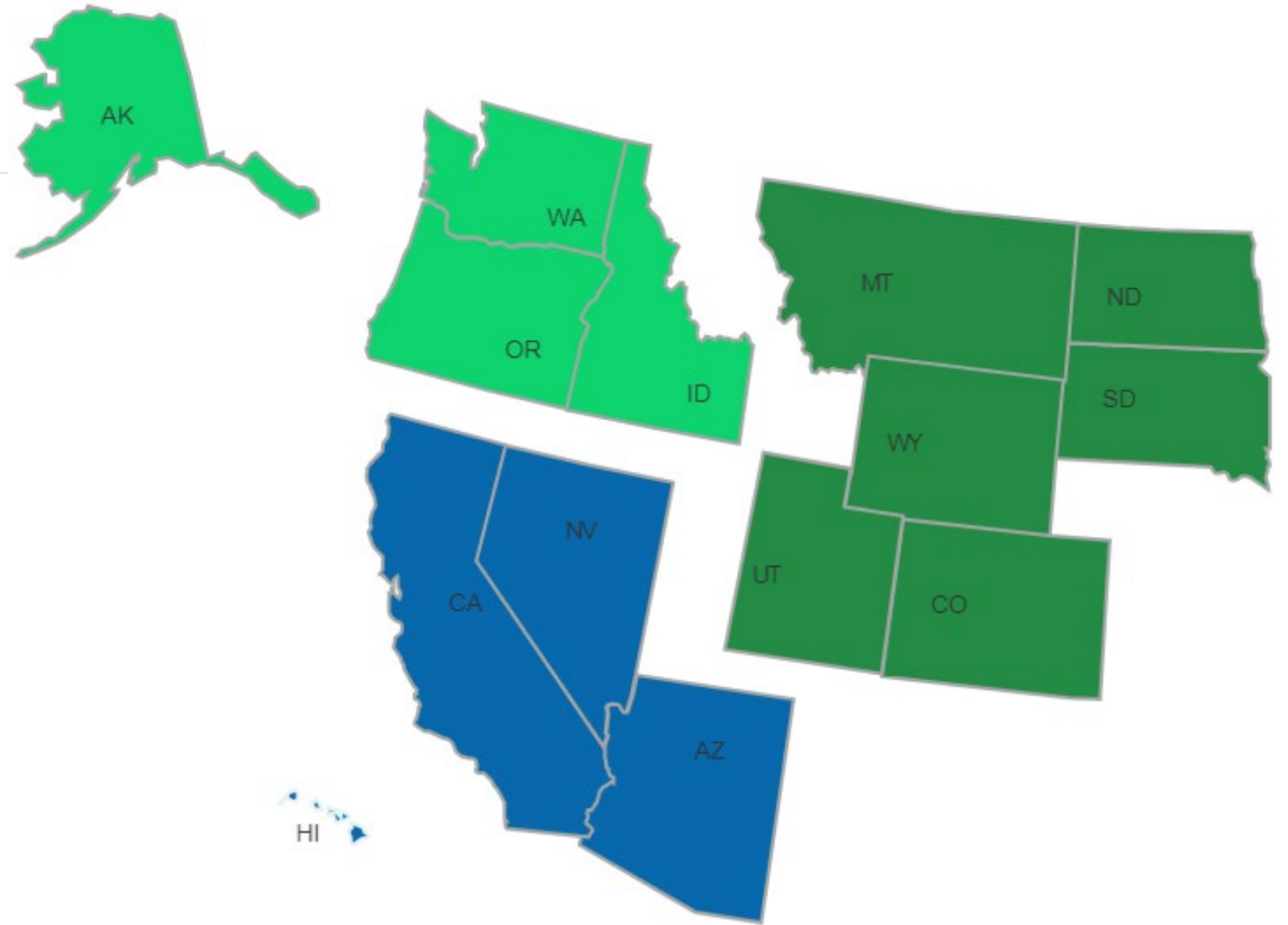


Tending the Herd

Asset Management Topics



Asset Management Topics

NSPIRE

Transfer of
Physical
Assets

10-year
PCNA
Renewals

Property
Insurance
Waivers

National Standards for the Physical Inspection of Real Estate (“NSPIRE”)

What is NSPIRE?

