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Section III Asset Management

Chapter 2 Controlling Documents

2.1 Introduction

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9 The Section 232 mortgage insurance closing documents are the controlling documents which
10 detail program requirements and obligations. These documents are comprised of contracts
11 (Agreements), certifications, forms, and regulations. ~~The documents~~ Documents discussed in this
12 Chapter were ~~published pursuant to approved by OMB, comply with~~ the Paperwork Reduction
13 Act (PRA) and are available on the Section 232 Program website.
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2.2 Regulatory Agreements and Other Controlling Documents

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17 **A. Regulatory Agreement.** The regulatory agreement is the contractual document under which
18 the Borrower, Operator and, if applicable, the Master Tenant are regulated by HUD, ~~as long~~
19 ~~as while~~ HUD is the insurer or holder of the mortgage. Therefore, depending on the
20 Borrower and Operator structure, the project may have one or more of the following
21 regulatory agreements:
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- 23 1. Healthcare Regulatory Agreement – Borrower, or Borrower Regulatory Agreement
24 (Form HUD-92466-ORCF),
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- 26 2. Healthcare Regulatory Agreement – Operator, or Operator Regulatory Agreement
27 (Form HUD-92466A-ORCF), or
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- 29 3. Healthcare Regulatory Agreement – Master Tenant, or Master Tenant Regulatory
30 Agreement (Form HUD-92337-ORCF).
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- 32 4. Supplemental Health Care Regulatory Agreement – Borrower , Form HUD-92467-
33 ORCF
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- 35 5. Supplemental Health Care Regulatory Agreement – Operator , Form HUD-92467A-
36 ORCF
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39 Depending on the date an FHA-mortgage was insured, the insured mortgage may have earlier
40 versions of these documents, which do still apply in full force and effect, and this Section III of
41 this Handbook does apply to those insured mortgages.

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43 If the Borrower and Operator are the identical legal entity, then that entity shall sign both the
44 Borrower Regulatory Agreement and the Operator Regulatory Agreement. The regulatory
45 agreement is recorded in the land records and thus is an encumbrance on the property. HUD will
46 agree to release the regulatory agreement when the FHA-insured loan is paid in full, either at
47 maturity or upon prepayment. (The prepayment approval process is in Asset Management,
48 Chapter 3.3.2.) ~~The For an FHA-Insured loan paid in full at maturity, the Borrower or Operator~~
49 ~~shall provide contact its Account Executive (AE) with a written request with a legible copy of the~~
50 ~~recorded regulatory agreement attached. The AE will forward both documents to Headquarters,~~
51 ~~Office of General Counsel, Insured Housing Multifamily Mortgage Division for~~
52 ~~processing further instructions.~~

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55 **B. Other Controlling Documents. Other Controlling Documents used in the Section 232**
56 **program include:**

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1. Limited Guarantee and Security Agreements – and other cross collateralization, if applicable

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2. Subordination Non-Disturbance and Atonement Agreement of Operator Lease – Form HUD-91110-ORCF

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Depending on the date an FHA-mortgage was insured, the insured mortgage may have earlier versions of these documents, which do still apply in full force and effect, and this Section III of this Handbook does apply to those insured mortgages.

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2.3

Mortgage and Mortgage Note

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70 A. **Mortgage:** A mortgage is a written instrument which evidences an interest in land or real
71 property and provides security for the performance of a duty or the payment of a debt. The
72 FHA mortgage is one in which the loan has been insured by the Federal Housing
73 Administration (FHA).

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75 B. **Mortgage Note:** A mortgage note is executed for all insured mortgages. It is the written
76 document that evidences a loan for which real estate has been offered as security and
77 includes an unconditional promise by the Borrower to repay the debt on a specified date. It is
78 also the document that FHA endorses as evidence of its insurance commitment. It sets forth
79 the original amount of indebtedness to the Lender, the interest rate, and the manner in which
80 the debt will be repaid. The following HUD forms are used;

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• Healthcare Facility Note Section 232 – Form HUD-94001-ORCF

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• Supplemental Healthcare Facility Note , Form HUD-94001A-ORCF

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2.4

Uniform Commercial Code (UCC) Filing

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Uniform Commercial Code. The Uniform Commercial Code (“UCC,” or “the Code”), deals primarily with transactions involving personal property (movable property), but not real property (immovable property). Article 9 governs how security interests may be obtained in personal property that a Borrower and a Lender agree will serve as security for payment of specified debts. Fundamental concepts under Article 9 include: how a security interest is imposed on property (“attachment”); how security interests are made complete (“perfected”); and what remedies are available to the secured party if the debtor defaults in payment or performance of the secured debt or obligation.

2.5

Operating Lease

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Operating Lease. The Operating Lease (or Agreement) provides the Operator with the use of the property for a particular period of time and sets forth the Borrower’s and Operator’s responsibilities and obligations. The terms of the Operating Lease must be consistent with Section 232 of the National Housing Act, Section 232 Regulations and Program Obligations (see Production, Chapter 8).

