
CHAPTER 2. PROVISIONS

- 2-1. GENERAL. For the purpose of reducing rentals for lower income families in Section 236 projects, HUD is authorized to make, and to contract to make, periodic interest reduction payments to mortgagees on behalf of owners of rental housing projects meeting the program requirements. The Secretary also includes in the payment to the mortgagee an amount which he deems appropriate to reimburse the mortgagee for its expense in handling the mortgage.
- a. For Each Unit in Housing Projects approved for receiving the benefits of this program, a basic rent charge is established. This basic rent charge is determined on the basis of payment of principal and interest due under a mortgage bearing interest at the rate of one percent per annum.
 - b. A Formula Rent Charge is also established, calculated on the basis of payment of principal, interest, and mortgage insurance premium (which the mortgagor is obligated to pay under the market rate mortgage covering the project). However, the total formula rental charge must not exceed the fair market rent estimated on a direct comparison basis.
 - c. For His Dwelling Unit, a tenant must pay the basic rental charge or such greater amount, not exceeding the fair market rental charge, as represents 25 percent of the tenant's adjusted income.
- 2-2. PROJECTS. The development of feasible Section 236 housing projects involves more than keeping within the cost limitations prescribed for the program. Considerable thought must go into the site selection and project design in order to best serve the intended low and moderate income market.
- a. The Sponsor's Architect and HUD Staff must make every effort to combine maximum livability with reasonable cost. Proper techniques and materials must be used to reduce construction costs and keep future operating costs to an acceptable minimum. The design should incorporate features that will prevent, not lead to, premature obsolescence. Certain amenities, such as more than one bathroom for larger units, swimming pools, dishwashers, carpeting and draperies, may be permitted provided that the market demands these amenities in unsubsidized moderate income residential apartment projects in the

(2-2) area and further provided that the inclusion of such amenities will not have a significant detrimental effect on other design elements of the project (such as unreasonably reducing the amount of living or recreation space). Projects which are intended to serve families with children should be designed to meet their needs. High-rise construction should be avoided in these cases. Attractive landscaping and adequate recreation space should be provided whenever possible. These features improve livability and marketability.

b. The Possibility of Over-Concentration of Low-Income Families must be considered when large projects are proposed. For this reason, sponsors should be encouraged to develop smaller projects, and/or to choose sites for development which are scattered throughout a community. Scattered development has the dual effect of preventing over-concentration of lower income families in one area of a community and providing prospective residents with a freedom of movement into a different area in which they may prefer to live and which may also be located within more reasonable distances from their places of employment.

* c. Maximum Insurable Mortgage. Unit mortgage limits established for both garden type and elevator type construction are listed in Chapter 5, paragraph 5-6.c. *

d. The Maximum Term of the insured mortgage is 40 years.

e. Projects Must Include at least five units, which may consist of elevator, garden, row or single-family type structures on contiguous or non-contiguous sites, provided they constitute a readily marketable real estate entity and are located so as to permit reasonable, efficient management. They may be designed for general use as rental projects for lower income families or exclusively for occupancy by elderly or handicapped persons (in which case they may include facilities for use by the elderly or handicapped). See Chapter 9 of this Handbook for further discussion of housing for the elderly, handicapped and displaced.

*

2-3. COMMERCIAL SPACE. Any Section 236 project may include commercial area not exceeding 10 percent of all net rentable floor area (both residential and commercial) except in urban renewal areas. In urban renewal areas, the commercial facilities allowed are

those deemed adequate and appropriate to serve the occupants and the surrounding neighborhood; provided that the project is predominately residential in nature; and further provided that any commercial space included in the mortgage (other than parking or coin-operated laundry facilities) will produce income sufficient to pay its proportionate share of expenses and a return on its cost equal to the market debt service rate of the insured mortgage. Consideration shall be given to the possible effect of the project and its facilities on other business enterprises in the community. *