Notices

Inspection Types

Inspectable Areas

NSPIRE in the West Region



National Standards for the Physical Inspection of Real Estate (“NSPIRE”)

- New physical inspection model that aligns multiple HUD programs to a single set of inspection standards
- An innovative approach for developing, updating, and adapting standards and scoring based on continuous learning and improvement
- Inspectors for HUD-assisted and HUD-insured housing will be able to conduct objective, defensible, and consistent assessments to evaluate housing conditions and therefore promote better living conditions for residents
- NSPIRE focuses on the condition of the dwelling unit and modernizes and streamlines HUD’s physical inspection process. Dwelling units must pass inspection.



NSPIRE – Notices

- Noticing of information gathering and for public comments on this new rule began in 2019
- Several Notices were published between 2019 and 2023 on various aspects of NSPIRE
- https://www.hud.gov/program_offices/public_indian_housing/reac/nspire/notices
- Final Rule was published May 11, 2023
- NSPIRE is effective as of October 1, 2023 for MF properties

NSPIRE – Notices (continued)



NSPIRE – Inspection Types



Self-Inspections: Property Owner / Management Agent will inspect all units annually and report deficiencies to HUD. This inspection type is to gain a reasonable level of confidence in results and to ensure work orders are being generated.



NSPIRE Inspections: Contract Inspectors and PHAs conduct periodic inspections every 1 - 5 years depending on previous inspection score. There will be a high sample rate at the property to gain a greater level of confidence in results.



NSPIRE Plus Inspections: HUD Federal and Contract Inspectors will conduct an inspection when requested or triggered by poor conditions. Depending on the trigger, the highest sample rate will be chosen to gain the highest level of confidence in results.



NSPIRE - Inspectable Areas



Unit– interior components of an individual dwelling, where the resident lives.



Inside– common areas and building systems within the building interior and are not inside a unit. This could include interior laundry facilities, workout rooms, and so on.



Outside– building site, building exterior components, and any building systems located outside of the building or unit. This includes things like playgrounds, sidewalks, and air-conditioning units.



NSPIRE in the West Region



Several Demonstration
Properties



10 official NSPIRE Inspections
to-date

Transfer of Physical Assets (“TPA”)

What is a TPA?

Full vs. Modified Review

TPA Key Documents

TPA Best Practices

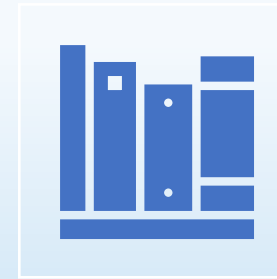
Transfer of Physical Assets (“TPA”)



TPA is HUD speak for (i) deed transfer of a Project or (ii) the transfer of interests in the Borrower (and sometimes in the upper tiers of the Borrower’s organizational structure) subject to a HUD-insured (or HUD-held) loan.



TPAs are governed principally by (i) HUD Housing Handbook 4350.1, Chapter 13 (“TPA Guide”) and (ii) Application for Transfer of Physical Assets (TPA) (HUD Form 92266) (“TPA Application”).



Per the TPA Application “If there appears to be a conflict between what is written here and the Handbook, the Handbook governs.”

TPA – Threshold Issues with the HUD Guidance

- Unfortunately, like the entirety of HUD Handbook 4350.1, Chapter 13 is woefully outdated and reflects an outdated view of the way in which Projects are owned which does not – in my view – reflect the all to common multi-tiered ownership structure we often have today.
- The TPA Application does not include a number of documents typically required by HUD or lenders. For example, it does not reflect credit reports and other items necessary for lenders to perform their mortgage credit analysis.
- Oddly, there is no standard Multifamily TPA Checklist meaning different Account Executives, HUD Counsel, and Lenders can and do require different documents for the same transaction.

