



ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

Date: September 7, 2022

MORTGAGEE LETTER 2022-16

TO: All Multifamily Regional Directors
All Multifamily Production Directors
All Multifamily Operations Officers
Multifamily FHA MAP Lenders

SUBJECT: Increase in Frequency of the Distribution of Surplus Cash for Non-Assisted HUD Insured Properties.

I. BACKGROUND AND PURPOSE

Surplus Cash Distributions from insured multifamily projects are governed by the HUD Regulatory Agreement (Form HUD-92466M). Section 13 of this document requires that the Borrower calculate “Surplus Cash” (as that term is defined in the Regulatory Agreement, along with the term “Distributions”) as of the last day of its fiscal year and submit a report of its Surplus Cash calculations to HUD with its required annual financial reports, pursuant to Program Obligations. The Borrower may also, at its election, calculate Surplus Cash as of the last day of the sixth month of its fiscal year.

The semi-annual distribution rule was created in the 1970s to control Distributions to owners of subsidized housing with extremely constrained operating income due to affordable rental rates (e.g., the Section 236 and Section 8 programs). The primary economic benefit of multifamily equity investment was large tax deductions, and manual bookkeeping methods precluded more frequent reporting.

Pursuant to this Mortgagee Letter, HUD will permit modification of Section 13 of the Regulatory Agreement (form HUD-92466M) to allow Distributions from Surplus Cash as frequently as monthly for eligible Borrowers. This policy is limited to FHA-insured multifamily properties not subject to a Section 8 project-based rental assistance payments contract or a HUD-held mortgage note. This policy aligns HUD’s multifamily insurance for unassisted projects with industry standards and increases its competitive standing in the lending industry.

There is no intent to modify the calculation of available Surplus Cash from current requirements, although a Borrower’s ability to take advantage of more frequent Distributions is subject to the eligibility conditions described below. This new policy is only available to eligible multifamily projects with loans endorsed after the effective date of the Mortgagee Letter. Projects with loans closed before the effective date are not eligible and HUD will not consider amendments to executed Regulatory Agreements on existing insured projects.

II. PERMITTED MODIFICATION TO THE REGULATORY AGREEMENT

Insert the following provision after the Project information and prior to the recitals toward the beginning of form HUD-92466M.

Election for Monthly Surplus Cash Distributions: _____ Yes _____ No

Only Borrowers not subject to a project-based Section 8 Housing Assistance Payments Contract or a HUD-held note may elect Monthly Surplus Cash Distributions, the eligibility requirements for which are further governed by Program Obligations.

Delete the entire Section 13 and replace with the following:

13. Surplus Cash.

a. Surplus Cash shall equal the sum of:

- (1) Project cash and cash equivalents (excluding the Reserve for Replacement account and other HUD-required reserves);
- (2) short-term investments;
- (3) project-based Section 8 Housing Assistance Payments earned but not yet received by Borrower; and
- (4) any amounts approved for withdrawal but not yet withdrawn from the Reserve for Replacements or any other reserves or escrow accounts; after deducting:
- (5) all sums due or required to be paid within the calendar month following the date as of which Surplus Cash is calculated under the terms of the Note and Security Instrument (including without limitation principal, interest, mortgage insurance premium deposits, deposits to the Reserve for Replacements and other reserves as may be required by HUD, and tax and insurance escrow deposits);
- (6) all special funds required to be segregated by this Agreement, the Note, the Security Instrument, or Program Obligations, including tenant security deposits and any other amounts held in trust for tenants; and
- (7) all other obligations of the Project payable within the next thirty days unless the obligation is paid subject to available Surplus Cash or subject funds for payment of the obligation are set aside or HUD has approved deferment of payment.

b. Borrowers that have elected not to take monthly Distributions of Surplus Cash, as indicated in this Agreement, or are otherwise not eligible for monthly Distributions of Surplus Cash, must calculate Surplus Cash as of the last day of their fiscal year; such Borrowers may also, at their own election, and if permitted pursuant to Program Obligations, calculate Surplus Cash as of the last day of the sixth month of their fiscal year. Further, such Borrowers shall

submit a report of their Surplus Cash calculation(s) to HUD with their required annual financial reports pursuant to Section 18 below.

- c. Borrowers that have elected Monthly Surplus Cash Distributions as indicated in this Agreement, and that have established and maintained all eligibility requirements pursuant to Program Obligations, must calculate Surplus Cash as of the last day of their fiscal year; such Borrowers may also, at their own election, calculate Surplus Cash as of the last day of any other month of the fiscal year if eligible pursuant to Program Obligations. Such Borrowers shall include a report of the required annual computation of Surplus Cash to HUD with the required annual financial reports pursuant to Section 18 below; such Borrowers shall maintain a record of all other monthly Surplus Cash calculations and Distributions in accordance with Section 16 below. Further, upon each required annual calculation of Surplus Cash, Borrowers under this Section 13.c. must demonstrate positive Surplus Cash or, to the extent Surplus Cash is negative, repay to Project-related accounts any Distributions taken during the fiscal year associated with the annual calculation of Surplus Cash referenced herein. Such repayment must be made within sixty (60) days of the conclusion of the fiscal year associated with the annual calculation of Surplus Cash referenced herein or such longer period approved by HUD.

