



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

OFFICE OF HOUSING

February 18, 2011

MORTGAGEE LETTER 2011-14

MEMORANDUM FOR: ALL FHA APPROVED MULTIFAMILY MORTGAGEES

SUBJECT: Subordination, Non-Disturbance and Attornment Agreements

A. Purpose and Applicability

This Mortgagee Letter (ML) provides guidance on the use of Subordination, Non-Disturbance and Attornment Agreements (SNDA) for commercial leases in certain FHA insured projects and delegates approval authority of SNDAs to Hub and Program Center Directors.

This ML is applicable as follows:

- Applicable in its entirety to non-assisted or non-subsidized FHA insured multifamily projects under all Sections of the Act, except Section 232.
- Section C.1 only is applicable to FHA insured projects that are subsidized under Section 202/811, 236, 221(d) (3) BMIR, or FHA insured projects with Project Based Rental Assistance. Guidance will be forthcoming on expanding the applicability of this ML to subsidized or assisted insured projects.

A predictable, stable income stream from commercial leases with high quality, credit worthy commercial tenants provides a benefit to a property's operating stability, particularly if the commercial tenants are nationally recognized or have national brands. FHA benefits by allowing borrowers the latitude to negotiate with the widest pool of credit qualified commercial tenants. A stronger tenant increases the certainty of the commercial income stream, enhances the property's marketability and decreases risk to the FHA Insurance Fund.

Permitting the use of SNDAs is necessary to induce higher quality commercial tenants to rent in insured properties. Therefore, this ML permits the use of SNDAs when a commercial lease is negotiated at a property with an existing insured mortgage, for a new property with a newly originated insured loan, or when a building owner with existing commercial tenants seeks an insured loan for refinancing.

B. Background

Prior to the issuance of this ML, HUD's policy on SNDAs was based on a concern over lack of flexibility in the event of a mortgage default, since an SNDA gives a commercial

tenant the right to remain in its space under the existing lease terms and conditions after a loan default and foreclosure. If there were a borrower approved SNDA, HUD would be bound to continue the commercial lease even after assignment of the insured loan. Because of HUD's prohibition on SNDAs, borrowers were negotiating into commercial leases the required lease termination language, were leasing to commercial tenants that would not insist on an SNDA or were deciding not to apply for financing under the FHA insurance programs.

Commercial tenants generally desire, and in many instances require, an SNDA in recognition of the expense put into lease negotiations and to enable them to continue to enjoy the business location and the economic benefits and certainty of the lease terms. In many cases, the tenant incurs costs to design and build out their unique tenant improvements, which costs must be amortized over the lease term. Nor does the tenant want to lose the good will and customer base associated with continuing to operate on the premises. Indeed, MAP lenders report that most national retail chains require an SNDA and will not execute a long term lease without the non-disturbance assurance.

C. Implementation

A sample form of SNDA is attached. This form should be used for all SNDAs approved by Hubs or Program Centers.

In the near future, the Department will issue guidance related to reviewing and setting rents for commercial space in insured and assisted properties. In the interim, existing guidance on underwriting commercial rents and commercial tenants as found in relevant sections of the MAP Guide, specifically Chapter 7, Section 6-F should continue to be utilized.

- 1) SNDAs are permitted for Rooftop, Cell Phone Tower, Cable Television and Internet Access Leases on all properties with an existing insured mortgage or on all properties applying for an insured mortgage subject to the following:
 - a) New, existing or renegotiated rooftop leases (including for cell phone towers, cable television or internet access) in all properties with currently insured mortgages, in all properties applying to refinance, or in all new construction or substantial rehabilitation properties, may use an SNDA. In those cases, the commercial lease and income that is or will be in place is a benefit to the property, while imposing little or no additional property operating expense. The presence of a rooftop cell phone tower or cable access to the building should not negatively affect the residents, the marketability of the units or HUD's recovery value on the note in the event of a default.
 - b) With respect to all such leases, the underwriting and review process should ensure that there are no exclusivity requirements under the leases that would prevent the owner from attracting competing services for the benefit of the residential tenants in the future.

