

TABLE 1—INITIAL INSPECTION THRESHOLDS—Continued

Appendix number of RR ASB No. RB.211–72–AG244, revision 4, that identifies affected LP compressor blades by S/N	Initial inspection threshold
3F .....	Within 46 months after the effective date of this AD.
3G .....	Within 58 months after the effective date of this AD.
3H .....	Within 70 months after the effective date of this AD.
3I .....	Within 82 months after the effective date of this AD.
3J .....	Within 94 months after the effective date of this AD.
3K .....	Within 106 months after the effective date of this AD.
3L .....	Within 118 months after the effective date of this AD.

(2) Thereafter, perform repetitive UIs of the affected LP compressor blades within every 100 flight cycles.

(3) Use paragraph 3.A.(2) of Accomplishment Instructions of RR ASB No. RB.211–72–AG244, Revision 4, dated December 22, 2011, and paragraphs 1. through 3.B. of Appendix 1 of that ASB, or paragraphs 3.B.(1) through 3.B.(3) of Accomplishment Instructions of RR ASB No. RB.211–72–AG244, Revision 4, dated December 22, 2011, and paragraphs 1. through 3.C. of Appendix 2 of that ASB, to perform the UIs.

(4) Do not return to service any engine with blades that failed the inspection required by this AD.

(5) For blades that are removed from the engine and pass inspection, re-apply dry film lubricant before re-installing the blades.

(6) After the effective date of this AD, do not install any affected LP compressor blade that has reached the initial inspection threshold in Table 1, unless it has passed the initial and repetitive UIs required by this AD.

**(f) Credit for Actions Accomplished in Accordance With Previous Service Information**

You may take credit for the initial inspection that is required by paragraph (e)(1) of this AD if you performed the initial inspection before the effective date of this AD using RR ASB No. RB.211–72–AG244, dated August 7, 2009; ASB No. RB.211–72–AG244, Revision 1, dated January 26, 2010; ASB No. RB.211–72–AG244, Revision 2, dated August 18, 2011; or ASB No. RB.211–72–AG244, Revision 3, dated December 13, 2011.

**(g) Alternative Methods of Compliance**

The Manager, Engine Certification Office, FAA, may approve AMOCs for this AD. Use the procedures found in 14 CFR 39.19 to make your request.

**(h) Related Information**

(1) For more information about this AD, contact Alan Strom, Aerospace Engineer, Engine Certification Office, FAA, Engine & Propeller Directorate, 12 New England Executive Park, Burlington, MA 01803; phone: 781–238–7143; fax: 781–238–7199; email: alan.strom@faa.gov.

(2) Refer to European Aviation Safety Agency AD 2012–0025, dated February 8, 2012, for related information.

(3) For service information identified in this AD, contact Rolls-Royce plc, Corporate Communications, P.O. Box 31, Derby, England, DE248BJ, telephone: 011–44–1332–242424; fax: 011–44–1332–245418, or email:

[http://www.rolls-royce.com/contact/civil\\_team.jsp](http://www.rolls-royce.com/contact/civil_team.jsp). You may review copies of the referenced service information at the FAA, Engine & Propeller Directorate, 12 New England Executive Park, Burlington, MA. For information on the availability of this material at the FAA, call 781–238–7125.

Issued in Burlington, Massachusetts, on April 27, 2012.

**Colleen M. D'Alessandro**,  
Assistant Manager, Engine & Propeller Directorate, Aircraft Certification Service.

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**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**

**24 CFR Parts 5, 200, 207, and 232**

**[Docket No. FR–5465 P–01]**

**RIN–2502–AJ05**

**Federal Housing Administration (FHA): Section 232 Healthcare Facility Insurance Program-Strengthening Accountability and Regulatory Revisions Update**

**AGENCY:** Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

**ACTION:** Proposed rule.

**SUMMARY:** In 2010 through 2011, HUD commenced and completed the process of revising regulations applicable to, and closing documents used in, FHA insurance of multifamily rental projects, to reflect current policy and practices in the multifamily mortgage market. The multifamily rental project regulations and closing documents had not been updated in more than 20 years. Through this proposed rule, HUD commences a similar process for its regulations governing insurance of healthcare facilities under section 232 of the National Housing Act, and the closing documents used in such transactions. HUD's Section 232 program insures mortgage loans to facilitate the construction, substantial rehabilitation, purchase, and refinancing of nursing homes, intermediate care facilities,

board and care homes, and assisted-living facilities. This rule proposes amendments to update HUD's Section 232 regulations, to reflect current policy and practices, and to improve accountability and strengthen risk management.

**DATES:** Comment Due Date: July 2, 2012.

**ADDRESSES:** Interested persons are invited to submit comments regarding this proposed rule to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street SW., Room 10276, Washington, DC 20410–0500. Communications must refer to the above docket number and title. There are two methods for submitting public comments. All submissions must refer to the above docket number and title.

1. *Submission of Comments by Mail.* Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street SW., Room 10276, Washington, DC 20410–0500.

2. *Electronic Submission of Comments.* Interested persons may submit comments electronically through the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov). HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the [www.regulations.gov](http://www.regulations.gov) Web site can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

**Note:** To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the rule. *No Facsimile Comments.* Facsimile (FAX) comments are not acceptable.

*Public Inspection of Public Comments.* All properly submitted comments and communications submitted to HUD will be available for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 708-3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number via TTY by calling the Federal Relay Service at 1-800-877-8339. Copies of all comments submitted are available for inspection and downloading at [www.regulations.gov](http://www.regulations.gov).

**FOR FURTHER INFORMATION CONTACT:** Michael B. Vaughn, Director, Office of Residential Care Facilities, Office of Healthcare Programs, Office of Housing, Department of Housing and Urban Development, 451 7th Street SW., Room 6264, Washington, DC 20410-8000; telephone number 202-708-0599 (this is not a toll-free number). Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Relay Service at 1-800-877-8339.