- 2-4. ELIGIBLE PROPOSALS. Only new construction or projects requiring substantial rehabilitation are eligible to benefit from Section 236. Please refer to Chapter 7 of this Handbook for a discussion of the criteria for acceptance of rehabilitation proposals.
- 2-5. CONDOMINIUMS.
- a. Although condominiums may not be insured as such under Section 236, projects may be designed so that individual units may later be released from the blanket mortgage, sold to lower income, elderly or handicapped purchasers, and insured under Section 235 or Section 234(c). Such projects must meet all the statutory and administrative requirements for participation in the Section 236 program, and must meet the requirements for conversion to condominium ownership as stated in Sections 234.26 and 235.20 of the Regulations. The price, including closing costs, of a unit to be sold to a Section 235 mortgagor may not exceed the HUD value of the unit.
 - b. Section 236 mortgagors who intend to spin-off units to individual (condominium) ownership should plan for a period of several years between final endorsement and actual release of the units from the blanket mortgage. This is preferable for several reasons: (1) Section 236 is not intended to be used to provide insured advances for single family development; (2) fees for multifamily projects are not appropriate for single family developments; (3) from planning and production points of view, it is not desirable to encumber substantial amounts of both Section 236 and Section 235 contract authority for the length of time it takes to construct a multifamily project; and (4) the spin-off provision is designed to help

lower income families move into decent rental housing at a price they can afford and then, when they have accrued sufficient capital and have become acceptable credit risks, progress to homeownership (assisted or unassisted). If there is

a market comprised of families who can become homeowners immediately, programs other than Section 236 should be used.

- 2-6. COOPERATIVES. Cooperatives are insurable under Section 236. For further information about the details of the sponsorship, organization and operation of cooperative housing-projects, please refer to Reference (4) of the Foreword.
- 2-7. COLLEGE HOUSING. The Section 236 program is not intended to stimulate the supply of housing for college students and such intended use will lower an application's priority for the limited funds available.
- a. College Students who qualify as eligible tenants under Section 236 may of course, apply for units in Section 236 projects; however, all such developments are open to any eligible tenant and may not be restricted to college students.
 - b. Educational Institutions may wish to consider submitting an application to participate in the College Housing Program, which is designed to meet specific college housing needs. Please see Reference (5) of the Foreword.
- 2-8. SPACE FOR COMMUNITY AND RELATED FACILITIES. Buildings for community use as recreational facilities, rent-free day care centers operated on a nonprofit basis, and other similar facilities, may be included in Section 236 mortgages. It may be desirable to design community facilities for possible future use by tenants of more than one subsidized project (not necessarily developed under the same program). However, due to the uncertainty of future development, care must be taken to include no more actual space for community facilities in one project than is feasible within individual project cost limitations. If community buildings are eventually to serve more than one project, with expansion to be undertaken as other projects are developed, the basic facilities should be planned to be as convenient as possible to all the projects. This situation is likely to occur in cooperative projects (which are often developed in several phases). If one of the first phases includes community facilities for all the phases and the rest of the planned phases are not developed, the financial position of the existing phases may be seriously jeopardized. Thus, reliance should be placed on planned expansion to the extent feasible.

-
- 2-9. MORTGAGORS. Private non-profit corporations. limited distribution entities and cooperative housing corporations are eligible mortgagor-sponsors of Section 236 projects. The builder-seller arrangement for cooperatives is also permitted.

- a. A Sponsor Group or Organization must have motivation, reliability, substance, and the ability to complete a project and provide competent, continuing management of the property. The capability and resources of the sponsor must be commensurate with the size of its proposed project.
- b. With Respect to Motivation, the sponsor must have a proper and clearly identified interest in providing housing for the intended occupants in the proposed location. This requirement applies to all types of mortgagors.
- c. Although There are No Precise Guidelines to be used making these findings, personnel engaged in the preliminary review should be at all times be aware of the requirement that a proposed mortgagor has (a) proper motivation and (b) sufficient competence to complete a successful project.

2-10. BORROWING BY NONPROFIT MORTGAGORS. It is permissible for non-profit mortgagors to borrow funds required for project purposes, subject to the following conditions:

- a. Nonprofit mortgagors may borrow funds from the contractor or other entities which furnish supplies or services but only for the cost of items to be covered by the insured mortgage. Any such loans must be paid in full at the time mortgage proceeds are advanced for the item for which the loan was made. In insurance upon completion cases, any such loans made must be paid in full at the time of endorsement of the note for insurance.
- b. Nonprofit mortgagors may borrow funds required for any project purpose from the sponsor or from entities which are in no way connected with the project. If funds are to be borrowed for project purposes not to be included in the mortgage, the total amount of the debt must be secured by a promissory note executed by the mortgagor on FHA Form 1710. Upon receipt of this Form, the field office must advise the mortgagor that the maximum rental schedule will not be increased to allow for repayment of any such loan.