TPA – Is TPA or Only 2530 Approval Required

- One of the great unsolved mysteries in the TPA Guide. “Corporate restructuring mergers if there is no change in control, or first user syndications prior to final endorsement” do not require TPA approval. I have never spoken with anyone who really knows what those mean.
- But arguably many changes in the organizational structure of Borrowers do not require TPA approval if those changes do not result in a new party being in control of the Borrower.
- Certain changes may not even require HUD 2530 approval if there are new Controlling Participants.

TPA – Lender’s Role or Lack Thereof

- Lenders are ultimately responsible for servicing a loan – most especially if the loan goes into default after a TPA has been approved – but Lenders are largely cut out of the formal TPA approval process. Contrast the Multifamily TPA Process with ORCF’s Change of Ownership or Change of Operator requirements which requires a Lender’s Narrative and submission by the Lender through the ORCF Portal. In fact, TPAs are often submitted directly to HUD without the Lender being aware of their submission until after the fact.
- Prudent Lenders should provide a role for themselves in the TPA process through provisions in a Lender’s Commitment or under their Engagement Letter with the Original Borrower/Seller.

TPA – Full Review and Modified Review

- Under the TPA Guide, Full Review TPAs include (i) a deed transfer of a Project, (ii) transfer of interest in a partnership borrower which causes a dissolution under state law [NOTE: It does not expressly address LLCs], and (iii) transfer of 100% of the beneficial interest in a passive trust which results in a change in control of the project.
- Modified Review TPAs include essentially all other transfers which result in a change of control of a borrower including changes in the general partners. NOTE: LLCs are not expressly addressed.
- In theory, Modified Review is supposed to be a “limited review”, of certain transactions involving transfers of interests in entities owning properties encumbered by HUD-insured, or HUD-held mortgages.

TPA – Full Review and Modified Review

- In reality, “Full TPAs” are often much more simple than “Modified TPAs.” [Like Francis Albert Sinatra, the middle name Review is typically dropped]
- NOTE: The TPA Application does not include any distinction between, or even any mention of, Full and Modified TPAs.
- But the 22 documents listed in the TPA Application – see attached TPA Application - most closely follow the documents typically needed for a Full TPA.

TPA – Substance Over Form: Is There a New Borrower?

- The key distinctions in my opinion are whether (i) there will be a deed transfer of the project requiring the loan to be assumed or (ii) the borrower will remain the same without a need for the loan to be assumed, but there will be change in the ownership interests in the Borrower – at one or tiers, which changes the control of the Borrower. As noted above, a change in ownership which does NOT result in a change in control, should in theory only require HUD 2530 approval.
- Another key distinction is whether they will be change in the management agent.

TPA – Key Documents – Purchaser’s Letter

- The letter is a roadmap of the TPA. At minimum, it should:
 - Identify the purchaser and its principals,
 - Indicate whether the transaction involves a deed transfer and assumption of the loan,
 - Describe the purchase price and all financial consideration to the seller,
 - Indicate the loan is current or, if not, describe how the loan will be brought current,
 - Indicate there are no outstanding physical needs of the project or how such needs will be addressed,
 - Indicate whether there will be change in management,
 - Address the Determinative Criteria, if applicable.

TPA – Key Documents – Determinative Criteria

- Determinative Criteria must be satisfied in all Full TPAs and in certain Modified TPAs :
 - Purchaser and its principals must obtain 2530 approval
 - Satisfactory management, including approval of new management agent, if applicable. HUD is encouraged to review management even if there is no change in management agent.
 - Determination that Physical Repair/Replacement Needs will be met, including addressing items reflected in the PCNA
 - Determination that a Project's Financial Needs will be met, including bringing the loan current if the loan is in default.