- 2) SNDAs are permitted for Commercial Leases, other than Rooftop, Cell Phone Tower, Cable Television or Internet Access Leases on all non-assisted or non-subsidized properties with an existing insured mortgage or on all non-assisted or non-subsidized properties applying for an insured mortgage subject to the following:
 - a) New, existing or renegotiated commercial leases with commercial tenants in properties with currently insured mortgages, in properties applying to refinance, or in new construction or substantial rehabilitation properties may use an SNDA.
 - b) A lease may be approved if the lease calls for a fair market rent in the local area and the activities to be conducted by, or the structures and equipment to be installed by, the proposed tenant will not have an adverse affect on the residents.
 - c) If any Identity of Interest (IOI) relationship (defined as a financial interest or family relationship with the officers, directors, stockholders, or partners of the Borrower) exists between the borrower as lessor and the commercial tenant as lessee, an SNDA is not permitted.
 - d) The commercial tenant must be appropriate for a residential building.

D. Approval

- 1) Hubs and Program Center Directors are authorized to approve all SNDAs for rooftop, cell phone tower, cable television and internet access leases.
- 2) For any property applying for a new mortgage insurance commitment, the Hub or Program Center will review and approve of the commercial lease terms and the form of SNDA when processing the application for Firm Commitment.
- 3) For existing properties with insured mortgages the Hub or Program Center Director may approve the proposed SNDA between the property owner and the commercial tenant.
- 4) The following is the typical supporting documentation, although depending on the circumstances, additional documentation may also be required:
 - a) Proposed commercial lease and SNDA agreement.
 - b) Form HUD-92458 and 92264.
 - c) Commercial market rent study.
 - d) Details of any proposed build out or finish of the commercial space or rooftop tower.
 - e) Disclose the existence of any related documents such as: Memorandum of Lease, Guaranty of Lease, Tenant Estoppels' Certificate, Lease Guaranties or Amendments, etc.

If you have any questions regarding this Guidance, please contact Howard Mayfield in the Office of Multifamily Development at (202) 402-2558 or Norm Dailey in the Office of Asset Management at (202) 402-8371.

/s/

David H. Stevens
Assistant Secretary for Housing-
Federal Housing Commissioner

RECORDING REQUESTED BY
AND WHEN RECORDED RETURN TO:

(Space above this line for Recorder’s Use)

**SUBORDINATION, NON-DISTURBANCE
AND ATTORNMEN T AGREEMENT**

THIS AGREEMENT, made as of this __ day of _____, 20__, by and between _____ (“Owner” or “Lessor”), as lessor under the lease hereinafter described, and _____ (“Operator” or “Lessee”), lessee under the aforementioned lease, in favor of _____ (“FHA Lender”), the owner and holder of the Mortgage hereinafter described.

W I T N E S S E T H:

WHEREAS, Lessor has executed, or will execute that certain Mortgage/Deed of Trust with Assignment of Rents, dated as of _____, 20 __, (the “Mortgage”), in favor of FHA lender and covering certain real property (the “Property”) located in the City of _____ County of _____, State of _____, with a legal description as set forth in Exhibit “A” attached hereto and incorporated herein by this reference, and covering the improvements situated thereon (the “Improvements”); and

WHEREAS, Lessor and Lessee entered into that certain unrecorded Lease dated _____, 20__, and all amendments thereto (the “Lease”), covering the Improvements for the term and upon the conditions set forth therein; and

WHEREAS, the parties hereto now desire to enter into this Agreement to establish certain rights and obligations with respect to their interests, and to provide for various contingencies as hereinafter set forth.