These or similar revisions will be made to the next edition of the HUD-92466M issued through the Paperwork Reduction Act and will supersede this portion of the Mortgagee Letter at that time.

Note that this Mortgagee Letter, or any successor policy as contemplated by Section III below or otherwise, is made part of the “Program Obligations” referred to in Section 13.c. by the terms of that definition.

III. CONDITIONS PRECEDENT TO PERMITTING MORE FREQUENT DISTRIBUTIONS OF SURPLUS CASH

HUD’s longstanding Surplus Cash calculation and Distribution policies were developed in the early years of HUD multifamily mortgage programs. For decades these policies remained relevant as property owners relied on paper-based accounting prevalent at the time which made monthly calculations impractical. Recognizing that accounting software now permits Borrowers, lenders, and HUD to monitor finances with greater efficiency than was possible in prior decades, it became apparent that HUD could increase the frequency of Distributions with minimal negative affect to the insurance fund. However, and notwithstanding the practical rationale for permitting more frequent Distributions, HUD is also concerned that this flexibility may be exploited, and to that end, HUD has developed the following eligibility conditions that must be met for more frequent (up to monthly) Surplus Cash Distributions:

- The Borrower must be in compliance with all applicable Program Obligations and HUD business agreements with no outstanding violations relating to Borrower’s financial management and annual financial reporting obligations (e.g., unauthorized Distributions, missing, incomplete or late filing issues, etc.) and must have no more than one instance,

during the three fiscal years immediately preceding the fiscal year in which Distributions are to be made, of non-compliance with all applicable HUD business agreements.

- The project shall meet the minimum Debt Service Coverage Ratio (DSCR) established in Program Obligations as of its most recent annual financial statement.
- The project's most recent REAC inspection score(s) must be 80 or above with no REAC inspection score(s) below 60 during the three fiscal years immediately preceding the fiscal year in which Distributions are to be made.
- Newly endorsed new construction and substantial rehabilitation properties and properties with transfers of ownership (TPA) require two full fiscal years seasoning from the date of final endorsement or transfer prior to permitting monthly Distributions.
- Newly endorsed Section 223(f) properties require one full fiscal year of seasoning prior to permitting monthly Distributions unless the Borrower or its Active Principal(s) have owned at least two FHA insured projects for the prior five full fiscal years and have had no APPS flags or regulatory violations during that time. The Regional Director may approve monthly Distributions for a newly endorsed property if the Borrower or its Active Principal(s) has owned at least one FHA insured project for at least three of the prior five full fiscal years and has had no APPS flags or regulatory violations during that time and has contracted with an experienced management agent and independent auditor that HUD, in its sole discretion, deems satisfactory.
- The Borrower must perform a Surplus Cash calculation as of the end of the month prior to each month in which it proposes to take the Distribution of Surplus Cash and can only distribute Surplus Cash to the extent Surplus Cash is positive. The calculation must be signed by the Borrower and contain a Warning Certification as follows "Any person who knowingly presents a false, fictitious, or fraudulent statement or claim in a matter within the jurisdiction of the U.S. Department of Housing and Urban Development is subject to criminal penalties, civil liability, and administrative sanctions." The calculation must be preserved by the Borrower and made available for HUD inspection as required by the Regulatory Agreement.
- The Borrower must demonstrate positive Surplus Cash for any fiscal year in which monthly Distributions are made. Otherwise, as required by 13.c of the Regulatory Agreement above, to the extent that monthly Distributions were made during such fiscal year, any deficit must be repaid to the Project within 60 days after the end of the fiscal year in which monthly Distributions were made. This requirement does not extend to authorized Distributions based on the annual computation of Surplus Cash for the prior fiscal year.
- Note that the additional opportunities for Distributions of Surplus Cash provided in this Mortgage Letter do not obviate Borrower's obligations on any Surplus Cash notes the Borrower may have outstanding.

- Unless and until Borrowers become eligible for monthly Distributions pursuant to their Regulatory Agreement and this Mortgagee Letter, such Borrowers are subject to the provisions in the revised Section 13.b. of the Regulatory Agreement shown above.

Any violation of these requirements may, at HUD's sole election and without HUD first declaring formal violations of the Regulatory Agreement, make the Borrower ineligible for monthly Distributions for a period of up to three (3) full fiscal years after the year in which the violation(s) occurred ("Exclusion Period"). During the Exclusion Period, Borrower shall be limited to annual/semi-annual Distributions based on the revised Section 13.b. above. Further, any violation of these requirements may result in a referral to HUD's Departmental Enforcement Center and/or any other remedies available to HUD.

III. POLICY ASSESSMENT

HUD will periodically conduct a review to assess whether the policy change is achieving HUD's objectives. HUD reserves the right to further modify this policy in response to the findings of such assessments.

For questions about this Mortgagee Letter, contact Thomas A. Bernaciak, Deputy Director, Office of Multifamily Production at Thomas.A.Bernaciak@hud.gov or (202) 402-3242.

IV. PAPERWORK REDUCTION ACT

The information collection requirements in this Housing Notice are already approved as OMB Approval number 2505-0029 for multifamily mortgage insurance application forms, and therefore the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) does not apply. In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

Julia R. Gordon, Assistant Secretary for Housing –
FHA Commissioner