
CHAPTER 22. PREPAYMENTS AND VOLUNTARY TERMINATIONS

SECTION 1. INTRODUCTION

22-1. General

A contract of mortgage insurance may be terminated either by prepayment in full of the insured project mortgage or by acceptance of a request for voluntary termination made jointly by the mortgagor and mortgagee. This Chapter provides guidance and procedures when a request for termination by prepayment in full or by voluntary termination is made. The Chapter does not address partial prepayments of the mortgage.

Projects covered by this chapter may or may not be insured under a program which restricts prepayment in full of the mortgage. When asked to do so by Headquarters, Field Office Asset Management/Loan Management and Legal staff are to review the Note and Mortgage to verify whether prepayment in full is restricted.

22-2. Applicability

- A. This chapter does not apply to those projects covered by Title II of the Housing and Community Development Act of 1987 and Title VI of the Cranston-Gonzalez National Affordable Housing Act of 1990 or various other projects as shown below where the mortgage is:
1. Insured or HUD-held under the Section 221(d)(3) Market Rate Program, if the project receives Rent Supplement or project-based Section 8 assistance; or
 2. Insured or HUD-held under the Section 221(d)(3) Below Market Interest Rate (BMIR) program; or
 3. Insured, assisted, or HUD-held under the Section 236 Program; or
 4. A Purchase Money Mortgage originated by HUD with respect to a project which, prior to HUD's acquisition, was insured under one of the programs referred to in 1, 2, or 3 above.

HUD Field Offices, mortgagees, and mortgagors are to follow instructions issued by the Office of Multifamily Housing Preservation and Property Disposition for any project that falls into one of the four categories above.

- B. This Chapter does apply to HUD-insured and HUD-held multifamily projects with moderate prepayment restrictions and no prepayment restrictions as follows:
1. There are mortgage insurance programs that generally have moderate prepayment restrictions.
 - a. Section 207/223(f), Purchase/Refinancing of Existing Multifamily Projects (NOTE: This category applies to mortgages where a commitment was issued after October 8, 1980; where a commitment was issued prior to October 8, 1980, the regulations in place at the time of commitment should be referred to in order to determine if a prepayment prohibition exists.)
 - b. Section 221(d)(3) Market Rate with non-profit mortgagors and with no Rent Supplement or Section 8 Assistance
 - c. Section 231, Housing for the Elderly with Nonprofit Mortgagors (Public and Private)
 - d. Section 232, Nursing Homes and Intermediate Care Facilities with Nonprofit Mortgagors
 - e. Section 242, Hospitals with Nonprofit Mortgagors (NOTE: This is only applicable to mortgages for which the commitment for insurance was issued prior to June 16, 1988, the effective date of the amended 24 CFR 242.51.)
 - f. Title XI - Mortgage Insurance for Group Practice Facilities

2. There are programs that generally have no

mortgage prepayment restrictions,

- a. Section 207, Multifamily Rental Housing
 - b. Section 213, Cooperatives
 - c. Section 220, Urban Renewal
 - d. Section 221(d)(3), Market Rate with Limited Dividend Mortgages and without Rent Supplement or project-based Section 8
 - e. Section 221(d)(4), Market Rate, Moderate Income Families
 - f. Section 231, Elderly Housing with Profit-motivated Mortgages
 - g. Section 232, Nursing Homes and Intermediate Care Facilities with Profit-motivated mortgages
 - h. Section 234, Condominiums
 - i. Section 241, Supplemental Mortgages
 - j. Section 242, Hospitals with any profit motivated mortgages and all nonprofit mortgages with mortgages for which an insurance commitment was issued on/after June 16, 1988
 - k. Section 608, Veteran Housing
 - l. Title X, Land Development
- C. There is one program that may have strict, moderate, or no mortgage Prepayment restrictions: Section 207/223(c), "Formerly HUD-owned Projects." These are projects that were owned by HUD at some point in time and subsequently sold. When these projects were sold by HUD, HUD often provided financing with a Purchase Money Mortgage, or a "PMM." When a Purchase Money Mortgage is placed on a project upon its sale to a new owner, HUD itself is the mortgagee and the new Purchase Money Mortgage is initially HUD-held. Some of these Purchase Money Mortgages continue to be HUD-held; others may have been sold by HUD, with mortgage insurance, to investing

mortgagees. Projects with PMMs commonly retain the prepayment restrictions that were characteristic of the project when it was originally processed for mortgage insurance.