NOW, THEREFORE, in consideration for the foregoing and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, and of the mutual benefits to accrue to the parties hereto, it is hereby declared, understood and agreed that the Lease, all terms and conditions set forth in the Lease, the leasehold interests and estates created thereby, and the priorities, rights, privileges and powers of Lessee and Lessor there under shall be and the same are hereby, and with full knowledge and understanding of the effect thereof,

unconditionally made subject and subordinate to the lien and charge of the Mortgage, all terms and conditions contained therein, any renewals, extensions, modifications or replacements thereof, and the rights, privileges and powers of the trustee and FHA lender there under,

and shall hereafter be junior and inferior to the lien and charge of the Mortgage. The parties further agree as follows:

1. It is expressly understood and agreed that this Agreement shall supersede, to the extent inconsistent herewith, the provisions of the Lease relating to the subordination of the Lease and the leasehold interests and estates created thereby to the lien or charge of the Mortgage.
2. FHA lender consents to the Lease.
3. In the event FHA lender or any other purchaser at a foreclosure sale or sale under private power contained in the Mortgage, or by acceptance of a deed in lieu of foreclosure, succeeds to the interest of Lessor under the Lease by reason of any foreclosure of the Mortgage or the acceptance by FHA lender of a deed in lieu of foreclosure, or by any other manner, it is agreed as follows:
 - (a) Lessee shall be bound to FHA lender or such other purchaser under all of the terms, covenants and conditions of the Lease for the remaining balance of the term thereof, with the same force and effect as if FHA lender or such other purchaser were the lessor under such Lease, and Lessee does hereby agree to attorn to FHA lender or such other purchaser as its lessor, such attornment to be effective and self-operative without the execution of any further instruments on the part of any of the parties to this Agreement, immediately upon FHA lender or such other purchaser succeeding to the interest of Lessor under the Lease.
 - (b) Subject to the observance and performance by Lessee of all the terms, covenants and conditions of the Lease on the part of the Lessee to be observed and performed, FHA lender or such other purchaser shall recognize the leasehold estate of Lessee under all of the terms, covenants and conditions of the Lease for the remaining balance of the term (as the same may be extended in accordance with the provisions of the Lease) with the same force and effect as if FHA lender or such other purchaser were the lessor under the Lease and the Lease shall remain in full force and effect and shall not be terminated, except in accordance with the terms of the Lease or this Agreement; provided, however, that FHA lender or such other purchaser shall not be (i) liable for any act or omission of Lessor or any other prior lessor, (ii) obligated to cure any defaults of Lessor or any other prior lessor under the Lease which occurred prior to the time that FHA lender or such other purchaser succeeded to the interest of Lessor or any other prior lessor under the Lease, (iii) subject to any offsets or defenses which Lessee may be entitled to assert against Lessor or any other prior lessor, (iv) bound by any payment of rent or additional rent by Lessee to Lessor or any other prior lessor for more than one (1) month in advance, (v) bound by any amendment or

modification of the Lease made without the written consent of FHA lender or such other purchaser, or (vi) liable or responsible for or with respect to the retention, application and/or return to Lessee of any security deposit paid to Lessor or any other prior landlord, whether or not still held by Lessor, unless and until FHA lender or such other purchaser has actually received for its own account as lessor the full amount of such security deposit.

Lessee hereby agrees that it will not exercise any right granted it under the Lease, or which it might otherwise have under applicable law, to terminate the Lease on account of a default of Lessor there under or the occurrence of any other event without first giving to FHA lender prior written notice of its intent to terminate, which notice shall include a statement of the default or event on which such intent to terminate is based. Thereafter, Lessee shall not take any action to terminate the Lease if FHA lender (a) within thirty (30) days after service of such written notice on FHA lender by Lessee of its intention to terminate the Lease, shall cure such default or event if the same can be cured by the payment or expenditure of money, or (b) shall diligently take action to obtain possession of the leased premises (including possession by receiver) and to cure such default or event in the case of a default or event which cannot be cured unless and until FHA lender has obtained possession, but in no event to exceed ninety (90) days after service of such written notice on FHA lender by Lessee of its intention to terminate.

