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CHAPTER 27. SECTION 202 DEBT SERVICE RESERVE

27-1. INTRODUCTION. Information on the debt service reserve requirement for some Section 202 loan projects is included in the comprehensive revision to Handbook 4350.1 so Loan Servicers will recognize its purpose and use. Debt service reserve, as with the reserve fund for replacements, is a separate line item on financial forms used in the original Section 202 loan program. Because the term of these mortgages generally is 50 years, projects financed under the original Section 202 program (funded between 1960-1970) are part of a Loan Management Branch's portfolio.

Original premise for establishing a debt service reserve: to provide mortgagors with an extra "cushion" to meet debt service payments on the project mortgage and thus, safeguard the project's financial viability. Time and experience revealed that such a separate reserve was not needed for later generation Section 202 projects with Section 8 subsidy and was omitted.

27-2. ELIGIBILITY OF MORTGAGOR. The requirement to fund a debt service reserve account was applicable to mortgagors of projects financed under what was known as the Senior Citizens Housing Loan Program, pursuant to Section 202 of the Housing Act of 1959. Projects constructed under this program contain "SH" (for Senior Housing) in their identification numbers, for example, 999-SH0010. The legal dockets for "SH" projects presently reside with Philadelphia's Regional Accounting Division (RAD). The Field Office with jurisdiction should have maintained a working file for each project.

27-3. TECHNICAL FUNDING REQUIREMENT. Controlling documents, i.e., Regulatory Agreement and Loan Agreement, mandated a debt service reserve account. The borrower was required to make an initial deposit to this reserve account no later than the date of final disbursement of loan proceeds. At the end of each fiscal year, after deducting a 90-day operating expense set-aside, any balance remaining in the Revenue Fund Account, now known as the project operating account, would be used for additional deposits to the Debt Service Reserve Account. Deposits were required until the account attained an amount equal to one year's debt service on the project. Mortgagors were released from making

additional deposits provided the account maintained the balance specified.

Funds in the Debt Service Reserve Account are to be used exclusively for payments of principal and interest on the Mortgage Note, or to meet escrows such as insurance premiums, real estate taxes or special assessments.

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