1. For example, if a project was originally processed and built as a non-profit Section 236 project, was acquired by HUD, was sold by HUD and financed by HUD with a Purchase Money Mortgage, the new Purchase Money Mortgage normally could not be prepaid. The project in this example is of the type cited in paragraph 22.A.4. of this Chapter and prepayment of its mortgage is not covered by this Chapter.
2. For another example, if a project was originally processed and built as a profit-motivated project under Section 221(d)(4), was acquired by HUD, was sold by HUD and financed by HUD with a PMM, the new PMM would normally not contain prepayment restrictions. Prepayment of the mortgage in this example is covered by this Chapter.

When requests for prepayment of a PMM Note or for voluntary termination of mortgage insurance are received by either the HUD Field Office or by HUD Headquarters, the controlling instruments (Note, mortgage, and Regulatory Agreement) and any corollary documents such as a Use Agreement must be examined in each instance to determine whether or not prepayment restrictions exist. Once this determination has been made, the prepayment/voluntary termination request will be acted upon according to the procedures described in this Chapter 22.

22-3. Glossary

Partial Prepayment - Payment in part of the principal amount of the mortgage note in advance of the established amortization schedule. (Partial prepayments which are the result of a partial release of the mortgage security are discussed in detail in Chapter 16, Partial Release of Security.)

Prepayment in Full - Payment in whole of the principal amount of the mortgage note in advance of expiration of the term of the mortgage note.

Voluntary Termination - The cancellation of HUD mortgage insurance made at the joint request of the mortgagee and the mortgagor and with HUD approval.

SECTION 2. REQUESTS FOR TERMINATION OF MORTGAGE INSURANCE

22-4. If the mortgage is insured, the mortgagor will first notify the mortgagee, consistent with the terms and conditions of the mortgage insurance, that the mortgagor wishes to prepay the mortgage in full or seek voluntary termination of the insurance. If the mortgage is HUD-held, the mortgagor should direct its notification to the appropriate HUD Field Office. The loan documents include time frames for mortgagor notification to the mortgagee (generally, at least 30 days) and any additional charges to be assessed by the mortgagee if the mortgagor chooses to prepay (established by the mortgagee).

22-5. If the mortgagee determines that the mortgagor's request meets loan requirements and agrees to the mortgagor's request, the mortgagee must prepare Form HUD-9807, "Request for Termination of Multifamily Mortgage Insurance," (Appendix 1) based on the following guidelines:

- A. If the mortgage loan and insurance contain no prepayment restrictions, the mortgagee:
 - 1. Prepares the form and required attachments;
 - 2. Obtains the mortgagor's signature on the form in cases of voluntary termination; and
 - 3. Sends the documents to HUD Headquarters at the address indicated on the front of the Form.
- B. If the mortgage insurance does contain prepayment restrictions, prior approval from HUD is required before the form may be prepared. (See Section 3 below.)

SECTION 3. TERMINATION BY PREPAYMENT IN PULL OR VOLUNTARY TERMINATION OF MORTGAGE INSURANCE WITH PREPAYMENT RESTRICTIONS

- 22-6. When prepayment restrictions exist, the mortgagee must request HUD approval of the proposed prepayment in full prior to completion of Form HUD-9807. Programs described in paragraph 22-2.B.1. are covered by this Section. For projects described in paragraph 22-2.B.1. (moderate prepayment prohibitions), the mortgagor's signed narrative request must be submitted by the mortgagee to the appropriate address on the back side of the Form. Program-specific guidance is provided below.
- 22-7. Some projects insured under Sections 231, 232, 242, and Title XI are described in paragraph 22-2.B.1. as having moderate prepayment restrictions. For these projects with insured mortgages, the mortgagee should send the mortgagor's signed request for prepayment/voluntary termination to the Headquarters Office of Multifamily Housing Management which will normally forward it to the HUD Field Office for review. Mortgagors with a HUD-held mortgage in this category should send their written requests directly to the HUD Field Office. The Asset management/Loan Management Branch Chief will review each request. Under normal circumstances the Branch Chief may issue approval of prepayment or voluntary termination by sending a letter of authorization to the mortgagee, with a copy of the letter to the mortgagor, the HUD Regional Office, the Office of Multifamily Housing Management, and the Office of Mortgage Insurance Accounting and Servicing (MIAS) in HUD Headquarters. If there are matters indicating that approval should not be granted, the Field Office Housing Management Division Director should forward a memorandum through the HUD Regional office to the office of Multifamily Housing Management outlining the issues and making a recommendation about conditionally permitting or prohibiting prepayment or voluntary termination. HUD Headquarters will issue the decision letters in these cases, which are expected to be relatively rare. If the mortgage is HUD-held, the above procedures should be followed except that actions involving the mortgagee are omitted.
- 22-8. Section 207/223(f) Insurance Program. For all insurance commitments made under this program after October 8, 1980, HUD may not approve prepayment for five years following final endorsement of the mortgage insurance unless one of the following conditions exists:

- A. The mortgagor has agreed to maintain the property as rental housing for the remainder of the five year period. To obtain HUD approval for prepayment for this condition, the mortgagor must submit a letter stating the reasons for the request and must provide HUD three completed, executed, and notarized copies of the Rental Use Agreement which has been authorized by the HUD Office of General Counsel. This Rental Use Agreement is contained in Appendix 2 of this Chapter.
 - B. The project is being converted to a condominium or cooperative and the conversion is sponsored by a tenant organization that represents a majority of the tenants.
 - C. HUD has determined that there is an adequate supply of low and moderate income housing in the community without this project. The Field Office Asset Management/Loan Management Branch Chief should obtain the assistance of its Economic and Market Analysis Division in making this decision.
 - D. HUD has determined that continuing the property as rental housing would have an undesirable and deleterious effect on the neighborhood.
- 22-9. For those projects with moderate prepayment restrictions, after the mortgagor's request is received by the Office of Multifamily Housing Management in Headquarters, that Office will normally contact the appropriate HUD Field and Regional Offices for additional comments. When these comments, and the Rental Use Agreements (if the latter are applicable), have been received by Headquarters they will be reviewed and a decision will be issued whether to permit prepayment. If the Use Agreements are contemplated, they will be executed and then returned to the Field Office for recording and distribution.
- 22-10. After the mortgagee receives a letter from either the HUD Field Office or from HUD Headquarters authorizing prepayment of the Note or voluntary termination of mortgage insurance, the mortgagee should complete preparation of the Form HUD-9807 by signing the Form and obtaining the mortgagor's signature on the Form. The mortgagee should then send the Form HUD-9807

together with HUD's letter authorizing the prepayment/voluntary termination to the address on the front of the Form.

- 22-11. Prepayment Penalties and Lockout Provisions. Reference is made to Mortgagee Letter 87-4 dated January 12, 1987, and Mortgagee Letter 87-9 dated February 20, 1987. Some mortgages may contain lock-out provisions and prepayment penalties. Where this is permitted, language similar to the following should be contained in the Mortgage Note:

"Notwithstanding any prepayment prohibition imposed and/or penalty required by this Note with respect to prepayments made prior to _____, 19____, enter first date on which prepayments may be made with a penalty of one percent or less the indebtedness may be prepaid in part or in full without the consent of the mortgagee and without prepayment penalty if HUD determines that prepayment will avoid a mortgage insurance claim and is therefore in the best interest of the Federal Government."

Where these restrictions exist and the mortgagee does not waive its optional prepayment or lockout penalty provisions, HUD would consider exercising an override of a mortgagee's prepayment lock-out or penalty provision only if all four of the following conditions are met:

- a. The project mortgagor has defaulted and HUD has received notice of such default as required by 24 CFR Section 207.256 (full insurance cases) or Section 251.810, 252.810, or 255.808 (co-insurance cases).
- b. HUD determines that the project has been experiencing a net income deficiency that was not caused solely by management inadequacy or lack of owner interest and that is of such a magnitude that the mortgagor is currently unable to make required debt service payments, pay all project operating expenses, and fund all required reserves.
- c. HUD finds there is a reasonable likelihood that the mortgagor can arrange to refinance the defaulted loan at a lower interest rate or otherwise reduce the debt service payments through partial prepayment.
- d. HUD determines that refinancing the defaulted loan at a lower rate or partial prepayment is necessary to

restore the project to a financially sound condition and to avoid an insurance claim.

- 22-12. If a mortgagor desires HUD's override, it must make its written request to the HUD Field Office with jurisdiction over the project. The mortgagor must provide sufficient information to enable HUD to make the determination stated in conditions b, c, and d in paragraph 22-11.
- 22-13. Asset Management/Loan Management Branch Chiefs must be satisfied that mortgagors in these circumstances did not intentionally cause a default in order to obviate prepayment penalties or lockout provisions. After performing the review required by paragraph 22-11 above, Asset Management/Loan Management Branch Chiefs should prepare written comments supporting their conclusions and recommendations and forward these comments through the HUD Regional Office to the Operations Division, Office of Multifamily Housing Management in HUD Headquarters. Headquarters will make the decision about overriding the prepayment lockout or penalty provision and will inform the mortgagee, the mortgagor, and the respective HUD Field and Regional Offices.

SECTION 4. PREPAYMENTS AND TERMINATIONS WHEN THERE ARE NO RESTRICTIONS

- 22-14. When there are no prepayment restrictions, the mortgagee sends the fully signed Form HUD-9807 to the Office of Mortgage Insurance Accounting and Servicing in HUD Headquarters at the address shown on the form. That Office forwards a copy of the form to the Office of Multifamily Housing Management, Operations Division, which will normally contact the appropriate HUD Field Office to verify that there are no prepayment restrictions for the particular project. When this is confirmed, the Office of Multifamily Housing Management will so inform MIAS and the termination or prepayment request will be honored.