TPA – Key Documents – Previous Participation and Organizational Charts

- See HUD form 2530 and Previous Participation Processing Guide for complete details.
- In addition to satisfying the HUD 2530 requirements, the Organizational Chart is key to Lender for determining who needs to undergo mortgage credit analysis and recommending a new Section 50 Party under the Regulatory Agreement, if required.

TPA – Key Documents – Purchaser’s Resume

- These are needed for any parties who will exercise control over or otherwise be principals of the purchaser/new borrower.
- The resumes must demonstrate satisfactory experience in owning and operating multifamily projects. There is no requirement for prior experience with HUD regulated projects.
- Practically speaking, the “resumes” are often a link to bios on a company’s website.

TPA – Key Documents – Purchase and Sale Agreement

- There is no required HUD form or any required “HUD Provisions,” but the Purchase and Sale Agreement (PSA) must expressly provide, as applicable, that the project or interests in the Borrower, will not be transferred until after HUD TPA Approval has been received.
- Practice Tips:
 - The Closing Date should reflect that HUD TPA Approval plus closing often takes 90 to 120 days from submission of the TPA Submission Package.
 - Replacement Reserve and other escrows will remain with the Project. PSA should be clear whether reserves are part of the purchase price or will be purchased dollar for dollar in addition to the purchase price.

TPA – Key Documents – Assignment and Assumption Documents

- Documents for the purchaser to assume the loan documents and Regulatory Agreement, if applicable. Typically, these are drafted by the Lender's counsel.
- Allonge, Assignment and Assumption of Note.
- Assignment and Assumption of Security Instrument.
- Assignment, Assumption and Modification of Regulatory Agreement. This will reflect the new Section 50 party.
- UCC-3 Amendments naming purchaser as debtor, or Stat UCC-1 if purchaser is organized in a different state than seller.

TPA – Key Documents – Management Documents

- If there will be a change in Management Agent.
- 2530 for Management Agent.
- Management Agreement, including HUD provisions.
- Management Certification (HUD 9839a or 9839b.)
- Management Entity Profile (HUD 9832) and Management Agent Resumes, if Management Agent is not already approved by applicable HUD office.
- Affirmative Fair Housing Marketing Plan (HUD 935.2A)

TPA – Key Documents – Title Insurance Policy

- If the loan is assumed, either a new Title Policy or a Title Endorsement insuring the ownership of the purchaser and assumption of the loan pursuant to the recorded assignment and assumption documents.
- The Date of Policy, not just the Date of Coverage, needs to be the date on which the documents are recorded.
- If a new Title Policy, it must contain all the original endorsements.
- A new survey is not typically required, but if one is obtained, the new survey should be reflected in the survey endorsement.

TPA – Key Documents – Purchaser’s Organizational Documents

- Just like for a new loan, the organizational documents of the purchaser must be consistent with the organizational chart and 2530 filing and contain the HUD Provisions.
- Although not expressly required under the various HUD guidance, the purchaser should provide an incumbency certificate, an authorizing resolution, operating agreement or partnership agreement, and good standing certificates like for a new loan.

TPA – Key Documents – PCNA

- As part of meeting the “Determinative Criteria,” the TPA Guide requires the physical condition of the project to be determined in one of two ways (i) by an acceptable HUD inspection not more than 12 months old if the TPA involves a “troubled or potentially troubled project or (ii) by a third-party inspection report.
- The first criteria is sometimes satisfied by a recent passing REAC inspection. The second by a new PCNA. If the TPA involves a new PCNA, the new PCNA involves all the issues discussed concerning the 10-year PCNA.

