

## **HUD-INSURED MORTGAGE MAY NOT BE THE ANSWER**

In the wake of the subprime lending meltdown, and as lending institutions tighten their access to capital, many owners of multifamily housing properties may consider securing HUD-insured loans. In either a re-finance or purchase, owners should consider the potential pitfalls.

### **Single Family v. Multifamily**

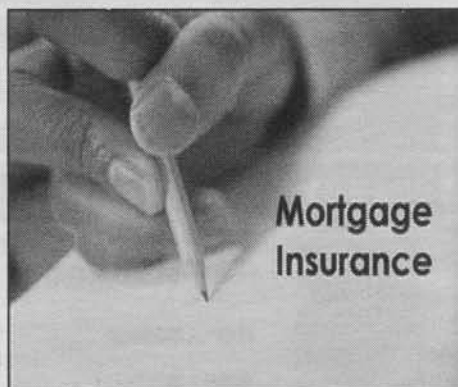
HUD, like most lenders, defines single-family housing as four units or less, and multifamily housing as five units or more. A single-family HUD-insured loan carries only a few requirements, such as owner-occupancy and mortgage insurance premiums.

Conversely, for most multifamily HUD-insured loans, the owner is required to execute and abide by a

Regulatory Agreement. At closing, most owners execute the Regulatory Agreement without realizing its full nature, the extent of its reach, and its potential financial liability.

### **Federal Statute Mirrors Regulatory Agreement Language**

In 1997, Congress amended an existing statute that essentially mirrors the language of the Regulatory Agreement, adding individuals as liable parties. It means that if the legal ownership entity, or an officer or director of the ownership entity, knowingly breaches the Regulatory Agreement, he or she has, in turn, violated the statute. Under the statute, each violation of the Regulatory Agreement exposes an owner to a potential civil money penalty of \$32,500,



per violation.

As with most administrative law proceedings, there is minimal procedural due process; the owner has no access to a jury trial; and goes before a HUD administrative law judge for adjudication regarding violations, as well as how much of a penalty

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will be imposed. Typical violations include failing to file

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(or timely file) audited financial statements with HUD, violating the provision of the Regulatory Agreement regarding tenant security deposits, or changing property management companies without prior approval from HUD.

The civil money penalty is cumulative, meaning each violation is worth \$32,500, and those violations can add up quickly. Moreover, the owner is not allowed to use project funds to pay the penalty. Most owners facing the uncertainty of going before a HUD administrative law judge either settle with HUD or try to pre-pay (or re-finance) their HUD-insured mortgages.

**Recent 9<sup>th</sup> Circuit Case: Pre-Paying HUD Loan No Cure**

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**Lesson Learned**

Even if the loan terms are enticing, think long and hard before entering into a HUD-insured multifamily housing loan.

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