**SUPPLEMENTARY INFORMATION:**

**I. Background**

The American population is undergoing a significant demographic change as an increasing portion is age 65 or older or approaching 65.<sup>1</sup> As several governmental and private organizations have reported, the growing number of older adults is placing increased demands on the public health system and on medical and social services.<sup>2</sup> These demands include greater need for nursing homes, long-term care facilities, and assisted living arrangements. Further, although options for long-term care and assisted living have expanded, nursing homes will likely retain a major role in caring for the most severely impaired and vulnerable populations.<sup>3</sup> Moreover, nursing homes are increasingly offering medical services similar to those offered in hospitals after surgery, illness, or other sudden medical problems. In those situations, older adults in particular need a higher level of care

because hospital stays are shorter than previously.<sup>4</sup>

*The Section 232 Program*

Section 232 of the National Housing Act (12 U.S.C. 1715w) (Section 232) authorizes FHA to insure mortgages made by private lenders to finance the development of nursing homes, intermediate care facilities, board and care homes, and assisted living facilities (collectively, residential healthcare facilities). The Section 232 program allows for long-term, fixed-rate financing for new and rehabilitated properties for up to 40 years. Existing properties without rehabilitation can be financed with or without Ginnie Mae<sup>5</sup> Mortgage Backed Securities for up to 35 years.

Eligible borrowers under the Section 232 program include investors, builders, developers, public entities (nursing homes), and private nonprofit corporations and associations. For nursing homes only, applicants may be public agencies that are licensed or regulated by a state to care for convalescents and people who need nursing or intermediate care. The documents executed at loan closing provide that the borrower entity may not engage in any other business or activity.

Facilities covered by an FHA-insured mortgage under the Section 232 program must accommodate 20 or more residents who require skilled nursing care and related medical services, or those who, while not in need of nursing home care, are in need of minimum but continuous care provided by licensed or trained personnel. Assisted living facilities, nursing homes, intermediate care facilities, and board and care homes may be combined in the same facility covered by an insured mortgage or may be in separate facilities. Insured mortgages may include the cost of major movable equipment, daycare facilities, and the installation of fire safety equipment. Assisted living facilities, nursing homes, intermediate care homes, and board and care homes must be licensed or regulated by the appropriate state agency, municipality, or other political subdivision where the facility is located.

The maximum amount of the loan for new construction and substantial rehabilitation is equal to 90 percent (95 percent for nonprofit organization sponsors) of the estimated value of physical improvements and major

movable equipment. For existing projects, the maximum is 85 percent (90 percent for nonprofit organization sponsors) of the estimated value of the physical improvements and major movable equipment.

As the need for residential care facilities has expanded, requests to FHA to make mortgage insurance available for such facilities has also expanded. As with any program expansion, FHA seeks to ensure that program requirements currently in place are sufficient to meet increased demand, and prevent mortgage defaults that not only impose a risk to the FHA insurance fund but also jeopardize residents of Section 232 facilities.

*The Need for Regulatory Update*

HUD's regulations governing the Section 232 program are codified in 24 CFR part 232. These regulations were promulgated in 1971, with some revisions made in the 1970s and the 1980s. Two regulatory updates were issued in the 1990s. On November 29, 1994, HUD issued a final rule that amended the Section 232 regulations to implement statutory authority to insure assisted living facilities for the care of frail elderly persons, as authorized by section 511 of the Housing and Community Development Act of 1992 (Pub. L. 102-550, approved October 28, 1992). (See 59 FR 61228.) On April 1, 1996, HUD issued a final rule to comply with the then-Administration's regulatory review initiative to streamline regulations, including by removing obsolete ones. (See 63 FR 14396.) The preamble to that final rule stated that the only changes being made to the Section 232 regulations were to remove the regulatory provisions concerning lender eligibility and to provide a cross-reference to 24 CFR part 200, subpart A, which addressed the general eligibility requirements to be approved as an FHA-approved lender. (See 63 FR 14397.) The 1996 rule was the last time that HUD amended the Section 232 regulations. Given the far greater demand today for nursing homes, and long-term care and assisted living facilities, and the changes, over the years, in how these facilities offer services to an aging population, as discussed above, HUD's Section 232 regulations need to be revised and updated.

In the 1970s, regulations governing FHA-insured transactions were generally structured so that details pertaining to the duties and obligations of parties involved in the transaction were primarily addressed in contractual documents, and that has been the case as well for the Section 232 regulations.

<sup>1</sup> See [http://www.aoa.gov/aoaroot/aging\\_statistics/index.aspx](http://www.aoa.gov/aoaroot/aging_statistics/index.aspx).

<sup>2</sup> See <http://www.cdc.gov/mmwr/preview/mmwrhtml/mm5206a2.htm>.

<sup>3</sup> Bercovitz, Anita, Decker, Frederic H., Jones, Adrienne, Remsburg, Robin, *End of Life Care in Nursing Homes: 2004 National Nursing Home Survey*, National Health Statistics Reports, No. 9, October 8, 2008, pages 1 and 2.

<sup>4</sup> See [http://www.healthinaging.org/agingintheknow/chapters\\_print\\_ch\\_trial.asp?ch=15](http://www.healthinaging.org/agingintheknow/chapters_print_ch_trial.asp?ch=15).

<sup>5</sup> Ginnie Mae is a registered service mark of the Government National Mortgage Association; See <http://www.ginniemae.gov/>.

This approach has offered FHA and the parties to a transaction the necessary flexibility to adjust requirements as may be appropriate given the specifics of a given transaction, and HUD believes they should be retained for certain transaction aspects. After 16 years, however, certain policy and practices have developed that are not unique to certain parties and transactions and should be reflected in regulation. For example, since the operating revenues of the healthcare facility determine the financial health of the project and the FHA insurance fund, it has become clear that oversight by FHA of such revenues is vital.

