, further retainage may not be required.\*

*Reason for Change: The Lender also needs to be part of the approval process for retained percentage.*

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**Part II Item 3.g. Page 14, Liquidated Damages.** The second paragraph shall be revised as follows:

Liquidated damages will be assessed in the Section 242 Program \*at the rate of \$.09/\$1,000 of construction cost\* and approved by HUD.

*Reason for Change: HUD sets the liquidated damages formula and not the Lender.*

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**Part II Item 3.i. Page 14, Performance and Payment Bonds.** The first paragraph shall be revised to read as follows:

Upon notice that the Owner elects to proceed with PART B of the Construction Manager Agreement, the Construction Manager shall post \*draft\* performance and payment bonds each in the amount of 100% of the GMP.

The following sentence is added to the last paragraph: **\*Finalized fully endorsed HUD Performance and Payment Bonds are required for Initial Endorsement.\***

*Reason for Change: Hospitals do not want to pay for Performance and Payment Bonds that are fully executed prior to closing due to the cost of the bonds. Fully executed Performance and Payment Bonds will only be required at initial endorsement when loan dollars may be utilized for payment.*

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**Part II Item 3.j. Page 15, Construction Manager’s Liability Insurance.** Add to the end after the last bullet:

\*Evidence of Builder’s Risk Insurance must be delivered at the Initial Endorsement.\*

**Part II EXHIBIT 4 (CM AGREEMENT) PART B, Page 9, Article 2.7.2. Insurance.** Add to the end of paragraph d.:

\*Evidence of Builder’s Risk Insurance must be made available to HUD prior to HUD-242 initial endorsement.\*

*Reason for Changes: There was no requirement for Builder’s Risk Insurance per se.*

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**Part II EXHIBIT 4 (CM AGREEMENT) PART B, Page 8, Article 2.6.2 Contract Awards.** Add to the end:

\*Note: If construction does not begin within 90 days of initial endorsement, any modifications to a wage decision that occur after initial endorsement become applicable to the construction work, unless DOL approves a request from HUD for an extension. See DOL regulations at 29CFR 1.6(c)(3)(ii) and (iv). In the less likely case of a “project” wage determination, issued upon request for an individual project, the wage determination is effective for 180 days from the date of the determination. [29 CFR 1.6(a (1))].\*

*Reason for Change: It was requested that these criteria be incorporated into Part B of the CM contract.*

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**Part II EXHIBIT 4 (CM AGREEMENT) PART B, Article 11, Page 17, CONSTRUCTION MANAGER'S COMPENSATION.** In the second paragraph of Article 11.5.a, change “Mortgagee” to \*Lender\*.

*Reason for Change: There was a request for consistency in language throughout the handbook.*

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**Part II EXHIBIT 4 (CM AGREEMENT) PART B, Article 16, Page 19, LIQUIDATED DAMAGES.** At the end of the first paragraph at the top of the page add:

\*This amount is based upon \$.09/\$1,000 of construction cost in the contract, ie. GMP.\*

*Reason for Change: There was a request to have the HUD FHA-242 formula for liquidated damages be included in Part B.*

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**Part II EXHIBIT 4 (CM AGREEMENT) PART B, Article 16, Page 19, LIQUIDATED DAMAGES, item b.** Change N.B. to read:

\*The above information for liquidated damages is provided for guidance only and should be discussed and approved by HUD.\*

*Reason for Change: The amount of liquidated damages formula is set and approved by HUD.*

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**Part II EXHIBIT 5, Page 1, PERFORMANCE AND PAYMENT BOND SAMPLE FORMS.**

Add note at the top:

\*Note: For FHA-242 projects only HUD format of Performance and Payment Bonds are acceptable.\*

*Reason for Change: Industry standard is typically on an AIA form but HUD requires its own forms from HUDCLIPS.*

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**Part II EXHIBIT 6 INVITATION TO BID FOR CONSTRUCTION MANAGEMENT SERVICES.** Under the Bidders for Role of Construction Manager section, **Page 3 (of Invitation to bid)**, the last paragraph shall state:

\*Bidders are cautioned that FHA-242 projects require that all construction contracts between the Owner and the Construction Manager and between his contractors, subcontractors and lesser tiers of subcontractors for work on this Project shall require the current edition of HUD-2554 Supplementary Conditions of the Contract for Construction.\*

*Reason for Change: The AIA form 201/SC is not acceptable for use on HUD FHA-242 projects.*

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**Part II EXHIBIT 8, Page 1, SAMPLE PRE-QUALIFICATION STATEMENT FOR SUB CONTRACTORS.** The double asterisk note is revised as follows,

\*\*Pre-qualifications shall be submitted \*for review and approval\* to the Office of Architecture & Engineering prior to issuance.

*Reason for Change: OAE must review and approve suggested pre-qualification statements to insure that bids are not unduly restrictive.*

**IMPLEMENTATION**

This transmittal is effective immediately. These changes will be incorporated into the existing handbook on HUDCLIPS at HUD.GOV.

If there are any questions regarding this Transmittal, please contact John Whitehead at (202) 402-5790.

Persons with hearing or speech impairments may access this number via TDD/TTY by calling 1-877-TDD-2HUD (1-877-833-2483).

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Carol J. Galante  
Assistant Secretary for Housing-  
Federal Housing Commissioner

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