TPA – Best Practices – Kick Off Call

- Shortly after receiving a request for a transaction which is arguably a TPA, the Lender should be sure it understands the scope of the transaction – I suggest requiring a Purchaser’s Letter or an equivalent email.
- There should be a kick-off call involving the Lender, Lender’s counsel, and at least the purchaser and its counsel. If the seller is not on the call, the Lender should confirm with the seller’s the seller’s consent for the Lender to have a call with the purchaser.
- The kick-off call should review the TPA requirements, agreed upon TPA checklist – including mortgage credit items - and responsible parties, requested timing, Lender’s fees, Lender’s counsel fees, etc.

TPA – Best Practices – Outreach to HUD

- Following the kick-off call, the Lender should notify the HUD Account Executive, provide an overview of the transaction, estimated timing, and reach agreement on the items to be required by HUD.
- Some Account Executives like to have a call with the purchaser as well as the Lender.
- Typically, HUD Counsel will not be assigned until after the TPA Package is submitted. However, if there are items such as new tax credits, secondary financing, etc. a referral to HUD Counsel should be requested prior to submission of the TPA Package.

TPA – Best Practices – Timing

- If the purchaser and its counsel are experienced with HUD, I estimate 30 days to prepare the TPA Package. That period is longer if the purchaser and its counsel are new to HUD.
- I typically estimate 60 to 90 days to receive HUD Preliminary TPA Approval from the time a TPA Package is received by HUD.
- Following receipt of the HUD Preliminary TPA Approval Letter, closing typically occurs within 30 days unless there are unusual conditions contained in the Preliminary TPA Approval Letter.
- So perhaps 90 to 120 days to close from the initial Kick-off call.

TPA – Best Practices – Closing

- The parties are free to close any time after receipt of the HUD Preliminary TPA Approval Letter provided the conditions in the Preliminary TPA Approval Letter are satisfied.
- HUD typically is not involved in setting a closing date.
- The longest lead items are often arranging for HUD's execution of the Assignment, Assumption and Modification Agreements and other any documents HUD needs to sign. For example, an Assignment and Assumption of HAP Contract if the Project has a HAP Contract.
- Typically, the purchaser has 45 days to submit the documents required for HUD Final TPA Approval.

10-year PCNA Updates

Housing Notice 2023-03

10-year PCNA Update Process

10-year PCNA Update Best Practices

Common Issues and Creative Problem Solving



Housing Notice and HUD eTool Training

- Housing Notice 2023-03, “Capital Need Assessment (CNA) eTool for Asset Management” was issued on 3/29/2023 to the special attention of Multifamily Directors and Account Executives, as well as to Multifamily Owners and Management Agents. The Notice remains in effect until amended, superseded or rescinded.
- The Notice details the policy for submission and review of Capital Needs Assessments required for 10-year updates for Federal housing Administration insured properties, RAD Conversions, and several eligible asset management milestones.
- The use of the CNA eTool is required for all CNA submission, with a limited number of exceptions.



10-year PCNA Update - Applicability

This notice applies to all FHA-insured properties that have a 10-year CNA update requirement (active Regulatory Agreement):

- RAD Conversions
- Housing Assistant Payment contract assignment (HAP Assignment) requests where HUD has requested a CNA
- Budget Based Rent Increase (BBRI) for 202/811 Project Rental Assistance Contracts (PRAC)
- Partial Payment of Claims (PPC)
- Transfer of Physical Assets (TPA).
 - Is only required for properties that consistently have an underfunded RR account, have 2 consecutive under 60 REAC scores or are considered troubled or potentially troubled assets

The CNA eTool is not required for non-insured properties that have thirty (30) units or less. FHA-insured properties, regardless of size, are subject to the requirements in the notice.



10-year PCNA Update – Process

- The lender is required to hire a third-party needs assessor to conduct the CNA at the property.
- For those properties that do not have a servicing lender, the owner must hire a third-party needs assessor to conduct the CNA who will fulfill the role of lender in consulting with the owner and use the CNA eTool to submit to HUD.
- Upon completion of the CNA, the lender must review the CNA and notify the owner of any immediate repair needs, potential issues, and the new calculated RfR deposits.
- The owner and lender must work together to address and resolve any issues noted in the CNA. Once these issues are resolved, the lender should submit the final CNA to HUD through the CNA eTool.