## II. This Proposed Rule

Through this rule, and similar to HUD's recent update of multifamily rental project regulations and closing documents, HUD proposes to update its Section 232 regulations and related closing documents. Notice of the publication of the documents is provided separately in the **Federal Register** through Notice FR-5623-N-01, Federal Housing Administration (FHA) Healthcare Facility Documents: Proposed Revisions and Updates and Notice of Information Collection. Through this proposed rule, HUD updates terminology and makes amendments to reflect current policy and practices. The specific amendments proposed to update HUD's Section 232 regulations by this rule follow. The update includes amendments to 24 CFR parts 5, 200, 207, and 232 dealing with, respectively, Uniform Reporting Standards, Real Estate Assessment Center (REAC) inspections, Multifamily Mortgage Insurance contract requirements, and strengthening of the eligibility and oversight provisions of the healthcare programs. As the most significant proposals are in 24 CFR part 232, these are addressed first in this part of the preamble.

### *A. Mortgage Insurance for Nursing Homes, Intermediate Care Facilities, Board and Care Homes, and Assisted Living Facilities (Part 232)*

#### Nomenclature Change

In its review of the regulations in 24 CFR part 232, HUD noted that the regulations use both the term "borrower" and "mortgagor." These terms have the same meaning, and to avoid any misunderstanding that they have different meanings, this proposed rule would substitute the term "borrower" for "mortgagor" throughout the part 232 regulations. Closing documents for the Section 232 program may sometimes refer to the borrower as

the "mortgagor," "lessor," and/or the "owner."

#### Eligibility Requirements (Subpart A)

Subpart A of the part 232 regulations, entitled "Eligibility Requirements," would be revised as follows:

The rule would revise eligibility requirements under § 232.1 to establish an exception from the multifamily program requirements for eligible borrowers. Eligible borrowers for multifamily projects are addressed in 24 CFR 200.5.

A new § 232.3 is added to part 232 to provide an appropriate definition of an eligible borrower for healthcare facilities. In a Section 232 transaction, HUD maintains a relationship with the borrower, and the borrower assumes a responsibility to ensure the appropriate maintenance and use of project assets. Given the importance of this relationship, the proposed rule would include a new definition of eligible borrower in § 232.3. This revised definition would conform to current legal changes in the forms of commercial property ownership. HUD notes that the single asset entity form of ownership has become the standard form of ownership for commercial real estate transactions. The revised definition, therefore, provides that the borrower shall be a single asset borrower entity acceptable to the Federal Housing Commissioner (Commissioner) and shall possess the power necessary and incidental to operating the project. The regulation provides that the Commissioner may approve an exception to this single asset requirement in limited circumstances based upon such criteria as may be specified by the Commissioner.

The rule would redesignate existing eligibility requirements presently contained in current § 232.3. That section presently establishes the standards for healthcare facility bathroom and resident ratios and access. Moving this section to § 232.7 would merely restructure the sequence of the eligibility requirements in the regulations.

The rule would add a new § 232.9 to define mortgaged property. Mortgaged property would be defined to include all of the borrower's interest in any property, real, personal, or mixed, covered by the mortgage or mortgages securing the note endorsed for insurance or held by the Secretary. This definition is consistent with the definition of mortgaged property currently in the Security Agreement, used in Section 232 transactions, and as used in the revised Borrower's Security Instrument.

The rule would add § 232.11 to require borrowers to establish at final closing and maintain throughout the term of the mortgage loan a long-term debt service reserve account. Given the complexities of, and volatility of both funding for and market demand for residential care facilities, such reserve account is important for improved risk management. The reserve account may be financed from mortgage proceeds, provided that the loan remains within the loan to value ratio. (See § 232.903, discussed below.) The amount required to be initially placed in the borrower's long-term debt service reserve account, and the minimum long-term balance to be *maintained* in that account, will be determined during underwriting and separately identified in the firm commitment. Although HUD may, under certain circumstances, permit the balance to fall below the required minimum long-term balance, the owner may not take any distribution except when both the long-term debt service reserve account is funded at the minimal long-term level and such distribution is otherwise permissible. The proposed establishment of the long-term debt service reserve account is in conjunction with the proposals governing the use and distribution of project funds, which is discussed below. This long-term reserve account would be required for new loans and refinancings.

#### Contract Rights and Obligations (Subpart B)

Subpart B of the part 232 regulations addresses contract rights and obligations to which all section 232 transactions are subject unless otherwise specified in another regulatory section in part 232.

Section 232.251, entitled "Cross-Reference," would be retitled "Other Applicable Regulations" and would continue to include the regulations cross-referenced in existing § 232.251, but also clarify the applicability of the new provisions included in subpart B.

The rule would add a new § 232.254 to provide that borrowers may, to the extent allowed in their transactional loan documents and applicable law, make and take distributions of mortgaged property. Although previously the borrower could take distributions only annually (or, in limited circumstances, semi-annually), the proposed rule would allow borrowers to take distributions more frequently, provided that, upon making a calculation of borrower surplus cash, no less frequently than semi-annually, they can demonstrate positive surplus cash in their semi-annual financial reports or repay any distributions made

during the fiscal period to the extent that they are not in a positive surplus cash position at the end of the fiscal period in which distributions are made. HUD has included language in the proposed regulation to clarify that it does not intend to override existing transactional agreements.

The proposed rule provides that upon each calculation of borrower surplus cash, the borrower must demonstrate positive surplus cash, or, to the extent that surplus cash is negative, the borrower must repay any distributions taken during such calculation period within 30 days or within such shorter period as may be required by HUD. The borrower shall be deemed to have taken distributions to the extent that surplus cash is negative unless, in conjunction with the calculation of surplus cash, the borrower provides to HUD documentation evidencing, to HUD's reasonable satisfaction, a lesser amount of total distributions.

New § 232.254 would also include a definition of borrower surplus cash, which would be defined in the Borrower Regulatory Agreement.

The rule would add a new § 232.256 to require that a borrower may not lease any portion of the project, or enter into any agreement with an operator without HUD's prior written consent.

