

Prepayment--Conversion of Rent Supp. Units to Sec. 8

Legal Opinion: GHM-0042

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Subject: Prepayment--Conversion of Rent Supp. Units to Sec. 8

July 17, 1992

MEMORANDUM FOR: Albert B. Sullivan, Deputy Director
Office of Multifamily Housing Management, HMM

Frank Malone, Director, Office of Preservation
and Property Disposition, HMP

FROM: David R. Cooper, Assistant General Counsel
Multifamily Mortgage Division, GHM

SUBJECT: Conversion of Rent Supplement Units to Section 8
Assistance

This memorandum is in response to Kevin East's and Buz Schick's May 8, 1992 request for a legal opinion concerning whether projects which convert from rent supplement to Section 8 assistance would be deemed eligible low income housing under the Low Income Housing Preservation and Resident Homeownership Act of 1990 ("LIHPRHA").

On May 19, 1992 a NOFA entitled "Fund Availability (NOFA) for the Conversion of Rent Supplement and Rental Assistance Program Units to Section 8 Assistance" (the "NOFA"), was published at 57 Fed. Reg. 21334 announcing funds for the conversion of rent supplement project units to Section 8 assistance under the loan management set-aside program. This conversion was authorized by Title II of the Departments of Veterans Affairs and Housing and Urban Development, and Independent Agencies Appropriations Act, 1992 (the "1992 Appropriations Act"). Owners of projects with HUD-insured or HUD-held mortgages would be eligible to apply for conversion under the NOFA. The effect of the conversion would be that the rental assistance payments contract ("RAP Contract") on the converted units would be terminated and a 5-year housing assistance payments contract ("HAP Contract") would be executed to cover those units.

About ten years ago, a similar conversion from rent supplement to Section 8 assistance occurred. The Department determined, in the preamble to the interim rule implementing LIHPRHA and amending Part 248 of Title 24 of the Code of Federal Regulations (the "Interim Rule"), published on April 8, 1992 at 57 Fed. Reg. 11992, that those projects which were converted from rent supplement to Section 8 assistance ten years ago may be considered eligible low income housing under LIHPRHA. The question has now arisen whether projects which will be converting

under the May 19, 1992 NOFA would also meet the definition of "eligible low income housing."

Section 229 of LIHPRHA defines the term "eligible low income housing" as any housing:

"that is financed by a loan or mortgage--

(A) that is--

(i) insured or held by the Secretary under section 221(d)(3) of the National Housing Act and assisted under section 101 of the Housing and Urban Development Act of 1965 or section 8 of the United States Housing Act of 1937;

(ii) insured or held by the Secretary and bears interest at a rate determined under the proviso of section 221(d)(5) of the National Housing Act;

(iii) insured, assisted, or held by the Secretary or a State or State agency under section 236 of the National Housing Act; or

(iv) held by the Secretary and formerly insured under a program referred to in clause (i), (ii), or (iii); and

(B) that, under regulation or contract in effect before February 5, 1988, is or will within 24 months become eligible for prepayment without prior approval of the Secretary."

At issue here is whether projects converting from rent supplement to Section 8 assistance which meet the criteria of paragraph (A), as quoted above, fulfill the requirements of paragraph (B) in order to qualify the projects as eligible low income housing.

Sections 221.524 and 236.30 of the Department's regulations state that a limited distribution mortgagor may prepay its insured or assisted mortgage without the prior consent of HUD if the prepayment occurs after the expiration of 20 years from the date of final insurance endorsement of the mortgage, "provided the mortgagor is not receiving payments from the Commissioner under a rent supplement contract." Because owners of projects currently receiving rent supplement assistance are prohibited, pursuant to Sections 221.524 and 236.30, from prepaying the mortgage without the Department's prior consent, those projects do not meet the requirements of paragraph (B) above, and therefore, are not eligible low income housing.

However, if the rent supplement is converted to Section 8 assistance, the project would no longer be considered a rent supplement project and would not be subject to the prepayment prohibitions of Sections 221.524 and 236.30; rather, a limited distribution mortgagor which is not receiving rent supplement assistance would be permitted to prepay its mortgage without HUD's consent after 20 years from the date of final endorsement.

Section 229 of LIHPRHA requires that in order for housing to be deemed "eligible low income housing" there must not only be the right to prepay without HUD's consent, but this right must

have existed by regulation or contract which was in effect prior to February 5, 1988. Sections 221.524 and 236.30, which permit a limited distribution mortgagor which is not receiving rent supplement to prepay its mortgage without HUD's approval after 20 years from final endorsement, became effective on December 22, 1971, long before February 5, 1988. Hence, a project meeting the requirements of paragraph (A), as quoted above, would fall within the definition of "eligible low income housing" if the mortgagor is a limited dividend entity and the mortgage is within 24 months of, or past, the 20th anniversary of final endorsement.

The preamble to the Interim Rule, at 57 Fed. Reg. 11997, summarizes the Department's position on converted rent supplement projects, stating that:

" a project whose rent supplement assistance was converted to section 8 assistance is no longer subject to the regulations concerning rent supplement assistance. These projects would be governed by the section 8 regulations once the conversion took place. Since projects receiving section 8 assistance are not subject to a prepayment prohibition based on the receipt of such assistance, these projects can qualify as eligible low income housing."

Projects which will be converting from rent supplement assistance to Section 8 assistance pursuant to the May 19, 1992 NOFA should be treated in the same manner as those projects which converted from rent supplement to Section 8 assistance ten years ago. Those projects which will be converting will be subject to the same provisions of Section 221.524 and 236.30 as the formerly converted projects. There is no reasonable basis for treating differently those projects which will be converting and those which have already converted from rent supplement to Section 8 assistance.

Therefore, as long as the project meets the requirements of paragraph (A), as quoted above, and can be prepaid, or is within 24 months of being able to prepay, without HUD's consent, the project that formerly received rent supplement assistance and has been converted to Section 8 assistance would be deemed "eligible low income housing" for purposes of LIHPRHA. Similarly, a project that is currently receiving rent supplement and subsequently converts to Section 8 assistance pursuant to the May 19, 1992 NOFA, will be considered "eligible low income housing" after conversion if it continues to meet the requirements of paragraph (A) and, as of the time it seeks to prepay, it is able, or is within 24 months of being able, to prepay without HUD's consent.

If you have any questions regarding this matter, please contact Susan M. Sturman at 708-3667.