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Selling or Buying an HUD Financed Nursing Home or Assisted Living: A Baker's Dozen Tips for TPA Transactions

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Interest rates are on the rise after being low for so long. Owners have taken advantage of those long-term, low fixed-rate loans insured under HUD Section 232 in record numbers. It is possible to keep those below-market loans in place through a purchase and sale transaction by obtaining HUD approval for loan assumption in a process called Transfer of Physical Assets (TPA). Of course, there are a number of requirements surrounding a TPA, and the process can take time. However, a TPA can preserve the value inherent in a 30-year term loan at below-market interest rates.

Here are a Baker's dozen tips for buyers and sellers to keep in mind as they start transactions that may involve a TPA.

1. **Application Timing:** TPAs take time, so that should be accounted for in a purchase agreement. The seller wants to wait until the buyer has satisfied its due diligence before getting its lender involved in the process. Allow at least 30 days after the end of the due diligence period to assemble the TPA application and send it to the FHA lender for submission to HUD. Be aware that the 30-day timeline is aggressive; it will likely be challenging to put the application together in this timeframe.
2. **Closing Timing:** Before closing, an HUD preliminary approval letter must be obtained. HUD review of an application may take 60 – 120 days, so the closing deadline should reflect that timeframe and allow for extensions if HUD is slower than expected in issuing its preliminary TPA approval letter.
3. **Connect FHA Lender and Buyer:** The FHA lender received the original FHA mortgage insurance, and as such, will be the party to submit the TPA application for the change in borrower. As a first step, the seller needs to direct its FHA lender to cooperate with the buyer and provide the buyer with copies of all existing loan documents so that the buyer can begin preparing the documents it needs to provide for the application.
4. **Old Forms vs. New Forms:** HUD rewrote the Section 232 loan forms in 2013. If the loan being assumed in the TPA closed under the old forms, the buyer, seller and FHA lender need to review the HUD policy to determine which forms may need to be replaced with new forms. This can be a complicated process and should be addressed as early as possible with counsel for both parties.
5. **Consider the Section 38 Parties:** Although HUD-insured loans are non-recourse to the borrower, under the new forms (post-2013), one or more "Section 38 Parties" have separately executed the owner's Regulatory Agreement to be responsible for certain "bad boy" acts of the owner. After the transaction, new Section 38 Parties will likely need to be designated and then submitted for approval to HUD and the FHA lender.
6. **DACA and DAISA:** If the operator is not changing and the bank account(s) controlled by the Deposit Account Control Agreements (DACA) and Deposit Account Instruction Service Agreements (DAISA) are not changing, they may remain in place through the transaction. However, if the accounts are changing, it will likely be necessary to get new DACA and DAISA agreements negotiated and

executed by the operator, FHA lender and the depository bank. HUD requirements have changed over time, and some depository banks may have difficulty agreeing to the HUD form of DACA, so this issue can take additional time.

7. **Existing Reserves Stay with the Project:** All existing reserves (reserve for replacement, et. al.) must remain with the project through the transaction. Sometimes a seller will assume that since it made the deposit at the initial closing, it should get the deposit back, and the new owner should make its own deposit upon its assumption of the loan. This is not the case with HUD TPAs. The purchase agreement needs to be drafted to account for the transfer of reserves.
8. **Seller's Final Report:** The seller must make the final financial report to HUD after the closing. The purchase agreement must obligate the seller to do so; otherwise, the loan could go into default, and the buyer may not have the ability to access the information needed for the final report that HUD requires.
9. **Check the Repair Escrow:** At most HUD 232 closings, a repair escrow was established for non-critical repairs. A careful buyer should ensure that all those repairs were, in fact, made and that the repair escrow has been disbursed.
10. **Seller's Secondary Finance – HUD Forms:** Perhaps the seller is giving some secondary financing of the purchase price or taking back a note for part of the purchase price. If so, note that HUD has strict requirements on the terms of any financing junior to the HUD-insured loan, and the terms are not comparable to commercial bank or mezzanine financing. If the seller is providing secondary financing as part of the deal, it is critical to specify that it will be provided on HUD-approved terms and forms.
11. **Secondary Finance – Secured by Equity:** Sometimes a buyer's affiliates or owners will obtain separate financing for the additional cash needed at closing and will pledge interests in the buyer entity as collateral. Note that foreclosure by the lender on its collateral interest in the borrower's equity is, itself, a transfer that will require HUD TPA review and approval. The lender should understand this important point.
12. **Unaffiliated Third Party Leases – Issues for Operators:** If the TPA results in a new owner which is no longer an affiliate of the operating lessee, the parties need to ensure that the operating lessee remains willing to pledge its accounts receivable to secure its unrelated landlord's mortgage and sign a Regulatory Agreement that imposes a number of specific requirements on it.
13. **Unaffiliated Third Party Leases – Issues for Owners:** Likewise, if the new owner keeps the existing operating lessee in place under a new lease, there are risks that the new owner needs to understand. For example, HUD and the FHA lender can declare an immediate loan default, without cure rights, if the lessee's operating license is at substantial and imminent risk of being terminated or suspended.

Assumption of HUD-insured loans is advantageous, but the TPA process requires careful attention to HUD requirements from initial negotiation through closing and post-closing. Parties should engage counsel familiar with the TPA process to prevent unforeseen issues arising along the way that can cause delay and frustration.

If you have questions regarding this or other HUD issues, please contact a member of our [Long Term Care Team](#).