The rule would revise the introductory paragraph of § 232.903, relating to the § 232/223(f) program, by amending the maximum mortgage amounts to provide that the new debt service reserve account may be considered part of the cost of financing. No such amendment is necessary for any § 232 programs other than § 232/223(f), since, for other programs, funding of the debt service reserve is an eligible cost that may be funded from mortgage proceeds to the extent that the insured loan remains below the maximum loan to value ratio.

#### Eligible Operators and Facilities and Restrictions on Fund Distributions (New Subpart F)

This proposed rule would add to part 232 a new subpart F entitled, "Eligible Operators and Facilities and Restrictions on Fund Distributions." As noted earlier in this preamble, operators carry out significant day-to-day duties in the administration of healthcare facilities. HUD finds that this important role needs to be explicitly addressed in regulation, by providing for the requisite accountability by such entities. The proposed new provisions recognize that a borrower may share its responsibility over the project with another entity. However, the fact that a borrower chooses to contract with a separate

entity to operate the project does not relieve the borrower of its obligation to safeguard and ensure the proper use of all project assets, or of its obligation to ensure that acts of the operator do not cause the borrower to be in noncompliance with the borrower's own obligations. Instead, these new provisions are directed to ensuring that an operator, which may be an entity separate from the borrower, is also required to safeguard and ensure the proper use of all project assets.

New § 232.1001 would advise that the scope of this new subpart is to establish the requirements applicable to the operator of a residential care facility under the Section 232 regulations.

New § 232.1003 would define several key terms used in a Section 232 transaction. Section 232.1003 would define "project," "identity of interest projects," "management agent," "operator," and "owner operator".

New § 232.1005 would address commingling of funds and direct that an operator must not, without HUD's prior approval, allow funds attributable to an FHA-insured or HUD-held healthcare facility to be commingled with funds attributable to another healthcare facility or business.

New § 232.1007 would provide that payments from operating funds for goods and services must be reasonable and not exceed amounts normally paid for such goods or services in the geographic area where the services are rendered or the goods are furnished, unless otherwise approved by HUD.

New § 232.1009 provides that no principal of the borrower entity may receive a salary or any payment of funds derived from operation of the project, other than from permissible distributions, without HUD's prior approval.

Violations of these requirements on the use of project assets and income would be subject to double damages, in addition to HUD's other remedies, pursuant to statutory amendments, described hereinafter, enacted in 2004. Section 421 of the Housing and Community Development Act of 1987 (12 U.S.C. 1715z-4a), entitled "Double damages remedy for unauthorized use of multifamily housing project assets and income," was amended by section 220 of Title II of Division I of the Consolidated Appropriations Act, 2005 (Public Law 108-447, 118 Stat. 2809, approved December 8, 2004), to expressly provide that a violation by "any person" of a regulatory agreement that applies to "a nursing home, intermediate care facility, board and care home, assisted living facility, or hospital whose mortgage is or, at the

time of the violations, was insured or held by the Secretary under title II of the National Housing Act" is subject to the double damages provisions of 12 U.S.C. 1715z-4a (See 118 Stat. 3320, and 12 U.S.C. 1715z-4a(a)(1)(A).) Section 220 further amended section 421 to include as "any person" subject to double damages "any nursing home lessee or operator" and to permit an action for double damages "to recover any assets or income used by a person in violation of \* \* \* any applicable regulation." (See 12 U.S.C. 1715z-4a(a)(2)(D) and 12 U.S.C. 1715z-4a(a)(1)(D).) Any assets or income used in violation of these regulatory requirements would be subject to double damages under section 421, as well as to all other remedies available to HUD, in the same way that use of assets or income in violation of a regulatory agreement is subject to such double damages and other remedies.

New § 232.1011 would address financial statements, which are also discussed in the proposed amendment to 24 CFR 5.801 below. This new section provides that, within 90 days following the end of each fiscal year, the owner must provide HUD with audited financial statements. These audited financial statements must be prepared and certified in accordance with the requirements of 24 CFR 5.801 and 200.36. The operator must provide HUD with complete quarterly and year-to-date financial reports based on an examination of the books and records of the operator's operations with respect to the healthcare facility.

New § 232.1013 would address leases and would provide that, except as provided in residential agreements in the normal course of business, an operator may not lease or sublease any portion of the project without HUD's prior written approval.

New § 232.1015 would address the role of management agents in a Section 232 project and would provide that an operator may, with the prior written approval of HUD, execute a management agent agreement setting forth the duties and procedures for managing matters related to the project. However, both the management agent and the management agent agreement must be acceptable to HUD and approved in writing by HUD. New § 232.1015 also provides that an operator may not enter into any agreement that provides for a management agent to have rights to or claims on funds owed to the operator.

New § 232.1015 would also address fees paid by an operator or borrower to a management agent. This section provides that management agent agreements and the fees set forth therein

must be approved by HUD, and that the fee may not be renegotiated without HUD's approval once the management agent agreement has been executed. New § 232.1015 also provides that HUD may approve an identity-of-interest management agent to be a management agent only if amounts paid to the identity-of-interest agent for goods and services provided to the healthcare facility are not in excess of amounts that would be charged by an independent agent and only if all goods and services benefit the project.

New § 232.1017 would address treatment of project revenue. New § 232.1017(a) directs that an operator must deposit in a separate segregated account in the project's name all revenue the operator receives operating the healthcare facility, and that the account must be with a financial institution whose deposits are insured by an agency of the Federal Government, provided that, in order to minimize risk to the insurance fund, where balances are likely to exceed federal limits on insurance of such deposits, funds must be in depository institutions acceptable to Ginnie Mae.

New § 232.1017(b) provides that operators, whether owner-operators or non-owner operators, must ensure that the healthcare facility maintain positive working capital at all times. If a quarterly financial statement demonstrates negative working capital, the operator must cure such violation or HUD may declare a default of the operator's regulatory agreement and pursue remedies.

