

Section III Asset Management

Chapter 4 Financial Operations

4.1

Introduction

This chapter addresses loan servicing related to the financial operations of projects insured under Section 232. For the purposes of this chapter, the term “Mortgagee/Servicer” means the primary Servicer responsible for servicing the mortgage loan, whether such party is the originating Lender or third party Servicer for the originating Lender.

4.2

Financial Submission Requirements

The *Healthcare Regulatory Agreement - Borrower* (Forms HUD 92466, HUD 92466-EH and HUD 92466-ORCF) requires the submission of audited annual financial information for the Borrower. Additionally, amendments in 2012 to the Uniform Financial Reporting Requirements rule (24 CFR 5.801 et seq.), applicable to all Section 232 Operators (amendments addressed in this chapter and also delineated in the *Healthcare Regulatory Agreement – Operator*, Form HUD 92466A-ORCF) require submission of quarterly/year-to-date and annual financial statements from the Operator. This same 24 CFR 5.801 requires that financial submissions for all Section 232 related projects (both Borrower and Operator) be submitted concurrently to HUD and the Mortgagee/Servicer.

Borrowers are required to submit their annual financial statements within ninety days of their fiscal year end into the Financial Assessment Subsystem (FASS) which uploads the financial statements into the Integrated Real Estate Management System (iREMS), which ORCF uses in its routine asset management of projects. Guidelines for accounting from HUD’s Real Estate Assessment Center (REAC), revised submission procedures formulated in 2004, and the guidelines for REAC submissions, can be found on the REAC website.

HUD systems perform an analysis of the financial submission of the Borrower to measure the financial condition of the project and to assess compliance with applicable laws, regulations and business documents. HUD requires Borrowers to submit audited financial statements each year to the Mortgagee/Servicer and to HUD. HUD analyzes these financial statements to assess compliance with program requirements, to evaluate the financial strength of the Borrower, and for many other purposes. Mortgagee/Servicers should conduct their examination to the extent necessary to classify asset values and make risk assessments.

A. FASS performs an initial assessment of the financial condition of the Borrower's statement, as well as a review of the project's compliance with applicable laws, regulations and business documents. Compliance deficiencies identified either by this assessment or the project's auditor may be referred to ORCF or the Departmental Enforcement Center (DEC).

B. Borrower Submission Requirements:

In addition to Regulatory Agreement financial submission requirements, the Uniform Financial Reporting Requirements rule (24 CFR 5.801 et seq.) requires the electronic submission to HUD and the Mortgagee/Servicer of Borrower financial information prepared in accordance with Generally Accepted Accounting Principles (GAAP).

1. For Profit Borrowers are required to electronically submit an audited Annual Financial Statement (AFS) within 90 days after the end of each fiscal year,
2. Non-profit Borrowers are required to electronically submit a Borrower-certified (unaudited) AFS within 90 days after the end of the fiscal year. An electronically submitted, audited AFS is due no later than nine months after the end of the fiscal year pursuant to 2 CFR 200. The Borrower may opt to submit the audited AFS within 90 days after the end of the fiscal year. By submitting the audited AFS within 90 days the Borrower may eliminate the additional step of submitting a Borrower-certified AFS. ORCF recommends Borrowers refer to 2 CFR 200 Subpart F for current exemption thresholds as well as how to calculate the amount of federal financial assistance received.
3. Non-profit Borrowers (receiving less than \$500,000 annually in combined federal assistance) are required to electronically submit a Borrower-certified AFS within 90 days after the end of the fiscal year.

C. The HUD systems review of the Borrower's financial statement in FASS may generate an "AFS Evaluation Financial Risk" action in the HUD system. The AE will review the action and contact the project or Mortgagee/Servicer for additional details or actions necessary to comply with the FASS deficiency.

D. Operator Submission Requirements:

1. As set forth in 24 CFR Part 5.801, unless otherwise specified by HUD, Operator shall submit, on a quarterly and year-to-date basis (or more frequently if specified by HUD), prepared and certified by an authorized representative or agent of Operator, such financial reports relating to the operation of the Healthcare Facility in the formats and at such times as may be approved by HUD in accordance with Program Obligations.
2. Detailed requirements for Operator quarterly and year-to-date submissions will be conveyed via the Section 232 Program website.

3. Such reports must be submitted no later than sixty (60) days after the period covered by the reports, except for reports relating to the final quarter of each year, which shall be submitted no later than ninety (90) days after end of the fiscal year. Such reports are subject to the sanctions contained in 18 U.S.C. Sections 1001, 1010, and 1012.

