

Whether Public Entity May Purchase 236-Insured Project

Legal Opinion: GHM-0035

Index: 3.160, 3.346

Subject: Whether Public Entity May Purchase 236-Insured Project

May 27, 1992

Mr. Daniel R. Watson
Assistant Director
King County Housing Authority
15455 65th Avenue South
Seattle, WA 98188

Dear Mr. Watson:

Bud Albright asked that I respond to the issue raised in your letter to him dated January 31, 1992 and in our subsequent discussion with you in his office. In your letter, you questioned whether the King County Housing Authority (the "Housing Authority"), a public entity, may purchase a Section 236 insured project (Hidden Village Estates/Project No. 127-44011) under a plan of action filed pursuant to the Emergency Low Income Housing Preservation and Resident Homeownership Act of 1987 ("Title II").

Section 236(j)(4) of the National Housing Act ("NHA") authorizes a mortgage to be insured under the Section 236 program only if the mortgage is executed by a private mortgagor. It should be noted that Section 236(b) of the NHA, which governs projects under the state-financed "non-insured" program, was amended by Section 203(a)(1) of the HUD Reform Act of 1989 to permit public entities to be mortgagors of state-financed projects. No comparable amendment, however, was made to Section 236(j) which governs the Section 236-insured program. Section 236(j) applies in this case because Hidden Village Estates is covered by the Section 236-insured program rather than the non-insured program.

Section 236(j) requires that the mortgage be executed by a private mortgagor, but this subsection does not state whether a subsequent mortgagor of a Section 236-insured project must also be a private entity. The Department's long-standing interpretation of this subsection has been that public mortgagors are not eligible to purchase Section 236-insured projects. The Housing Authority is now contesting the Department's position, claiming that the enactment of Title II and Title VI implicitly authorize the purchase of Section 236-insured projects by public entities if the projects are sold pursuant to HUD-approved plans of action under either Title II or Title VI.

Title II was enacted by Congress in 1987 with the intent of preserving certain types of insured and assisted multifamily housing for low income residential use. Title II restricts the right of an owner of eligible low income housing to prepay its mortgage and terminate the mortgage insurance contract and

authorizes HUD to provide incentives to the owner (or purchaser, if the project is to be sold) in exchange for continuing the low income use of the housing. Title II was enacted as a temporary, emergency measure and was superseded by Title VI in 1990. Title VI serves the same purposes as Title II, but provides a much more definitive statutory framework for administering the preservation program.

The Department's position regarding Title VI is that public entities are eligible to purchase Section 236-insured projects pursuant to a Title VI plan of action. The basis for this position is set forth in the preamble to the proposed regulations amending 24 CFR part 248 and implementing Title VI which states:

Section 236(j)(4) of the National Housing Act, 12 U.S.C. 1715z-1, provides that a mortgage is eligible for insurance under section 236 only if executed by a "private mortgagor" eligible under section 221(d)(3) or section 221(e). However, recent legislation, including title VI, makes clear that Congress intends State and local government agencies to be eligible purchasers of section 236 projects in the context of plans of action under subpart B of part 248. Section 203(a)(1) of the HUD Reform Act amended section 236(b) to provide that interest reduction payments may be made with respect to a mortgage on a project owned by a public entity,.... The legislative history of the HUD Reform Act indicates that these amendments were included in the Senate bill to "(make) public entities eligible mortgagors to acquire section 236 projects." Cong. Rec. H9686.... The inclusion of State or local government agencies in the definition of priority purchaser under section 231(a) of title VI is further evidence of Congressional intent in this regard. Therefore, under the proposed rule, State or local government agencies can be priority purchasers with respect to section 236 projects as well as other eligible low income housing projects. 56 FR 20268.1

While Title VI never explicitly states that public entities may purchase Section 236-insured projects, such a conclusion also may be drawn from an analysis of the preservation process established under that title.

1 It should be noted that this statement applies only to projects sold pursuant to plans of action approved under Title VI, which has been implemented as subpart B of part 248. Subpart C of part 248, which implements Title II, is not covered by this statement.

