

Legal Opinion: GCH-0064

Index: 2.895

Subject: Section 202 Project--HUD Approval of Prepayment

July 7, 1992

MEMORANDUM FOR: Robert W. Wilden, Director, Assisted
Elderly and Handicapped Housing Division, HMEE

FROM: Michael H. Reardon, Assistant General Counsel
Assisted Housing Division, GCH

SUBJECT: Eagles Manor
Project No. SH-Mont-07

The purpose of this memorandum is to assist you in responding to a memorandum from the Denver Regional Office, addressed to Assistant Secretary Hill and Associate General Counsel Kenison, concerning the request made by the owner of the above section 202 project for HUD to accept prepayment of the loan. The owner asserts that it is not required to obtain HUD approval to prepay the loan, since the note and mortgage are silent on this issue. It further asserts that the 1983 amendment to section 202(j)(1) of the Housing Act of 1959 restricting HUD approval of prepayments of loans is not applicable since the original note and mortgage were dated June 3, 1965.

Although the note and mortgage documents may be silent on prepayment, the loan agreement and regulatory agreement, which are attached to and made a part of the mortgage, address this issue. The loan agreement permits prepayment from any revenues remaining at the end of the owner's fiscal year in excess of operating expenses for the next 90 days. The regulatory agreement prohibits prepayment without prior written approval of the Government, except as provided in the loan agreement. We have therefore concluded that the loan contract does preclude payment without HUD's approval except as provided in the loan agreement. Although the owner asserts that, under Montana law, a debtor may prepay if the note and mortgage instruments are silent on the subject no cases are cited to contradict the general rule that an express provision permitting prepayment is needed. Further, we believe that the mortgage includes the loan and regulatory agreements which are incorporated by reference for this purpose. Copies of June 4, 1987 and February 1, 1990 legal opinions addressing these issues are attached.

The owner further questions applicability of the 1983 statutory amendment limiting circumstances under which HUD may approve prepayment of section 202 loans to loans made before November 30, 1983, the date of that statutory change. Application of the statutory criteria for HUD approval of

prepayment would not impair the owner's contract since it did not have the right to prepay, which was completely in HUD's discretion. Neither the statutory language prohibiting approval of prepayment unless HUD determines that the project will be operated on terms equally favorable to tenants for the remaining period of the original loan agreement nor its legislative history suggest any time limitation on imposition of this restriction. This provision has been construed from its enactment to be applicable to all section 202 loans. In fact the situation leading to enactment of the restriction (although not referred to in the legislative history) was the HUD approval of prepayment and refinancing of an early section 202 loan, Concord-Pasadena, which caused so many problems that HUD reinstated the loan.

We agree with the Denver office's conclusion that the owner has not demonstrated that, under the refinancing, the project would be able to operate until the maturity date of the original loan on equally favorable terms to tenants. Not only is it unlikely that the interest on the commercial loan would be as favorable as the 3 5/8 percent rate on the original loan, but the proposed conversion to care facilities would place an additional burden on the project. To the extent that units would be converted to care facilities, tenants similar to the present occupancy could be denied units.

Attachments (2)