E. Ongoing Master Tenant Financial Requirements:

Master Tenant shall submit, or cause to be submitted, to HUD and Mortgagee/Servicer, on a quarterly and year-to-date basis (or more frequently if specified by HUD), prepared and certified by an authorized representative or agent of Master Tenant, such financial reports relating to the Master Tenant. Such reports must be submitted no later than sixty (60) days after the period covered by the reports, except for reports relating to the final quarter of each year, which shall be submitted no later than ninety (90) days after end of the fiscal year. Such reports are subject to the sanctions contained in 18 U.S.C. Sections 1001, 1010, and 1012. Additional information regarding the Master Tenant financial submission will be provided for on the Section 232 Program website.

F. Midsize and Large Portfolio Post Closing Quarterly Financial and Operational Review and Analysis:

For the entity that was the subject of a corporate credit review, HUD will require ongoing submission of the same financial and operational information. The data to be collected will be similar to the initial review material, and made available on the Section 232 Program website.

4.3

**Financial Assessment System (FASS)
Submissions**

- A. The Borrower must notify their Mortgagee/Servicer within two business days of receiving a Notification of Failure to File Financials by the required deadline in Financial Assessment System (FASS).

This notification is sent automatically to the email the project registered in the system when a deadline for submission of annual financial information is missed.

- B. Once notified, the Mortgagee/Servicer must work with the Borrower to ensure submission is forthcoming, and address any delays.

The Mortgagee/Servicer must notify the AE if there are extenuating circumstances that are preventing the immediate submission, and provide the AE with the action plan to submit the required information expeditiously.

- C. Extended periods without filing FASS requirements by the deadline will warrant referral to the DEC, and additional actions may be taken by HUD to ensure compliance.

A. Key Indicators

The annual and quarterly review of the project operations by the Operator, coupled with the annual Borrower financial submissions, will allow both HUD and the Mortgagee/Servicer to maintain an ongoing understanding of performance. Key indicators of the Operator financial statements will be used to monitor performance and to measure against future routine reviews. Typically, the annual and quarterly reviews are all that are necessary for monitoring the financial operations of a project; however, HUD does reserve the right to require monthly financial reports (of the Operator, the Borrower, or both) to be submitted (to HUD, the Mortgagee/Servicer or both) if financial indicators suggest this level of monitoring is needed or if noncompliance with HUD business agreements (by the Borrower, Operator or Management Agent) is suspected.

If the Borrower is the same legal entity as the Operator, then the Borrower itself will submit the Operator financial data. Detailed instructions for the submission of quarterly and annual Operator financials, using the Section 232 Healthcare Portal, may be found on the Section 232 Program website.

B. Withdrawal of Project Funds (Distributions)

As set forth in federal regulation 24 CFR 232.254, and applicable only to transactions for which a firm commitment has been issued on or after July 12, 2013, with mortgage insurance transactional documents consistent with the regulation (see in particular the ORCF *Healthcare Regulatory Agreement – Operator*, and specifically Sections 15 and 16 thereof), a Borrower may make and take distributions of mortgaged property, to the extent and as permitted by the law of the applicable jurisdiction, provided that:

1. The calculation shall be made no less frequently than semi-annually.
2. The Borrower must demonstrate positive surplus cash. To the extent surplus cash is negative, the Borrower must repay any distributions taken during such calculation period within 30 calendar days, unless a longer time period is approved by HUD.
3. The Borrower shall be deemed to have taken distributions to the extent that surplus cash is negative, unless in conjunction with the calculations of surplus cash, the Borrower provides to HUD documentation evidencing, to HUD's reasonable satisfaction, a lesser amount of total distributions.

Note, however, that the distributions of an Operator in transactions for which a firm commitment was issued on or after July 12, 2013, are governed separately by 24 CFR 232.1013, and if a Borrower and Operator are the same legal entity then that entity's distributions are constrained by both the Borrower restrictions and the Operator restrictions.

C. Mortgagee/Servicer's Analysis of Its Overall Portfolio

To have a full and accurate picture of the financial condition of its portfolio, Mortgagee/Servicers must assess the probability that existing loans might not be repaid. Mortgagee/Servicers will need to estimate the losses that could be incurred and to establish procedures for assessing the risk inherent in each loan in their portfolios. An annual meeting between a Mortgagee/Servicer and their assigned AE(s) should be conducted to align risk mitigation efforts. The Mortgagee/Servicer shall contact the AE when the project is experiencing operational challenges which may warrant discussions amongst the parties.