Those projects which are eligible to file a plan of action under Title VI include 236-insured, 236-noninsured, 221(d)(3)-

assisted and 221(d)(3)BMIR projects. Throughout Title VI, the projects are collectively known as "eligible low income housing." No distinction is ever made between the different programs under which these projects are assisted or insured. This implies that Congress intended that all eligible low income housing would be treated in the same manner throughout the preservation process. Indeed, all eligible low income housing is required to comply with the same sales procedures, set forth in sections 220 and 221 of Title VI, when an owner elects to sell the housing pursuant to a Title VI plan of action.

Section 231 of Title VI specifies two different types of potential purchasers of eligible low income housing; priority and qualified purchasers. Priority purchasers are resident councils, any nonprofit organization, or state or local agencies. Qualified purchasers are any other type of entity which agrees to maintain the use restrictions on the project, including priority purchasers and for-profit entities. Under the voluntary sale provisions of Section 220 of Title VI, an owner may choose whether or not to accept any bona fide offer it receives from a priority or qualified purchaser. Under the mandatory sales provisions of Section 221, an owner who receives a bona fide offer from a priority purchaser is obligated to accept that offer. No exception to this obligation is created for an owner of a Section 236-insured project which receives a bona fide offer from a priority purchaser which is a state or local agency. This supports the position that Congress intended that all eligible low income housing would be treated in the same manner under Title VI.

In comparison to Title VI, Title II does not identify potential purchasers of eligible low income housing. Its only mention of sales of eligible low income housing is to require that the plan of action include "a description of any change in ownership that is related to prepayment...." No further guidance is provided on this issue in either the statute or the regulation in the existing part 248. Unlike Title VI, an owner of eligible low income housing under Title II is not required to comply with a sales process imposed by statute which establishes specific time periods for the sale, identifies the potential purchasers, or requires an owner, in certain cases, to accept the first offer it receives. Title II permits an owner to create its own deal, subject only to the existing TPA requirements and HUD approval of the plan of action. The failure of Title II to establish any specific framework for the sale of eligible low income housing implies that Title II was not intended to amend any existing program requirements or to exempt eligible low income housing from those requirements.

4

In his letter of January 8, 1992 to Jim Wiley of the Housing Authority, Waller Taylor, Esq., of Reed McClure, claimed that there should be no differentiation between sales under Title II and Title VI since Title VI supersedes Title II. We disagree with Mr. Taylor. While it is true that Title VI supersedes Title II, Title VI provides certain owners of eligible low income

housing with the option of choosing between Title II and Title VI. (Hidden Village Estates is one of the projects which has the option of switching to Title VI.) This option was provided specifically because the two programs are different. Projects are still being processed under the Title II regulations and will continue to be governed by those regulations for as long as the low income use restrictions remain on the project. To this extent, Title II is still in place.

Mr. Taylor also stated in his letter that his discussions with the Department and the House Subcommittee on Housing indicate agreement that the failure to amend Section 236(j) to include public mortgagors was a legislative oversight. Even if this is the case, there still is not sufficient legal support for interpreting Title II as permitting public entities to become Section 236-insured mortgagors.

John Blankinship, of the law firm Montgomery, Purdue, Blankinship and Austin, in his letter of February 5, 1992 to Jim Wiley, argues that Title II implicitly permits public entities to become Section 236 mortgagors because Section 224(a)(7) of Title II authorizes the Secretary to take such actions "authorized in other provisions of law" to facilitate a transfer of sale of the project to a qualified purchaser. He claims that since public entities may become Section 236 mortgagors under Title VI, this type of transfer is contemplated by Title II as "authorized in other provisions of law." However, because Title II was enacted prior to Title VI, Congress could not have intended HUD to take actions under Title II which did not exist when Title II was enacted.

I understand your concerns that it would be costly for the Housing Authority to form a private entity to purchase the project under Title II and that it would be time consuming to attempt to purchase the property under Title VI. Another option you may wish to consider would be to pay off the Section 236-insured mortgage at the time of the transfer, thereby permitting the Housing Authority to obtain ownership of the property without becoming a mortgagor of a Section 236-insured mortgage.

If you have any further questions regarding this matter, please contact Susan M. Sturman at 202-708-3667.

Very sincerely yours,

5

John J. Daly
Associate General Counsel
Insured Housing and Finance

cc: Bud Albright