

## HUD's Mark Up to Market Program For Profit-Motivated or Limited Distribution Mortgagors

By

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Originally introduced as an Emergency Initiative in June 1999 to provide incentives for owners to maintain Section 8 project-based assistance at properties in strong markets, The Mark Up to Market Program has become a critical preservation tool for both owners and HUD. The Mark Up to Market Program became permanent under Section 524(a)(4)(A) of the Multifamily Assisted Housing Reform and Affordability ("MAHRA") Act in FY 2000, solidifying HUD's commitment to preserving its dwindling privately-owned affordable housing stock. Under this program, owners now have the ability to obtain the *comparable market-rate* rent levels for all units covered under a project-based Section 8 contract *and* distribute the increased cash flow resulting from such rents. These incentives provide owners with an effective tool to recapitalize and preserve their properties as affordable housing.

Chapter 3 of the Section 8 Renewal Guide published in January 2001 provides the latest guidance on this program.

### **Eligibility.**

To be considered as "entitled" to participate in the Mark Up to Market program, properties must meet the following criteria:

- A Section 8 contract that has received its initial renewal under MAHRA;
- A Real Estate Assessment Center ("REAC") physical inspection score of 60 or above with no uncorrected Exigent Health and Safety violations;
- Ownership that is a profit-motivated or limited distribution entity;
- Market comparable rents that are at or above 100% of the FMR potential;
- Free from low- and moderate-income use restrictions that cannot be eliminated by unilateral action by the owner. Examples are Rent Supplement Contracts, Flexible Subsidy Use Agreements, or Low-Income Housing Tax Credits.

If a property doesn't meet every one of the criteria outlined above, an owner may be eligible for consideration of a waiver *if* certain discretionary eligibility criteria are met.

### **Discretionary Eligibility.**

HUD will consider requests for participation in the Mark Up to Market program if the project meets at least one of the following three characteristics:

1. **Vulnerable Populations.** The residents of a property must be a particularly vulnerable population, demonstrated by at least 50% of the units being rented to elderly families, disabled families, or large families of five or more persons.
2. **Vacancy Rates.** The property must be located in a low-vacancy market area (or in a rural area with no comparable rental housing) where there is a lack of affordable housing and where Section 8 vouchers would be difficult to use. HUD considers this criteria to be met if the vacancy rate is less than three percent.
3. **Community Support.** The property must be a high priority for the local community as demonstrated by a contribution of state or local funds to the property. This matching requirement may be in the form of tax abatements, capital improvement funds, etc.

Discretionary MUM requests must be reviewed and recommended by the HUD field office and forwarded to HUD Headquarters for final approval.

### **The Process.**

Owners must submit to HUD the required worksheets and a market-rent comparability study completed by a third-party appraiser in accordance with Chapter 9 of the Section 8 Renewal Guide. In addition, owners should provide additional documentation to evidence eligibility under Option 1A. For owners requesting MUM renewals under Option 1B, more comprehensive documentation and a narrative justification should be provided to support the request. Upon receipt, HUD will determine eligibility and then proceed to order another third-party rent comparability study to validate the owners requested rent levels. Once HUD's comparability study is completed, the two studies are reconciled. For Section 236 and 221(d)(3) BMIR properties, market rent levels will be reduced by the level of interest reduction subsidy attributable to each unit type. HUD will generally cap the new marked up rent levels at 150% of the Fair Market Rent and approve an increase in the annual distribution equal to the difference between the current rents and new marked up rents. For properties with 100% Section 8 assistance, HUD will allow owners to distribute 100% of cash flow at year-end. Once HUD approves the final market rent levels, funds are reserved for the Section 8 Contract.

### **Section 8 Contract and Future Rent Adjustments.**

Owners participating in the Mark Up to Market program are required to execute a Section 8 contract with a term of at least five (5) years. For Section 236 and 221(d)(3)



BMIR properties, owners must give up their prepayment right except in situations where HUD considers prepayment to be a critical component of a transaction that preserves the property as affordable housing. Please note, however, that owners maintain the right to prepay such mortgages prior to execution of a MUM contract, provided that the terms of the mortgage note provide this right. Many owners combine prepayment with a MUM renewal as part of a comprehensive recapitalization strategy.

After the first year, rents are increased for the next four years of the contract by application of HUD's published Operating Cost Adjustment Factor. At the end of the five-year term, the owner has the ability to (i.) terminate the Section 8 Contract, (ii.) request another five-year renewal under the Mark Up to Market Program whereby market rents are re-determined by new owner and HUD-contracted comparability studies, or (iii.) renew the contract for one-year under outstanding procedures.

The Mark Up to Market program is an effective tool that enables owners to recapitalize their HUD-assisted properties. Given that Congress made this program permanent in FY2000, HUD's strong commitment to preserving its assisted inventory is clear. Owners of Section 8 properties should strongly consider this option and HUD's Mark Up to Market Nonprofit Transfer Program before considering market-rate conversions.