4. Lessor and Lessee hereby certify to FHA lender that the lease as previously submitted to FHA lender has not been further amended.
5. For the purposes of facilitating FHA lender's rights hereunder, FHA lender shall have, and for such purposes is hereby granted by Lessee and Lessor, the right to enter upon the Property and the Improvements thereon for the purpose of affecting any such cure.
6. Lessee hereby agrees to give to FHA lender concurrently with the giving of any notice of default under the Lease, a copy of such notice by mailing the same to FHA lender in the manner set forth herein below, and no such notice given to Lessor which is not at or about the same time also given to FHA lender shall be valid or effective against FHA lender for any purpose.
7. Subordination of Lease to Mortgage and Regulatory Agreements and Regulation by the U.S. Department of Housing and Urban Development ("HUD").
 - (a) The Lease and all estates, rights, options, liens and charges therein contained or created under the Lease are and shall be subject and subordinate to the lien or interest of (i) the Mortgage on the Lessor's interest in the Property in favor of FHA lender, its successors and assigns insofar as it affects the real and personal property comprising the Property (and not otherwise owned, leased or licensed by Lessee) or located thereon or therein, and to all renewals, modifications, consolidations, replacements and extensions thereof, and to all advances made or to be made there under, to the full extent of amounts secured thereby and interest thereon, and (ii) that certain Regulatory Agreement for Multifamily Housing Projects between Lessor and HUD to be recorded against the Property.

- (b) The parties to the Lease agree to execute and deliver to FHA lender and/or HUD such other instrument or instruments as the FHA lender and/or HUD, or their respective successors or assigns, shall reasonably request from time to time to reconfirm the status of the lease and to effect and/or confirm the subordination of the Lease to the lien of the Mortgage and the above-described Regulatory Agreements. To the extent that any provision of the Lease shall be in conflict with the HUD Program Obligations (as such term is defined below), the HUD Program Obligations shall be controlling.
 - (c) In the event HUD, at a foreclosure sale or sale under private power contained in the Mortgage, or by acceptance of a deed in lieu of foreclosure, succeeds to the interest of Lessor under the Lease by reason of any foreclosure of the Mortgage or the acceptance by HUD of a deed in lieu of foreclosure, or by any other manner, it is agreed as follows:
 - (i) HUD can terminate the Lease for any violation of the Lease that is not cured within any applicable notice and cure period given in the Lease.
 - (ii) As used in this Agreement “HUD Program Obligations” shall mean all applicable statutes and regulations, including all amendments to such statutes and regulations, as they become effective, and all applicable requirements in HUD Handbooks, Notices and Mortgagee Letters that apply to the Property, including all updates and changes to such Handbooks, Notices and Mortgagee Letters that apply to the Property, except that changes subject to notice and comment rulemaking shall become effective upon completion of the rulemaking process.
 - (d) To the extent there is any inconsistency between the terms of this Subordination, Non Disturbance and Attornment Agreement, and the Lease, the terms of this Subordination, Non Disturbance and Attornment Agreement shall be controlling.
8. For purposes of any notices to be given to FHA lender hereunder, the same shall be sent by U.S. certified mail, return receipt requested, postage prepaid, to FHA lender at the following address:

[Insert Address]

or to such other address as FHA lender may hereafter notify Lessee in writing by notice sent to Lessee as aforesaid at Lessee’s address at the Property, or such other address as FHA lender may hereafter be advised of in writing by notice sent to FHA lender as aforesaid.

9. The agreements contained herein shall run with the land and shall be binding upon and inure to the benefit of the respective heirs, administrators, executors, legal representatives, successors and assigns of the parties hereto.
10. This Agreement may be executed in one or more counterparts, all of which when taken together shall constitute a single instrument.
11. This Agreement shall, in all respects, be governed by and construed and interpreted in accordance with the laws of the _____.

[SEE ATTACHED SIGNATURE PAGES]