Internal / External
Topic: Other - Section 242
Healthcare Facility

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-0500

OFFICE OF GENERAL COUNSEL

July 23, 2012

MEMORANDUM FOR: Roger E. Miller, Deputy Assistant Secretary, Office of Healthcare Programs, HP

FROM: Millicent B. Potts, Associate General Counsel for Insured Housing, CAHA

SUBJECT: Section 242/Section 223(a)(7) Refinancing Loans Date on Endorsement Panel

This memorandum supersedes the December 23, 2003 memorandum from John Daly, Associate General Counsel for Insured Housing, to Roger Miller, Deputy Director, Office of Insured Healthcare Facilities, regarding the correct date to use on the endorsement panel of a Note for a Section 242 refinancing pursuant to Section 223(a)(7) of the National Housing Act (the "December 2003 memorandum").

The issue of which date should be used for purposes of determining the debenture interest rate of a project that is being refinanced pursuant to Section 242/Section 223(a)(7) was brought to the attention of my office in connection with the recent closing of the refinancing loan for [redacted] (the "[redacted] loan"). Consistent with the advice provided in the December 2003 memorandum, Lender's counsel inserted the date that the Section 242 loan was endorsed for insurance on the endorsement panel, as opposed to the date that the commitment to insure the Section 223(a)(7) was issued. In the December 2003 memorandum, Mr. Daly opined that because Section 223(a)(7) states that a loan refinanced pursuant to Section 223(a)(7) *"shall be documented through amendments to the existing insurance contract and shall not be structured through the provisions of a new insurance contract,"* the controlling date would be the date that the insurance contract for the Section 242 loan was entered into as long as the correct FHA insurance endorsement panel was used to implement the authority in Section 223(a)(7)(A)(iv). At present, the Office of Multifamily Housing and the Office of Residential Care Facilities apply a different interpretation to refinancing loans endorsed under their respective programs. Thus, we took this opportunity to revisit the advice provided in the December 2003 memorandum and to provide a uniform interpretation of the relevant statutory provision.

We believe that this issue is governed by Section 224, not Section 223(a)(7), of the National Housing Act. Section 224 states that:

> *"...debentures issued under any section of this Act...shall bear interest at the rate in effect* ***on the date the commitment to insure the loan or mortgage was issued,*** *or the date the loan or mortgage was endorsed for insurance, or (when there are two or more insurance endorsements) the date the loan or mortgage was initially*

endorsed for insurance, whichever rate is the highest..."

The relevant question is which loan is the statute referring to—the refinancing loan or the original FHA-insured loan? The answer to that question has two significant impacts: (1) it determines which regulations will apply to the loan; and (2) it determines the debenture interest rate that HUD will pay to the lender should there be a claim. In the first instance, as a matter of policy and practice, the regulations in effect on the date the loan is endorsed for insurance are the regulations that HUD has consistently indicated govern the loan. To read Section 224 as requiring that the endorsement panel of a mortgage bear, a date that precedes the closing of the refinancing, e.g. the date the Section 242 loan was endorsed for insurance, would produce an absurd result—the loan would be governed by potentially archaic regulations that do not take into effect recent amendments or new regulatory provisions in effect on the date of the Section 223 (a)(7) commitment. In the second instance, to determine the debenture interest rate based on the date the original mortgage was endorsed, which may be decades earlier, would require the Department to pay interest at an extremely high rate, despite the fact that the current rate (the rate at which the lender made the refinancing loan to the borrower) is significantly lower. These results were not contemplated by the plain language of the statute or by Congress. Consequently, it is our opinion that the loan that is referenced in Section 224 is the loan for which a commitment is presently being issued or the mortgage that is presently being endorsed for insurance.

We believe the following guidance provided by the Office of Multifamily Housing in Mortgagee Letter 06-03 ("Mortgagee Letter") may be instructive. In addition to establishing that the correct date for purposes of determining the debenture interest rate is the date the Section 223(a)(7) commitment was issued, the Mortgagee Letter includes the following sample endorsement panel to ensure that lenders insert the correct date:

> ***For purposes of compliance with Section 223(a)(7)(D) of the National Housing Act, the contract of mortgage insurance regarding FHA Project #(Insert old Project Number) is transferred to FHA project #(Insert new project Number), and said contract of mortgage insurance is hereby amended to reflect the terms, conditions and provisions of the FHA Firm Commitment for Project # (Insert New Project Number and date) and the National Housing Act as evidenced by the Federal Housing Commissioner's endorsement for insurance of the Note dated_____, executed by _____,(Maker), and payable to _____ in the amount of $_____."***

In conclusion, we recognize that the [redacted] loan was endorsed for insurance prior to the issuance of this superseding memorandum and therefore the Lender was allowed to insert the date of the Section 242 loan on the endorsement panel, based on the December 2003 memorandum. However, effective immediately, the endorsement panel on any future refinancing loans closed under the Section 242/ Section 223(a)(7) refinancing authority must bear the date that the commitment to insure the Section 223(a)(7) loan is issued. The regulations in effect on that particular date will govern the Section 223(a)(7) loan, and any debentures issued shall also bear interest at the rate in effect on that date.

If you have any questions, please contact Kelly Gil at extension 5261.