

SUPPLEMENTAL LOANS
FOR
PROJECT MORTGAGE INSURANCE

SECTION 241

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A HUD HANDBOOK

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HOUSING PRODUCTION AND MORTGAGE CREDIT-FEDERAL HOUSING ADMINISTRATION

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 TABLE OF CONTENTS

Paragraph		Page
CHAPTER 1. INTRODUCTION AND ADMINISTRATIVE PROCESSING		
1-1.	Program Coverage	1-1
1-2.	Loan Amounts and Terms	1-1
1-3.	Special Provisions for Nursing Homes and Group Practice Facilities	1-2
1-4.	Application Requirements	1-2
1-5.	Commitment for Insurance - Initial Closing	1-3
1-6.	Commitment for Insurance - Final Closing	1-3
CHAPTER 2. UNDERWRITING		
2-1.	General	2-1
2-2.	Valuation Analysis	2-1
2-3.	Cost Estimation and Processing	2-2
2-4.	Mortgage Credit Analysis	2-2
* 2-5.	Land Planning Analysis	2-4
2-6.	Architectural Analysis	2-4 *

 FOREWORD

This Handbook is addressed to owners of multifamily housing subject to HUD-FHA insured mortgages, including mortgages held by the Secretary, where such owners desire to improve their projects under Section 241 of the National Housing Act. Supplemental loans may be insured by HUD-FHA to pay for alterations, repairs, additions or improvements of multifamily projects, as well as to finance the purchase of equipment for operation of nursing homes and group medical practice and intermediate care facilities.

Although Section 241 has not been used to the extent hoped for by its proponents, there has been an increased interest in the program as an additional medium for financing the purchase of equipment.

This Handbook is divided into two Chapters. The first Chapter sets forth HUD-FHA basic eligibility requirements and explains administrative processing in general terms. The final Chapter discusses underwriting considerations.

References:

- (1) HPMC-FHA 4200.15 (4480.1)* - Multifamily Reports and Forms Catalog

*The information in parenthesis indicates the location of the referenced material in the new classification system.

Cancellations: This Handbook cancels Appendix G of Sections 31, 33 and 34 contained in Volume VI, Book 2; Volume VII, Book 2; Paragraphs 72737 thru 72737.1; Paragraphs 72927 thru 72927.2; and Paragraphs 73090 thru 73090.8 of the FHA Manual.

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HUD-Wash., D. C.

CHAPTER 1. INTRODUCTION AND ADMINISTRATIVE PROCESSING

1-1. PROGRAM COVERAGE.

- a. A supplemental loan under Section 241 is defined as a loan for the purpose of financing improvements or additions to a multi-family project, a nursing home, an intermediate care facility or a group practice facility covered by a mortgage insured under any Section of Title of the National Housing Act. With respect to a nursing home, intermediate care facility, or group practice facility, the supplemental loan may also provide financing for furniture and equipment to be used in the operation of such nursing home or facility.
- b. This financing will supplement existing insured mortgages and will be available without refinancing the existing mortgage.
- c. The purpose of the supplemental loan is not to provide luxury items in a subsidized project. Neither is its purpose to provide expensive hospital type treatment equipment in nursing home projects. The purpose is to provide the HUD-FHA insured or Secretary-held project with means to keep the project competitive, extend its economic life, and provide for financing replacement of obsolescent equipment through the use of HUD-FHA insured loan.
- d. Legal Authority. The supplemental loan program is authorized by Section 241 of the National Housing Act (Public Law 73-479) as added by the Housing and Urban Development Act of 1968 (Public Law 90-448) and amended by the Housing and Urban Development Act of 1970 (Public Law 91-609); U.S.C. 1715Z-6.

1-2. LOAN AMOUNTS AND TERMS.