New § 232.1019 reflects recognition of the highly regulated environment in which many Section 232 projects operate, and would require operators, unless HUD determines otherwise, to promptly notify the owner, mortgagee, and HUD of certain matters placing the facility's viable operation, and thus the mortgage security, at substantial risk. These matters include violations of permits and approvals, imposition of civil money penalties, or governmental investigations or inquiries involving fraud. HUD has determined that, given the responsibilities of servicing lenders with respect to risk mitigation of their residential care facility portfolio, it is appropriate that the lenders are timely provided with the same financial, census, and performance data (of the owner entity, as well as operator entity) that HUD is requiring borrowers and operators to routinely provide to HUD. Accordingly, this regulatory section provides that, concurrently with submitting to HUD financial data and census and performance data, the

borrower and operator also provide this data to the servicing lender.

In addition to the amendments made to the Section 232 regulations, HUD makes the following conforming amendments to 24 CFR parts 5, 200, and 207.

#### *B. Uniform Financial Reporting Standards (24 CFR Part 5; § 5.801)*

This proposed rule would amend the reporting requirements of 24 CFR 5.801 to include operators of projects with mortgages insured or held by HUD under the Section 232 program as entities that must submit financial reports. Borrowers are currently subject to this regulatory reporting requirement. HUD has determined that the audited financial statements of a borrower/owner are not sufficient to assess the financial status of a Section 232 project, because the viability of the project is heavily dependent on the operator's financial performance. HUD must also receive and review the financial statements of the operator, as may be applicable, for an accurate assessment of the project's financial status.

This proposed rule would, therefore, require owners to submit audited financial statements on an annual basis and would require operators to submit financial statements quarterly, covering separately the most recent quarter and the fiscal year to date. Quarterly and year-to-date financial statements are appropriate for operators for a number of reasons. First, they provide much more timely notice of operator financial weaknesses and trends than annual statements would provide. The timeliness is further enhanced in that the operator statements may be operator-certified rather than audited, allowing the operator to provide them much more promptly at the end of a reporting period. With respect to the skilled nursing facilities (of which a large portion of HUD's residential care facility portfolio is comprised), much of the information is also furnished in Medicare and Medicaid Cost Reports to fulfill other government obligations and serve as a basis for reimbursement, a practice that provides an additional check on accuracy.

This proposed rule also amends the reporting requirements with respect to facilities insured under Section 232, by specifying that the financial statements being submitted to HUD must be concurrently submitted to the servicing lender. Given the servicing lenders' responsibilities with respect to risk mitigation of their residential care facility portfolio, and given the difficulty that some lenders have in obtaining financial data related to the

facility, it is appropriate that the lenders be timely provided the same financial data (of the owner entity, as well as the operator entity) that HUD is requiring borrowers and operators to routinely provide to HUD. Both owner and operator financial reporting requirements would apply beginning with the year in which the final rule following this proposed rule becomes effective.

#### *C. Introduction to FHA Programs: Physical Condition of Multifamily Properties (Part 200, Subpart P)*

Section 200.855(c) of HUD's regulations (24 CFR 200.855(c)), which addresses timing of inspections, would narrow and streamline the scope of Section 232 facilities that are routinely inspected by the Real Estate Assessment Center (REAC). In particular, facilities such as assisted living facilities and board and care facilities would be subject to routine REAC inspections unless the state or local government had a reliable and adequate inspection system in place. The remainder of the Section 232 properties, and properties that are routinely surveyed pursuant to regulations of the Centers for Medicare and Medicaid Services, would be inspected only when and if HUD determined, on a case-by-case basis and on the basis of information received, that inspection of such facility is needed to assure protection of residents or the adequate preservation of the project. This amendment would help assure that facilities surveyed frequently by state regulatory agencies, for physical condition matters related to resident care and safety, are not subject to duplicative inspections. HUD- and FHA-approved mortgagees now have ready electronic access to the results of state agency inspections conducted pursuant to requirements of the Centers for Medicare and Medicaid Services.

#### *D. Multifamily Housing Mortgage Insurance (Part 207)*

##### *Contract Rights and Obligations (Subpart B)*

Subpart B of the part 232 regulations addresses contract rights and obligations and the rights and duties of the mortgagee under the contract of insurance.

HUD is taking this opportunity to make changes to HUD's regulations in this subpart affecting the Section 232 programs. These proposed changes alter several of the amendments to the multifamily regulations adopted last spring. (See 76 FR 24363 May 11, 2011, HUD Multifamily Rental Projects: Regulatory Revisions.)

Section 207.255, "Defaults for purposes of insurance claim," includes language defining the date of defaults. This proposed rule revises § 207.255(a)(4) by clarifying the dates on which certain monetary and other defaults occur.

This proposed rule modifies § 207.258, "Insurance claim requirements," by deleting in paragraph (a)(2) a parenthetical expression.

This proposed rule also modifies § 207.258(b)(1)(i) by clarifying the time period within which a mortgagee may elect to assign a mortgage to the Commissioner.

#### *E. Costs and Benefits of Proposed Revisions to the Section 232 Program Regulations*

As discussed in this preamble, this proposed rule updates HUD's Section 232 program regulations similar to the 2011 updates that were made to HUD's multifamily rental project regulations and accompanying closing documents. The revisions proposed by this rule update the Section 232 regulations to reflect existing practices in financing and refinancing healthcare facilities, and to decrease risk to the program due to outdated regulations and the need for greater accountability by healthcare facility operators. Key changes highlighted in the preamble include requiring borrowers to establish a long term debt-service reserve account, requiring operators to submit quarterly and year-to-date self-certified financial reports, and reducing duplicative physical inspections.

The valued benefits from fewer physical inspections, and the costs from increased financial reporting and the opportunity cost of the debt service reserve fund, each total less than \$1 million. Unvalued benefits include uninterrupted services of healthcare facilities, which otherwise would close due to foreclosure. Transfers from avoided claim payments total \$13 million. The total costs, benefits, and transfers of this rule will not in any year exceed the \$100 million threshold set by Executive Order 12866 (Regulatory Planning and Review). Therefore, the rule is not economically significant.

