FHA SECTION 242

LEAN | Healthcare

Critical Access Hospitals New Construction or Substantial Rehab

ELIGIBILITY	To qualify for the Sec. 242 program, a facility must have a positive average operating margin for the last three full fiscal years, and the average debt-service coverage ratio must be equal to or greater than 1.25. If a hospital recently obtained CAH status, it may recast the last three years' historical financial statements in order to illustrate what its operating margins and debt service coverage would have been if it had been receiving CAH reimbursement. HUD will accept applications of CAH facilities that meet the operating margin and debt-service coverage tests based on the recast financial statements.
MAXIMUM LOAN AMOUNT	There is no limit on the amount that can be financed. However, the loan-to-value ratio may not exceed 90%. In meeting the 90% loan-to-value test, a hospital may include as equity the net remaining value of its existing property, plant and equipment.
MAXIMUM TERM	The maximum term is 25 years from initial principal payment after completion of construction. Principal amortization is calculated to produce level principal and interest payments. The construction period is interest only.
INTEREST RATE	The interest rate is fixed, subject to market conditions at rate lock for taxable debt or at closing for tax-exempt bonds.
LIABILITY	Loans insured by the 242 program are secured by a mortgage and pledge of revenues related directly to the project. Collateral pledged for 242 program loans may not be part of an obligated group or be used as collateral for other debt. Subject to attainment of certain debt service coverage and liquidity levels, hospitals utilizing the 242 program may transfer excess cash flow to parent health systems or hospitals.
FUNDING OPTIONS	Nonprofit hospitals can utilize mortgage insurance as credit enhancement to issue tax-exempt bonds. Depending on market conditions, a commercial bond insurer may be utilized to achieve an "AAA" bond rating. Of note, nonprofit organizations may elect to issue taxable notes in conjunction with GNMA mortgage insurance without tax-exempt bonds. For-profit hospitals can utilize mortgage insurance in conjunction with GNMA mortgage insurance to issue taxable loans for expansion, renovation or replacement projects.
SECURITY	The hospital must grant the 242 program lender a first mortgage on the entire hospital, including all real estate and improvements being financed. (Note: Exceptions may include leased equipment, off-site property, capital associated with affiliations, city and/or county owned facilities, etc.)
ESCROWS	Standard monthly escrow deposits are required for all insurance, real estate taxes and mortgage insurance premiums. Over the initial five years of principal amortization, the 242 program requires that participants accumulate a mortgage-reserve fund balance equal to one year's annual net debt service. From year six to year 10, the hospital must build the mortgage reserve fund balance to two years' annual debt service. If tax-exempt bonds are issued, rating agencies and investors will require an additional debt service reserve fund equal to one year's annual debt-service, as well as sufficient cash escrows and/or letters of credit to cover negative arbitrage during the construction period.

COSTS & EXPENSES

Fixed closing costs include:

- 0.30% FHA application fee; one half paid with application, one half at closing.
- 0.50% FHA inspection fee.

Variable closing costs include:

- 2.00% to 5.50% for financing expenses (including mortgage bankers, investment bankers, attorneys and rating agencies).
- $25,000 to $100,000 for an examined financial forecast.

Annual expenses (based on outstanding principal amount):

- 0.50% annual FHA mortgage insurance premium; first year paid at closing.

CONSTRUCTION GUIDELINES

Davis-Bacon prevailing wage rates apply to new construction, additions and substantial rehabilitation projects.

TIMING

The entire process can be completed in as little as six to nine months and is divided into four phases outlined in the table below. Actual processing times vary depending on the project.

STAGE	PURPOSE	ESTIMATED TIME
PRE-ASSESSMENT PHASE	Provide HUD with basic information on project.	Third month.
PRE-APPLICATION PHASE	Arrange visit to HUD's headquarters for half-day meeting to present and discuss further detail about the project.	Fourth month.
APPLICATION PHASE	Complete full application for HUD's review, including a financial examination. After submission, HUD's goal is a 60-day application processing period.	Fifth and sixth months.
CLOSING PHASE	Complete funding documentation and issue debt.	Seventh and eighth months.

Lument is a leading FHA-approved Mortgagee and MAP/LEAN lender and actively provides financing utilizing FHA insurance programs nationwide pursuant to Multifamily Accelerated Processing (MAP) and LEAN underwriting methods.

In its prequalifying review, Lument will attempt to estimate both the loan amount and the fees and costs associated with the transaction. Actual loan amounts and actual fees and expenses may vary from the prequalifying estimates. A prequalifying estimate is not a commitment to make a loan.