- a. Statutory Limits. The supplemental loan is limited in amount to not more than 90% of the HUD-FHA estimate of the cost of improvement or addition and in term to a period not longer than the remaining term of the mortgage. The maximum interest rate is presently 7%. Statutory dollar limits and statutory unit limits are applicable to the total of (1) the outstanding mortgage and (2) the supplemental loan.
- b. Insurance of Advances. Insurance of advances will be available only for supplemental loans of \$100,000 or more.

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- c. Employment, Wages, Fees and Premiums. Non-discrimination in employment and prevailing wage requirements are the same as in new projects, as are fees and premiums to be collected. In the Section 221(d)(3) BMIR program, no premium charge is applicable to Section 221(d)(3) supplemental loans.
 - d. Applicability of Mortgage Cost Limitation. It is important to notice that the 90% mortgage/cost limitation is applicable to all programs, including those which permit insurance of 100% loans to nonprofit sponsors. Note: Special provisions apply to certain supplementary loans to cooperatives.
- 1-3. SPECIAL PROVISIONS FOR NURSING HOMES AND GROUP PRACTICE FACILITIES. In Nursing Homes and Group Practice Facilities, part or all of the proceeds of an insured supplemental loan may be used to purchase equipment to be used in operating the facility.
- 1-4. APPLICATION REQUIREMENTS.
- a. Amortization Period. The Amortization Period is not to exceed the remaining term of the first mortgage.
 - b. Payment Provisions. The Level Annuity payment plan is available under all Sections of the Act.
 - c. Commencement of Amortization. Amortization should be scheduled to commence no later than three months after estimated completion of the addition or improvement.
 - d. Preparation of Commitment.
 - (1) FHA Form 2432 will be used for insurance of advances, with appropriate adjustments, the major changes being as follows:
 - (a) No working capital deposit will be required.
 - (b) Operating deficit deposits should not be required since additions or improvements which are not demonstrable as necessary and economically feasible should not be financed with insured supplemental loans.
 - (2) FHA Form 2453 will be used for insurance upon completion.
 - e. Fees. Fees are calculated at the same rates as are used in connection with insurance of first mortgages.

- 1-5. COMMITMENT FOR INSURANCE - INITIAL CLOSING.
- a. Information for closing attorney, requirements as to title evidence, assurance of completion, availability of funds for completion, in addition to working drawings and schedules of payments are unchanged from present procedures used in connection with Section 207 insured mortgages.
 - b. Preconstruction conference is required except where purchase of equipment only is involved.
 - c. Prepayment privileges and charges are the same as for Section 207 insured loans except that no provision for a charge by the mortgagee may be included in loans for \$200,000 or less. No adjusted premium charge will be due HUD-FHA in connection with prepayment of any supplemental loan or the voluntary termination of HUD-FHA insurance on the loan.
 - d. All contract documents presently required in connection with Section 207 insured mortgages are to be used in supplemental loans, including assurances of completion, property insurance requirements as well as the mortgagee's and mortgagor's certificates.
- 1-6. COMMITMENT FOR INSURANCE - FINAL CLOSING. The instructions, procedures and requirements for final closing with regard to a Section 241 Supplemental Loan are the same as those for the basic Section 207 Multifamily Rental Housing Program.

CHAPTER 2. UNDERWRITING

- 2-1. GENERAL. In processing an application under Section 241, the basic Section 207 rental housing underwriting instructions shall apply except as modified herein.
- 2-2. VALUATION ANALYSIS.
- a. A preapplication analysis will first consider whether the improvements are eligible in accordance with the above definitions. The sponsors should furnish the Assistant Director for Technical Services/Chief Underwriter with the confirmed outstanding balances of the mortgage and the estimated cost of the improvements, etc. The ADTS/CU will then make a determination with respect to the eligibility of the proposal. He must be certain that the existing indebtedness when added to 90% of the value of the improvements does not exceed the maximum amount insurable.
- b. The next consideration is the value of the proposed alteration, improvement, etc., as opposed to its cost. The analysis will consider the following:
- (1) Will the increased income, if any, offset expense and show a return?
 - (2) Will the addition, alteration, etc., extend economic life, increase occupancy, lower operating expense or, add amenities necessary to make project more competitive.
 - (3) Is the proposal to cure obsolescence?
 - (4) Is the proposal primarily for deferred maintenance? If so, it should be rejected.
 - (5) Should the reserve for replacements be used rather than a supplemental loan?
 - (6) In connection with Nursing Homes and Group Practice Facilities where very expensive equipment may be proposed, it is proper for the valuator to seek professional advice from the trade and suppliers as to the advisability, cost, etc., of equipment.