The risk mitigation requirements proposed by this rule are necessary due to the combination of two particular risks facing healthcare facilities. First, similar to multifamily residential properties, the owner usually relies on a separate entity to operate the facility. The performance of the operator is crucial to the mortgagor's ability to repay the mortgage. Since the operator may not be known to FHA at the time of underwriting, or may change during

the term of the mortgage, the risk of operator deficiency is difficult to assess. Second, unlike residential or other commercial properties, the value of a poorly maintained and operated facility can decrease dramatically because the building was designed specifically for healthcare use and may not retain the mortgaged value at resale due to a lack of alternative uses. Thus, FHA may face more uncertainty when selling foreclosed healthcare properties than foreclosed residential properties. This rule therefore proposes requirements intended to identify operator deficiencies earlier and ensure that funds are available if financial problems arise.

The rule also proposes to require the borrower to establish a long-term debt service reserve fund. Although FHA currently requires owners of new construction projects to maintain a reserve fund until sustainable occupancy is reached, usually one to two years, this new requirement would require a reserve fund to be maintained throughout the life of the mortgage and used in case of operator deficiency. Of the 30 insurance claims from 2009 to mid-2011, operator deficiencies played a role in the property's performance demise in 23. Further, these claims were distributed widely over age of loan, not simply in the first few years, indicating the need for a reserve fund over the life of the mortgage. The maintenance of a reserve is to decrease the number of nonperforming mortgages by providing additional time to resolve operator deficiencies.

Based on FHA's experience, a reserve fund can be an important source for debt service payments during a period of instability. Thus, the reserve can delay the point at which a lender finds it necessary to file a claim, providing extra time for the parties to restructure and stabilize a project and avoid a claim to HUD. FHA has accepted claims where borrowers were pursuing workouts, but stability could not be achieved prior to the lenders' expenses becoming too burdensome to sustain. The extra time afforded by a debt service reserve makes avoiding a claim more likely under such scenarios. In its analysis of 2009, 2010, and early 2011 claims, HUD found that 5 out of 30 projects brought to claim may have benefited from the additional time provided by a debt service reserve. Finally, as an additional offset for borrowers to the added requirement of debt service reserve, the rule also provides greater flexibility to borrowers in the making of distributions and use of surplus cash. Assuming that, as a result of the rule, 2 fewer claims were

paid annually, FHA would save \$13 million per year, if projected based on the average unpaid balance (UPB) of assigned Section 232 mortgages from 2009–2011, which was \$6.5 million. In the absence of these claim payments, FHA could pass these savings on to its mortgagors and thus such savings are best viewed as a transfer between borrowers.

The amount of funds required to be initially placed in the debt service reserve fund, and the minimum long-term balance, will be determined during underwriting. FHA estimates that on average, a borrower's monthly debt service will increase by approximately 1.5 percent. Based on an expected average of \$3.4 billion annually in the value of new mortgage endorsements, borrowers would be required, in aggregate, to place and maintain \$51 million in the fund. The cost to borrowers is the lower return from restricting this amount to the reserve fund compared to other investment options. This opportunity cost of holding these funds in a reserve account is, therefore, calculated as the difference between the average market rate of return and the risk-free interest rate. The average market rate is represented by the real annualized return of the S&P 500 between 1990 and 2011, which equals 5.37 percent. The risk-free interest rate is the average 10-year Treasury rate between 1990 and 2011, which equals 2.6 percent. The opportunity cost of holding the estimated funds in a reserve fund totals \$141,270.

This rule also requires operators to submit annual and year-to-date financial reports. Currently, the borrower, but not the operator, is required to provide audited financial statements. Although submission of the operator's financial reports is a new requirement, the expense of such reports is mitigated by allowing the operator to submit self-certified, rather than audited statements. Moreover, the required operator financial information is data that operators need to maintain in the normal course of business in order to monitor and manage their own operations effectively. FHA estimates this will require approximately 10,000 employee hours annually to prepare and submit these reports (2,500 respondents, 4 reports per year and 1 hour to generate each report). The median wage of the employees who prepare these reports is approximately \$75 per hour. Thus, the total cost of complying with this requirement would be \$750,000.

Finally, this rule exempts facilities from FHA physical inspection requirements if they are inspected by

state or local agencies in order to eliminate duplicative inspections. FHA estimates that, as a result, approximately 1,391 inspections would be avoided per year. The estimated cost per inspection totals \$475, which would mean a total annual inspection savings of \$660,725.

In addition to the valued benefits, this rule also provides benefits that are less easily quantified. As explained above, HUD expects the reserve fund and financial reporting requirements to

decrease the number of claims paid. While some troubled facilities may be stabilized and continue operating, at this stage of delinquency, they are often forced to close. Thus, there is a disruption of healthcare services to the community and costs to moving residents from one facility to another. In smaller communities, there are fewer alternatives for facility residents, and the benefits of avoiding foreclosure are greater as residents may be without needed services for a long period. In

larger cities, existing facilities may be able to absorb the additional demand fairly quickly. In both of these cases, however, residents bear costs associated with transferring between facilities. Although the avoided loss or interruption of services is difficult to quantify and varies by city, the avoided loss or interruption of services is an important benefit that this rule is trying to achieve.

SUMMARY OF VALUED ANNUAL BENEFITS, COSTS, AND TRANSFERS

	Benefits	Costs	Transfers
Debt Service Reserve Fund .....	\$660,725	\$141,270	\$13,000,000
Financial Reporting .....	.....	750,000	.....
Physical Inspections.			
<b>Total .....</b>	<b>660,725</b>	<b>891,270</b>	<b>13,000,000</b>

III. Findings and Certifications

Executive Order 13563, Regulatory Review

The President’s Executive Order (EO) 13563, entitled “Improving Regulation and Regulatory Review,” was signed by the President on January 18, 2011, and published on January 21, 2011, at 76 FR 3821. This EO requires executive agencies to analyze regulations that are “outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned.” Section 4 of the EO, entitled “Flexible Approaches,” provides, in relevant part, that where relevant, feasible, and consistent with regulatory objectives, and to the extent permitted by law, each agency shall identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public. As discussed earlier in this preamble, the Section 232 regulations have not been updated since 1996. HUD submits that the changes proposed by this rule to the Section 232 regulations are consistent with the EO’s directions. As the preceding section discussed, the changes proposed by this rule will modernize the Section 232 program, reduce burden by eliminating duplicative physical inspections, providing flexibility to borrowers in the making of distributions and use of surplus cash, and increasing accountability to strengthen the program, thereby helping it ensure that it remains viable for the financing of healthcare facilities.