2.6

Master Leases

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Master Lease. Master Leases, also known as Sandwich Leases or Credit Pass Throughs, are used by national and regional healthcare Borrowers. These transactions create a tiered structure with a Master Tenant leasing multiple projects from the Borrowers, and then entering into sub-leases, which are sometimes referred to as master subleases, with the entities that will operate the healthcare facilities. Through the master lease agreement, the Master Tenant agrees, among other things, to pay the Borrowers’ rent necessary make a lease payment to the Borrower in an amount that is, at a minimum, sufficient to satisfy the Borrower’s financial obligations under the FHA-insured mortgage. Also, the sublessees (or subtenants) are required, among other things, to agree to contribute additional amounts when needed and as available to cover any shortfall in the rent that the Master Tenant owes to the Borrower (see Production, Chapter 13).

Some states do not allow Master Leases. In this situation, Limited Guarantee and Security Agreements – and other cross collateralization will be utilized as an alternative risk mitigant (See Production, Chapter 13).

2.7

Accounts Receivable Financing, Deposit Account Control Agreements (DACAs), Operator Bank Accounts and Deposit Account Instruction Service Agreements (DAISAs)

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- 123 A. **Accounts Receivable (ARA/R) Financing.** A majority of skilled nursing facility operators
- 124 now use accounts receivable (ARA/R) loan financing mechanisms to ensure that adequate
- 125 cash flow is available to meet ongoing operating expense needs. Typically, the Operator
- 126 provides patient services which are reimbursed by Medicaid and Medicare 30 to 90 days after
- 127 the services are provided. The timing of these reimbursements varies from state to state and
- 128 can be subject to significant delays. The remaining patients either pay for their services from
- 129 their own private resources (private-pay) or have private insurance coverage. Absent ARA/R
- 130 lines of credit, Operators may be at risk of experiencing short-term cash liquidity shortfalls.
- 131 The ARA/R line of credit provides a source of funds to sustain ongoing operations until
- 132 Medicaid and/or Medicare reimbursement funds are received. In addition, the ARA/R
- 133 Lender supplements ORCF's oversight as a third party monitoring the financial operations of
- 134 the Operator. This results in additional oversight and proactive intervention with the
- 135 Operator if unusual or troubling financial trends appear (see Production, Chapter 15, and
- 136 Asset Management, Chapter 10).
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- 138 B. **Deposit Account Control Agreement (DACA).** The accounts receivables ("ARA/R") of
- 139 the Operator of a project subject to a FHA-insured loan, constitutes "project income." There
- 140 are two types of project income: non-governmental and governmental receivables. The
- 141 Deposit Account Control Agreement ("DACA") addresses the non-governmental
- 142 receivables. A security interest in those ARA/R must be executed by the Operator, via a
- 143 security agreement. Pursuant to UCC §9-104, a DACA is used to perfect ORCF's and the
- 144 Lender's security interest in the Operator's deposit accounts. A DACA is an agreement
- 145 made among a secured party (generally, the FHA Lender), a debtor (generally, the Operator,
- 146 whether the Borrower or lessee), and depository bank (the bank at which the Operator
- 147 maintains its deposit accounts) in which the debtor has agreed that the bank will comply with
- 148 the secured party's instructions regarding disposition of the funds in the debtor's deposit
- 149 account without further consent by the debtor. DACAs are referred to by various names,
- 150 including Blocked Account Agreements, Lockbox Agreements and Springing Lockbox
- 151 Agreements (see Production, Chapter 15 and Chapter 16, and Asset Management, Chapter
- 152 10).
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- 154 C. **Operator Bank Accounts:** It is understood that the Operator will typically maintain at least
- 155 two separate bank accounts. The first account, the Governmental Healthcare Receivables
- 156 Account (GHR Account), is an account into which all Medicare/Medicaid receivables are
- 157 deposited. It is expected that the FHA Lender, depository bank and, where applicable, the
- 158 ARA/R Lender will enter into a Deposit Account Instructions Service Agreement ("DAISA")
- 159 that requires the depository bank to "sweep" the GHR Account daily (or less frequently with

160 HUD approval) such that all funds deposited in the GHR Account are transferred to a second
161 account of the Operator, known as the "Operating Account" (see Production, Chapter 16).

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163 **D. Deposit Account Instructions Service Agreement (DAISA) guidelines:** A DAISA refers
164 to the instructions provided to the bank by the debtor that details how the bank is to dispose
165 of governmental healthcare funds in the GHR Account. The DAISA must not grant the FHA
166 Lender the right to direct disbursements from the GHR Account as in a DACA in order to
167 avoid a conflict with applicable healthcare program restrictions (e. g. the Medicare/Medicaid
168 anti-assignment provisions). Unlike a DACA, a DAISA should be terminable by the
169 Operator in order to comply with all applicable healthcare program restrictions (e. g.
170 Medicare/Medicaid anti-assignment provisions). The Security Agreements shall also provide
171 that the Operator must procure the FHA Lender's written consent prior to closing a deposit
172 account subject to a DAISA or terminating the DAISA ~~FHA Lender~~ (see Production, Chapter
173 15 and Chapter 16, and Asset Management, Chapter 10).

2.8

Management Certification

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177 The definition of a Management Agent, including the distinction between a Management Agent
178 and an Operator, is discussed in Production, Chapter 8 and Asset Management, Chapter 8. A
179 party who is deemed a Management Agent by HUD, rather than an Operator, must execute a
180 Consolidated Certification – Management Agent (Form HUD-90017-ORCF). In addition, the
181 Management Agent must execute a Management Agreement Addendum (Form HUD-92071-
182 ORCF).