c. A supplemental project loan does not alter the usual requirements outlined in the original Regulatory Agreement. For example, there is still a prohibition for hotel and transient use. FHA Form 2264 instructions contain detailed directions for processing a Section 241 loan. See reference 1 of the Foreword.

2-3. COST ESTIMATION AND PROCESSING. Projects submitted under Section 241 are processed and estimated in accordance with basic Section 207 procedures, except as follows:

The Cost Analyst shall develop an estimate for the new improvements, additions and/or new equipment only, and record his conclusions on the applicable FHA Form 2264.

2-4. MORTGAGE CREDIT ANALYSIS.

a. Mortgage Credit procedures and analyses are to be completed in accordance with Section 207 basic instructions, except as modified herein.

b. Loan Multiples, Term and Amortization Plan - The loan shall be in even multiples of \$100, except that a loan under \$10,000 may be in even multiples of \$50. The term of the loan cannot exceed the remaining life of the insured mortgage. The amortization plan may be the same as the insured mortgage, or the Level Annuity Payment Plan.

c. Maximum Insurable Loan - The principal amount of the loan shall not exceed:

- (1) 90% of the HUD-FHA estimated value of the improvements additions, or equipment; or
- (2) An amount which when added to any outstanding indebtedness relating to the property, does not exceed the maximum mortgage amount currently insurable under the Section or Title pursuant to which the mortgage covering such project or facility is insured.

NOTE: "Outstanding indebtedness relating to the property" means the total outstanding amount of unsecured obligations of the borrower incurred in connection with improving, repairing or maintaining the property and outstanding mortgage or obligations constituting liens on the title of the property to be improved.

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- (2-4) d. Form of Security - A recorded lien against the property.
- e. Interest Rate - As agreed upon by lender and borrower, but not exceeding the maximum currently in effect for this Section of the Act.
- f. Assurance of Completion - The following requirements apply except for loans solely for purchasing equipment in nursing homes, group practice facilities and hospitals. However, nothing in the instructions shall be construed as to limit or restrict the absolute right of the mortgagee or owner to impose additional requirements.

Minimum Requirements

When:	Required:
HUD's estimated cost of construction of the improvement is \$500,00 or less	A personal indemnity agreement (Personal Undertaking Form 2459) signed by the principal(s) responsible for construction or rehabilitation of the project.
HUD's estimated cost of construction improvement is more than \$500,000 or when a personal undertaking agreement is not signed.	A performance and payment bond each for 100 percent of the HUD estimated cost of construction or rehabilitation; or a completion assurance agreement secured by 15 percent of HUD's estimated cost for construction or rehabilitation.

- g. Insurance of Advances - Loans less than \$100,000 are not eligible for insurance of advances. For loans of \$100,000, or more advances are eligible for insurance in amounts consistent with construction progress and the Building Loan Agreement signed by the borrower and lender. Prescribed procedures under basic instructions apply.
- h. Cost Certification - Mortgage credit analysis is governed by Section 241 and the procedures under basic Section 207 instructions.

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- 2-5. LAND PLANNING ANALYSIS. Land planning analysis shall conform to the basic Section 207 rental housing procedures.
- 2-6. ARCHITECTURAL ANALYSIS. Architectural analysis shall be in accordance with instructions set forth for the basic Section 207 rental housing program.
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