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) (5 U.S.C. 601 *et seq.*) generally requires an agency to conduct a regulatory flexibility analysis of any rule subject to notice and comment rulemaking requirements, unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities.

This rule is directed to creating transparency in HUD’s Section 232 program by, codifying existing and longstanding provisions imposed on a Section 232 borrower, and strengthening this program through stronger risk management practices, such as making operators more accountable for their role in administering Section 232 healthcare facilities. As noted under the discussion of EO 13563, this rule proposes amendments that will enhance HUD’s oversight ability, while minimizing the burdens on private actors, to the benefit of participants and facility clients. Additionally, by clarifying and codifying existing requirements, the rule makes it easier for borrowers and operators to comply with their legal obligations. Through this rule, the viability of the Section 232 program and HUD’s enforcement authority are increased, and waste, fraud, and abuse are reduced.

Approximately 3,343 of the anticipated annual participants in the Section 232 program are small entities, including approximately 2,500 entities involved in nursing homes, 725 entities involved in assisted living facilities, and 70 other entities. (The total figure exceeds the number of facilities involved, because a single transaction many involve distinct legal entities

serving as the operator and owner.) The changes required by this rule do not impose significant economic impacts on these small entities or otherwise adversely disproportionately burden such small entities. The reporting requirements of this rule have been tailored to complement normal business accounting practices. Accordingly, the undersigned certifies that this rule will not have a significant economic impact on a substantial number of small entities.

Notwithstanding HUD’s determination that this rule will not have a significant effect on a substantial number of small entities, HUD specifically invites comments regarding any less burdensome alternatives to this rule that will meet HUD’s objectives as described in this preamble.

Environmental Impact

A Finding of No Significant Impact with respect to the environment has been made, in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)). That finding is available for public inspection between the hours of 8 a.m. and 5 p.m. weekdays in the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street SW., Room 10276, Washington, DC 20410–0500. Due to security measures at the HUD Headquarters building, please schedule an appointment to review the finding by calling the Regulations Division at 202–402–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this

number via TTY by calling the Federal Relay Service at 800-877-8339.

*Executive Order 13132, Federalism*

Executive Order 13132 (entitled “Federalism”) prohibits an agency from publishing any rule that has federalism implications if the rule either: (1) Imposes substantial direct compliance costs on state and local governments and is not required by statute, or (2) preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This rule will not have federalism implications and would not impose substantial direct compliance

costs on state and local governments or preempt state law within the meaning of the Executive Order.

*Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) (UMRA) establishes requirements for federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments, and on the private sector. This proposed rule does not impose any federal mandates on any state, local, or tribal governments, or on the private sector, within the meaning of UMRA.

*Information Collection Requirements*

The information collection requirements contained in this proposed rule have been submitted to the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520). In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

The burden of the information collections in this proposed rule is estimated as follows:

**REPORTING AND RECORDKEEPING BURDEN**

Section reference	Number of respondents	Number of responses per respondent	Estimated average time for requirement (in hours)	Estimated annual burden (in hours)
24 CFR 5.801(c)(4) Financial information .....	2,500	4	1	10,000
24 CFR 232.11 HUD written approval .....	100	1	1	100
24 CFR 232.1005 HUD written approval .....	25	1	1	25
24 CFR 232.1007 HUD approval .....	25	1	1	25
24 CFR 232.1009 HUD written approval .....	50	1	1	50
24 CFR 232.1011 Financial statement .....	2,500	1	60	150,000
24 CFR 232.1013 Specifications for lease agreement, HUD written approval .....	25	1	1	25
24 CFR 232.1015 HUD written approval .....	25	1	1	25
24 CFR 232.1017 HUD written approval .....	25	1	1	25
24 CFR 232.1019 HUD written approval .....	1,750	2	.50	1,750
<b>Totals .....</b>	<b>7,025</b>	<b>14</b>	<b>68.5</b>	<b>162,025</b>

In accordance with 5 CFR 1320.8(d)(1), HUD is soliciting comments from members of the public and affected agency concerning this collection of information to:

- (1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of HUD, including whether the information will have practical utility;
- (2) Evaluate the accuracy of HUD’s estimate of the burden of the proposed collection of information;
- (3) Enhance the quality, utility, and clarity of the information to be collected; and
- (4) Minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated collection techniques or other forms of information technology; e.g., permitting electronic submission of responses.

Interested persons are invited to submit comments regarding the information collection requirements in this rule. Comments must refer to the proposal by name and docket number (FR-5465-P-01) and must be sent to:

HUD Desk Officer, Office of Management and Budget, New Executive Office Building, Washington, DC 20503. Fax number: 202-395-6947. and

Reports Liaison Officer, Office of Housing, Department of Housing and Urban Development, 451 Seventh Street SW., Room 9116, Washington, DC 20410-8000.

Interested persons may submit comments regarding the information collection requirements electronically through the Federal eRulemaking Portal at <http://www.regulations.gov>. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the <http://www.regulations.gov> Web site can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

**List of Subjects**

*24 CFR Part 5*

Administrative practice and procedure, Aged, Claims, Grant programs—housing and community development, Individuals with disabilities, Intergovernmental relations, Loan programs—housing and community development, Low and moderate income housing, Mortgage insurance, Penalties, Pets, Public housing, Rent subsidies, Reporting and recordkeeping requirements, Social Security, Unemployment compensation, Wages.