10-year PCNA Update – Process (cont.)

- The submitted CNA will be assigned to a HUD Account Executive (AE) for review and analysis. In the West Region the AM staff then requests an assignment from the Tech Branch for a Construction Analyst (CA), who is then assigned to review the CNA.
- The CA addresses any flags and deficiencies in the report and once it is finalized, the report findings are submitted to the Account Executive.
- The CA focuses the review on verifying the correct number of units were inspected, analyze all business flags, financial factors, and repair schedules, such as RfR deposits, critical and non-critical repairs, attachments, and other system generated reports.



10-year PCNA Update

- Every 10 years from the date of final endorsement or other events triggering a CNA, one shall be performed on the Property by the lender at owner's expense.
 - May be treated as an eligible project operating expense,
 - It may be paid out of the RfR escrow as an eligible project operating expense,
 - Eligible cost of financing for refinance applications.
- TPAs or HAP Assignments: the purchaser is typically responsible for the CNA's cost.
- Lenders and Owners need to adequately plan for repair and maintenance needs that will occur in years 11-20. Might need higher initial and monthly deposits to ensure the borrower has sufficient funds to cover critical and non-critical repairs. This is especially important for subsidized or income-restricted properties which have only a limited opportunity to increase revenue or secure additional capital funds.




10-year PCNA Update – Process (cont.)

- If the RfR account balance is insufficient to fund all the required repairs identified in the CNA submittal, or if the property cannot afford the suggested increase to the RfR deposits, the CNA may be conditionally approved subject to a plan to bring the property in to compliance.
- Properties that receive conditional approval shall be required to have a Corrective Action Plan (CAP) which shall be documented in the Multifamily Housing Action Plans section of iREMS.
- The CAP will be developed through a collaboration between the owner and AE to prioritize the necessary repairs to ensure a reasonable completion schedule is agreed upon and implemented.



10-year PCNA Update – Best Practices

- Process should start 90 – 120 days prior to due date of the 10-year PCNA
 - Initiate contact with the Borrower early to ensure sufficient time to complete process and address unforeseen issues
 - Engage PCNA provider and hold kickoff call with Owner and Management Agent to review process and timeline
 - Review draft PCNA report with Owner and Management Agent



10-year PCNA – Best Practices


- Kickoff Call
 - Site Inspection Requirements
 - Identify point person to schedule/facilitate site inspection
 - Discuss any completed and proposed repairs for the property
 - Identify types of repairs typically paid out of operating funds
 - Discuss any deferred maintenance or repairs needed at the property
 - Discuss the potential for accessibility issues with regards to FHA and UFAS due to more rigorous interpretations of these standards
 - Discuss any potential lower costs that the property may have for R4R items
 - Review prior disbursement history and prior RR schedule



10-year PCNA – HUD Inspection Requirements

Per the requirements of the CNA e-Tool:

- Need to inspect 25% of the units, including ~25% of each building and ~25% of each layout (e.g. 1Br, 2BR, etc.)
- Need to inspection 100% of accessible, vacant, and down units
- Documentation in advance of the site visit is critical
 - Presurvey Questionnaire with site details and information
 - CAP-Ex expenses vs. operational expenses (e.g. general ledger)
 - R4R reimbursement history/summary of items reimbursed from RR from past 10 years (HUD Form 9250)
 - Prior PCNA report
 - Rent roll
 - Building permit and certificate of occupancy for 1990, 1991 and 1992 properties
 - Building plans whenever possible especially for post 1991 construction
 - ALTA survey



10-year PCNA – Best Practices

- Draft PCNA Report Review
 - Critical Repairs
 - Non-Critical Repairs
 - Accessibility Repairs
 - Replacement Reserve Schedule
 - Any Report Revisions
 - Hold call with all parties (Borrower, Lender, Consultant) to identify issues and coordinate solutions.