4510.1

-
- c. If a nonprofit mortgagor receives gifts or donations from the general contractor, a subcontractor, the architect or other parties furnishing supplies or services, the amount of such gifts or donations must be deducted by the mortgagor in cost certification.

2-11. ALLOWANCE FOR MAKING PROJECTS OPERATIONAL (AMPO). The working

capital deposit is not required for projects sponsored by nonprofit organizations. To provide capital required to make the project operational, there shall be included in the estimated replacement cost an allowance equal to two percent of the total replacement cost figure. For a full discussion of AMPO see Reference (6) of the Foreword.

- 2-12. HOUSING CONSULTANTS. Nonprofit organizations may be sincerely interested in providing multifamily housing, yet lack technical staff and other facilities needed to develop a project. Therefore, HUD may recognize in the mortgage commitment the expenses to these organizations of obtaining the services of housing consultants. Consultants' efforts will be directed solely to assisting the nonprofit sponsor. See Reference (6) of the Foreword.
- 2-13. ELIGIBLE LENDERS OR MORTGAGEES. To be eligible to apply for and receive commitments for HUD-FHA-insured loans under Section 236, a lender must be an HUD-FHA-approved mortgagee and must be willing to receive monthly interest reduction payments on behalf of the project mortgagors. HUD-FHA mortgagee approval is not required in the case of state or local assisted projects not involving HUD-FHA mortgage insurance. The lender should also be an approved FNMA/GNMA seller-servicer if the loan is to be sold to FNMA/GNMA.
- 2-14. FEES AND CHARGES.
- a. HUD-FHA Fees are as follows:
- (1) Application fee is \$1.50 per \$1,000 of mortgage amount.
 - (2) Commitment fee is \$3.00 per \$1,000 of commitment amount less application fee previously paid.
 - (3) Inspection fee is \$5.00 per \$1,000 of commitment amount.
 - (4) Mortgage Insurance Premium is 1/2 of 1% of mortgage amount.
- b. The Financing Fee is 2%, computed on the original principal amount of the mortgage.

- * c. FNMA/GNMA Fee: Commitment, purchasing and marketing fee for Section 236 is 1-1/2 percent of the mortgage amount. See paragraph 1-3 b.
- 2-15. SPECIAL RISK INSURANCE FUND. Claims arising from mortgages insured under Section 236 will be paid in cash in accordance with Section 236.265 of the Project Mortgage Regulations, from the

Special Risk Insurance Fund established under Section 238 (added to the National Housing Act by Section 104 of the Housing and Urban Development Act of 1969). Under certain circumstances, a mortgagee may be requested to assign its mortgage to HUD. In any such instance the mortgagee will receive, as consideration for the assignment, the outstanding balance of principal plus any accrued interest, without the customary deduction of 1 percent (see Regulations 236.265(c)).

2-16. ANTICIPATED ADJUSTMENTS IN RENTS.

a. Adjustments prior to or at closing. Occasionally, during processing or closing, adjustments must be made in the anticipated rent schedule in order to provide for unexpected changes in debt service or operating expenses (including tax increases) which have occurred or will occur in the near future. Although all mortgages which HUD insures should be self-supporting at the time of closing and remain so throughout the life of the mortgage, rent increases can mean that the persons for whom the project was originally intended will be financially unable to pay the rents prescribed in a new schedule. Thus, an absence of housing for lower income families will continue to exist and the good intentions of the sponsors and local governing bodies will be thwarted. In addition, a project may have been built for which there may be no market at all. Further, public relations problems may be anticipated when housing originally intended as part of a city program for providing housing for low income families misses its mark.

b. Notification of Regional Administrator. The Area Office Manager is to ensure that the Regional Administrator is informed of any significant upward revisions of rent proposed for any projects designed for low and moderate income occupancy, and the reasons therefore.

*

4510.1 CHG-7

2-17. ASSURANCE OF COMPLETION. HUD standardized requirements to assure completion (see Reference (7) of the Foreword) are minimum requirements imposed primarily for HUD's own protection. Nothing in these instructions shall be construed as limiting or restricting the absolute right of the mortgagee or the owner to impose additional or stricter requirements, but the HUD requirements will not vary. See HUD Regulations Section 221.542.