SECTION 5. EFFECT OF PREPAYMENT/VOLUNTARY TERMINATION ON SECTION 8 HAP CONTRACTS

- 22-15. Prepayment of the mortgage or voluntary termination of the mortgage insurance does not relieve the mortgagor of any obligations under a Section 8 New Construction/Substantial Rehabilitation or Section 8

Project Name: _____

Project Number: _____

Location: _____

RENTAL USE AGREEMENT

(for use in the Section 223(f) Mortgage Insurance Program)

This Agreement is made and entered into this _____ day of _____, 19_____, by and between the Secretary of Housing and Urban Development acting by and through the Federal Housing Commissioner ("HUD"), and _____ (Mortgager); WITNESSETH:

WHEREAS, HUD endorsed for mortgage insurance that certain Note made by Mortgagor dated _____ and secured by a Mortgage (Deed of Trust) of even date therewith made to _____, said Mortgage being recorded at Official Records Book _____, Page _____ in the _____; and

WHEREAS, the property secured by the said mortgage is described in Exhibit A to that Mortgage and in Exhibit A of this Agreement and is currently operated by Mortgagor as (Name of Project, Address); and

WHEREAS, the said Note contains a prepayment provision as follows:

The debt evidenced by this Note may not be prepaid either in whole or in part for a period of five years from the date of endorsement hereof except in cases where the prior written approval of the Federal Housing Commissioner is obtained and such written approval is expressly based upon the existence of one of the following:

- (i) The grantor has entered into an agreement with the Commissioner to maintain the property as rental housing for the remainder of the specified five-year period;
- (ii) The Commissioner has determined that the conversion of the property to cooperative or condominium ownership is sponsored by a bona fide tenants, organization representing a majority of the households in the project;

- (iii) The Commissioner has determined that continuation of the property as rental housing is unnecessary to assure adequate rental housing opportunity for low and moderate income people in the community; or
- (iv) The Commissioner has determined that continuation of the property as rental housing would have an undesirable and deleterious effect on the surrounding neighborhood.

WHEREAS, Mortgagor is the original Mortgagor and has requested the prior written approval of HUD acting by and through the Federal Housing Commissioner to prepay the _____ pursuant to the above quoted provision; and

WHEREAS, Mortgagor is willing to agree to maintain the subject property as rental property until _____, which is the requisite period of five years after the date of HUD's endorsement of the _____;

NOW, THEREFORE, in consideration of the mutual covenants contained herein, and other good and valuable consideration, the receipt and sufficiency of which are expressly acknowledged, the parties agree as follows:

1. The execution and recording of this Agreement shall constitute HUD's approval of the prepayment of the Note described above, provided such prepayment is made in accordance with the terms of the Note for a prepayment penalty, if applicable.
2. The Mortgagor agrees that, during the period that it owns the property, it will maintain the property as rental housing until _____, or until any earlier date agreed to by HUD in writing. During such period the Mortgagor shall not market project dwelling units for any purpose other than rental housing without HUD's prior written approval.
3. The provisions of this Agreement shall be binding upon the heirs, successors and assigns of the Mortgagor.

4. The provisions of this Agreement relating to the rental

use of the property shall be binding for the benefit of, in favor of and enforceable by the Secretary and his successors in office. The Secretary and his successors in office and/or any third-party beneficiary shall be entitled to (a) institute legal action to enforce performance and observance of, (b) enjoin any actions which are violative of, and (c) exercise any other legal or equitable right or remedy with respect to, such provisions. For the purpose of these covenants, a third-party beneficiary shall be any person eligible for occupancy in a rental project insured pursuant to the provisions of Section 223(f). These rights and remedies may be exercised separately or in combination.

- 5. The Mortgagor agrees that during the period it owns the property and after the prepayment has been made, it will comply with the provisions of the Fair Housing Act which prohibits discrimination in housing on the basis of race, color, religion, sex, handicap, familial status, or national origin, and with all regulations issued pursuant to the Act.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed the day and year first above written.

ATTEST:

MORTGAGOR:

by (Title):

by (Name):

SEAL

UNITED STATES OF AMERICA
SECRETARY OF HOUSING AND
URBAN DEVELOPMENT

By: Director, Office of
Multifamily Housing Management

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APPENDIX 2

County of _____, State of _____, SS:

I, _____,

notary public on and for the State of _____, do hereby certify

that _____,

WITNESS my hand and Notarial seal the day and year aforesaid.

Notary Public

My commission expires: _____

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