



Section 236 Decoupling Updates **(HUD Notice H 00-8 as extended by Notice H 01-05)**

(As of 03/01/02)

In the opening statement of Notice H 00-8, HUD indicates that it would consider making changes to the IRP Decoupling processing guidelines upon gaining more experience with these transaction types and understanding the tools that are critical to successful recapitalizations under this program. Since issuance of HUD Notice H 00-8 in May, 2000, HUD has revised and clarified certain provisions of the Notice which has resulted in some significant program changes that improve the viability of these IRP Decoupling Transactions.

The most notable policy changes and clarifications concern Multifamily Accelerated Processing ("MAP), Rent Caps, Rent Increases, Section 8 Contract Administration, Preservation Projects, and Debt Deferral.

MAP. MAP lenders may now apply to refinance and decouple Section 236 mortgages using MAP under Section 223(f), 221(d)(4) or 221(d)(3). Though HUD has always maintained that these transactions could be refinanced and processed under Traditional Application Processing (TAP), MAP processing was prohibited until Michael McCullough, Director of Multifamily Development in HUD Headquarters, issued a memorandum in March, 2001 allowing the use of MAP in connection with Section 236 Decoupling transactions. However, until MAP guidelines are published to provide instruction regarding the processing of these loan types, HUD Headquarters review and approval of the underwriting is required.

Rent Caps. HUD will now permit projects to increase rents to comparable market levels – *without subtracting the IRP subsidy* – provided that the calculation is based on a budget-based procedure. This procedure, however, may not be used where an "immediate" equity takeout is proposed or where the purchase price for the project is above market comparables. Shaun Donovan's 2/21/01 Memorandum to HUB Directors acknowledges that HUD's IRP "ding" requirement outlined in Notice H 00-8 precludes some projects from undertaking these transactions due to the low market areas in which they are located or their significant repair needs. By allowing owners to obtain full market rents *and* continued Interest Reduction Subsidies, HUD now provides owners with a powerful financial resource that will undoubtedly spur increased IRP decoupling activity and lead to the rehabilitation and preservation of many more Section 236 properties.

Rent Increases. Shaun Donovan's 11/06/00 memorandum to HUB Directors clarified policies surrounding HUD field offices' authority to approve rent increases. Multifamily HUB Directors have the authority to approve the following rent increases:

- Section 8 Mark Up to Market rent increases, subject to Mark Up to Market processing guidelines.
- All budget-based rent increases on Section 8 units.
- Rent increases of 10% or less on non-Section 8 units.

HUD Headquarters retains the authority to approve rent increases where they exceed 10%.

The 11/06/00 memorandum also specified allowable expense items that can be included in budget-based rent increases. New debt service, reasonable debt service coverage and Section 236 oversight monitoring fees may be included in HUD's budget-based rent increase calculation. However, if an agency performs both the Section 8 Contract Administration function *and* the Section 236 oversight monitoring role, it may receive a fee for only one of these services.

Section 8 Contract Administration. Given that HUD has either contracted with entities to do Performance-Based Section 8 Contract Administration ("CA") or is in the process of contracting with other entities to perform similar services for all other states, HUD has decided that all new contract administration functions will be given only to the state-wide entity that has been selected to perform these functions. To the extent that HUD has not yet selected the state-wide CA, HUD will perform the CA functions until the state-wide CA is in place. This changes HUD's original policy outlined in Notice H 00-8 which allowed any public agency to administer the HAP contract provided that they had the capacity and experience to do so.

Preservation Projects. HUD has indicated that it considers ELIHPA or LIHPRA use restrictions to be at least equal to those restrictions imposed by the IRP Use Agreement. As such, the Department will allow the existing Preservation Use Agreement to remain in effect as long as there is no rent increase provided in connection with the IRP transaction, and the property, its residents and HUD are in the same or better position. The term of the use agreement will, however, be extended by five years as required by the governing statute.

Debt Deferral. Though relatively clear in H 00-8, HUD confirmed that Multifamily HUB Directors have the authority to defer Flexible Subsidy Capital Improvement Loans, Section 241 Loans and Section 106(b) loans in cases where it has been determined that deferral is a necessary component of the IRP transaction due to insufficient financial resources. Flexible Subsidy Loans that are considered "Operating Assistance Loans" may be deferred only if the HUB Director recommends and HUD Headquarters approves a good cause waiver.