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MARCH 7, 2019

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RAD for PRAC guidance published in draft for comment

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HUD published on its website, at the Multifamily Housing "Policy Drafting Table," a draft of the highly-anticipated Section IV of the RAD Notice, Rev-4, setting forth the policy and procedures for RAD for PRAC conversions. HUD has indicated it intends to alter this guidance in response to stakeholder feedback, but requests comments by March 12.

Some highlights of this draft guidance:

— **Rents.** The guidance does not provide a lot of comfort on rents, stating that initial contract rents shall be set at the lesser of (a) "approved PRAC rents" or (b) 120% of FMR for PBRA projects, 110% of FMR for PBV projects. A process for standardizing PRAC project rents, which vary greatly from project to project, was not included. Many of the existing PRAC rents are so low, conversion at those rent levels would be impossible. However, there is some hope: (i) HUD requires project owners to analyze project operating expenses, capital needs and resident services and request adjustments to the Operating Expense Amount accordingly at the current's PRAC annual renewal. This process could provide a rent increase before conversion allowing the project to leverage adequate debt upon conversion. (ii) "Rent bundling" is allowed to pool and share subsidy among several projects, presumably with some common ownership among the new project owners. (iii) Without elaborating, HUD reserves the right to modify PRAC rents if necessary to adequately fund replacement reserves, support a service coordinator or otherwise meet the needs of the residents.

— **Use Restrictions & Existing Debt: Gone!** Upon conversion, all existing obligations of the Capital Advance are terminated—both debt and existing regulatory obligations. In their place, a new Housing for the Elderly Declaration of Restrictive Covenants and Use Agreement ("Elderly Housing Use Agreement") will be in effect for the remaining term of the Capital Advance Use Agreement plus 20 years. Among its provisions, any excess proceeds from a sale or refinancing during the original term of the Capital Advance Use Agreement must go back into the project or be used for affordable housing purposes. It's unclear if this could affect valuation for LIHTC purposes. Also, the Elderly Housing Use Agreement will be in first position and survive foreclosure. This will likely necessitate lender and investor provisions in the HAP contracts in order to accommodate lender and investor concerns, as in RAD Component I ("RAD I").

- **Social Services required.** Responding to concerns from current providers and advocates, the conversion plan must account for the provision of social services. Presumably, the costs for services can be accounted for in the budget. It's unclear if they can be prospectively included in budget-based rent increases. Upon conversion, HUD is increasing allowable payment to social services coordinators from rents to $27 per unit per month, up from $15.

- **Nonprofit involvement required, but flexible.** Nonprofits must maintain ownership or control rights, but these requirements are much more flexible than the current Section 202 loan prepayment requirements. HUD explicitly allows for the possibility of LLC owner entities and for a nonprofit controlling 51% of a general partner or managing member interest when joint venturing with a for-profit entity.

- **Other requirements blend RAD I and RAD II.** The conversion process largely mirrors the RAD I process and requirements, with some helpful RAD II aspects. Interested parties must first provide some basic project information in a letter of interest and conduct resident consultations before submitting a full conversion plan. Site and neighborhood standards and therefore a potential fair housing review apply. The Uniform Relocation Act applies, but Davis-Bacon wage requirements do not apply for PBRA. The conversion plan requires a 20-year CNA and environmental review.

Stakeholders are encouraged to submit comments and comments are requested by March 12. HUD has specifically asked whether there is interest in maintaining PBV as an option or if projects will overwhelmingly choose PBRA; whether the terms of the Elderly Housing Use Agreement are reasonable and adequate; and whether there are unique features to PRAC projects or elderly housing that have not been adequately accounted for. In addition, if any provisions are unclear, or unworkable, please identify those provisions in comments.

RAD for PRAC conversions provide a valuable opportunity for existing project owners and new partners to preserve this important source of affordable housing for low-income elderly residents. Nixon Peabody's Affordable Housing team is one of the largest in the country, and we offer unparalleled knowledge in this field. Our experience, coupled with the key strategic relationships we continue to forge gives our clients a special advantage as we bring parties together.

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