10-year PCNA Update – Common Issues

- Significant increase in annual deposits and property's ability to afford
 - Are there items in the RR schedules that can be moved to operational expenses due to historical treatment of such items (e.g. flooring, appliances)
- Completion of accessibility repairs and development/implementation of Corrective Action Plan (CAP)
 - If residents do not want changes made to their unit, accessibility repairs should be included in CAP to be completed during tenant turnover or at request of a specific tenant
 - Since there are no renovations or new money for a 10-year PCNA, accessibility repairs should be deferred and money included in CAP to be completed during future renovations or refinance



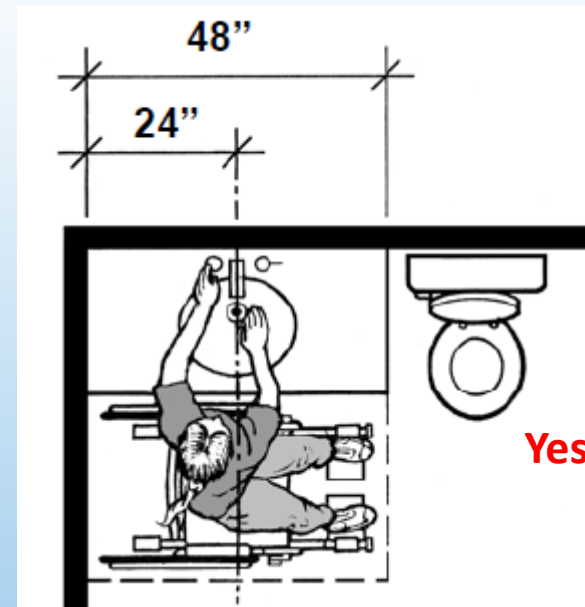
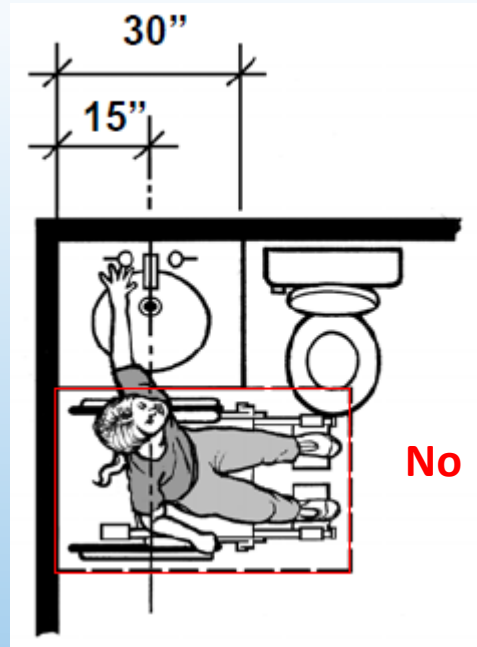
10-year PCNA Update – Creative Problem Solving

- Lender Involvement
 - Evaluate Capital Resources Available (owner contribution, surplus cash, secondary financing)
 - Maintain an open line of communication between PCNA Analyst, Borrower, and HUD
- Reserve Analysis
 - Review prior PCNA, reimbursement history, REAC, and financial statements
- Accessibility issues not identified in original PCNA
 - Corrective Action Plan (CAP) for future repairs
 - Removable front vanities (clear floor space at sinks);
 - Lowered countertop workspace in kitchens;
 - Reversing door swings in bathrooms to allow for proper clear floor space;
 - Widening doors or replacing hinges with offset hinges to allow proper clearance;
 - Converting units to be fully accessible (UFAS/504 for older projects);
 - Typically the CAP includes the specific repairs and costs required as well as the estimated timeline to complete the repairs
 - See examples on following slides

10-year PCNA Update – Creative Problem Solving

Clear floor space at sinks

- Sinks that do not have knee clearance must have a 30" x 48" parallel clear floor space centered on the sink basin.





10-year PCNA Update – Creative Problem Solving

Bathroom clear floor space issues

NON-COMPLIANT Parallel approach



NON-COMPLIANT Frontal approach without removable cabinetry



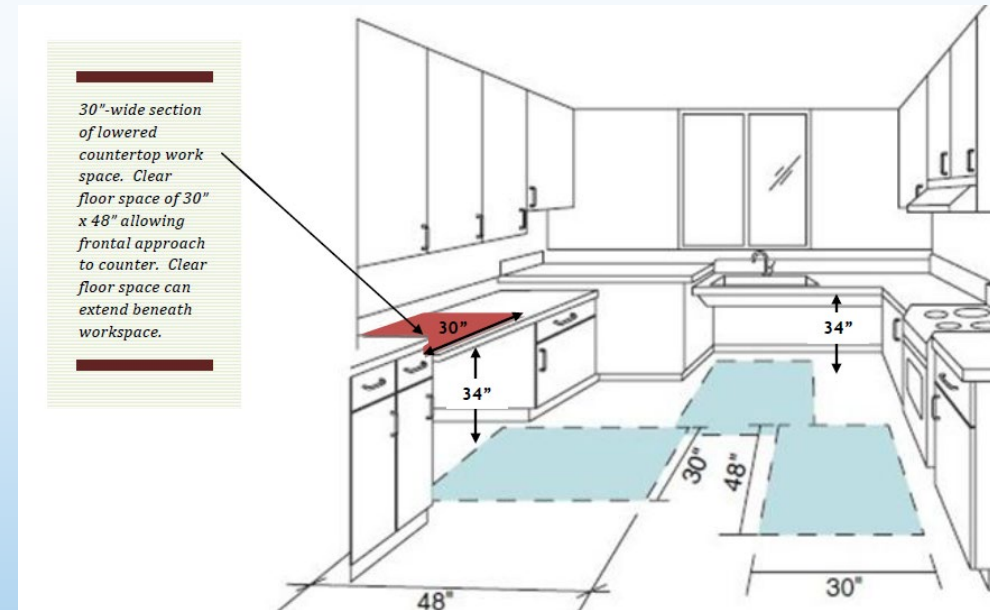
COMPLIANT Frontal approach



10-year PCNA Update – Creative Problem Solving

Countertop Work Space in Kitchens

30" wide section of countertop workspace that is no more than 34" above finished floor with knee space beneath is required in accessible unit kitchens.



10-year PCNA Update – Creative Problem Solving

Countertop Workspace Alternative Designs





e-Tool

- HUD e-Tool training is not yet formalized for asset management field staff
- There are some recorded tutorials for HUD staff found on YouTube
- We expect e-Tool and CNA review training in the field within the next 6 months or sooner

(Property) Insurance Waivers

Overview

Property Insurance Waivers - Process

(Property) Insurance Waivers



Some regions of the U.S. are experiencing major natural disasters on an increasingly frequent basis



Insurance companies are increasing rates and deductibles that exceed HUD policy requirements



HUD can waive certain program provisions – work with your Production or Asset Management staff at the appropriate stage of application review or servicing renewal obligations.



(Property) Insurance Waivers - Process

- Submit a written request to the assigned Account Executive for a waiver of specific program requirements
 - Cite which requirements you are waiving under MAP Guide 3.9.2
- Include documentation demonstrating the property has attempted to obtain insurance in line with HUD's requirements, which state deductibles may not exceed the greater of \$50,000 or 1% of the insurable value for any particular building, up to a maximum amount of \$250,000.
- Borrower may be required to place into an additional reserve account the amount equal to the difference between the maximum deductible of 1% and the deductible amount approved for each building. It shall be held for as long as the FHA mortgage insurance remains in place.