*24 CFR Part 200*

Administrative practice and procedure, Claims, Equal employment opportunity, Fair housing, Home improvement, Housing standards, Lead poisoning, Loan programs—housing and community development, Mortgage insurance, Organization and functions (Government agencies), Penalties, Reporting and recordkeeping.

*24 CFR Part 207*

Mortgage insurance—Nursing homes, Intermediate care facilities, Board and



care homes, and Assisted living facilities.

24 CFR Part 232

Fire prevention, Health facilities, Loan programs—health, Loan programs—housing and community development, Mortgage insurance, Nursing homes, Reporting and recordkeeping requirements.

Accordingly, parts 5, 200, 207, and 232 of title 24 of the Code of Federal Regulations are proposed to be amended as follows:

PART 5—GENERAL HUD PROGRAM REQUIREMENTS; WAIVERS

1. The authority citation for 24 CFR part 5 continues to read as follows:

Authority: 42 U.S.C. 1437a, 1437c, 1437d, 1437f, 1437n, 3535(d), and Sec. 327, Pub. L. 109-115, 119 Stat. 2936.

- 2. Amend § 5.801 to:
a. Add paragraph (a)(6),
b. Revise the first sentence of the introductory text of paragraph (b),
c. Add paragraph (b)(4),
d. Revise the heading of paragraph (c),
e. Add paragraph (c)(4), and
f. Add paragraph (d)(4) to read as follows:

§ 5.801 Uniform financial reporting standards.

(a) \* \* \*
(6) Operators of projects with mortgages insured or held by HUD under section 232 of the Act (Mortgage Insurance for Nursing Homes, Intermediate Care Facilities, Board and Care Homes).

(b) Entities (or individuals) to which this subpart is applicable must provide to HUD such financial information as required by HUD. Such information must be provided on an annual basis, except as required more frequently under paragraph (c)(4) of this section.

\* \* \* \* \*

(4) With respect to financial reports relating to properties insured under Section 232 of the Act, concurrently with submitting the information to HUD, this information must also be submitted to the mortgagee in a format and manner prescribed by the Secretary.
(c) Filing of financial reports. \* \* \*

(4) For entities listed in paragraph (a)(6) of this section, the financial information to be submitted to HUD in accordance with paragraph (b) of this section must be submitted to HUD on a quarterly and fiscal-year-to-date basis, within 30 days of the end of each quarterly reporting period. The financial statements submitted pursuant to

paragraph (a)(6) of this section may, at the operator's option, be operator-certified rather than audited, provided, however, that if the operator is also the borrower, then that entity's obligation to submit an annual audited financial statement within 90 days of its fiscal year end (in addition to its obligation as an operator to submit financial information on a quarterly and year-to-date basis) remains and is not obviated. Additionally, if HUD has reason to believe that a particular operator's operator-certified statements may be unreliable or are presented in a manner that is inconsistent with Generally Accepted Accounting Principles, HUD may, on a case-by-case basis, require audited financial statements from the operator. Additionally, with respect to facilities with FHA-insured or HUD-held Section 232 mortgages, HUD may request more frequent financial statements from the borrower, as specified under (a)(4)(x), and/or the operator on a case-by-case basis when the circumstances warrant. Nothing in the regulations in this section limits HUD's ability to obtain further or more frequent information when appropriate pursuant to the applicable regulatory agreement.

(d) \* \* \*
(4) Entities described in paragraph (a)(6) of this section must comply with the requirements of this section with respect to fiscal years ending [a date of one year after the effective date of the final rule to be inserted at the final rule stage] and later.

\* \* \* \* \*

PART 200—INTRODUCTION TO FHA PROGRAMS

3. The authority citation for part 200 continues to read as follows:

Authority: 12 U.S.C. 1702-1715-z-21; 42 U.S.C. 3535(d).

4. In 200.855, add a new paragraph (c)(5) to read as follows:

§ 200.855 Physical condition standards and physical inspection requirements.

\* \* \* \* \*

(c) \* \* \*
(5)(i) For Assisted Living Facilities and Board and Care Facilities, the initial inspection required under this subpart will be conducted within the same time restrictions set forth in paragraph 200.855(c)(4) immediately above, and any further inspections will be conducted at a frequency determined consistent with § 200.857, and

(ii) For any other Section 232 facilities, the inspection will be conducted only when and if HUD determines, on the basis of information

received, such as through a complaint, site inspection, or referral by a state agency, on a case-by-case basis, that inspection of a particular facility is needed to assure protection of the residents or the adequate preservation of the project.

PART 207—MULTIFAMILY HOUSING MORTGAGE INSURANCE

5. The authority citation for part 207 continues to read as follows:

Authority: 12 U.S.C. 1701z-11(e), 1713, and 1715b; 42 U.S.C. 3535(d).

6. In § 207.255(a)(4) introductory text, remove the reference to "paragraph (b)" and add in its place a reference to "paragraph (a)".

7. In § 207.258 revise paragraphs (a)(2) introductory text and (b)(1)(i) to read as follows:

§ 207.258 Insurance claim requirements.

(a) \* \* \*

(2) For mortgages funded with the proceeds of state or local bonds, GNMA mortgage-backed securities, participation certificates, or other bond obligations specified by the Commissioner (such as an agreement under which the insured mortgagee has obtained the mortgage funds from third-party investors and has agreed in writing to repay such investors at a stated interest rate and in accordance with a fixed repayment schedule), any of which contains a lock-out or prepayment premium, the mortgagee must, in the event of a default during the term of the prepayment lock-out or prepayment premium:

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(i) If the mortgagee elects to assign the mortgage to the Commissioner, the mortgagee shall, at any time within 30 days after the date HUD acknowledges the notice of election, file its application for insurance benefits and assign to the Commissioner, in such manner as the Commissioner may require, any applicable credit instrument and the realty and chattel security instruments.

\* \* \* \* \*

PART 232—MORTGAGE INSURANCE FOR NURSING HOMES, INTERMEDIATE CARE FACILITIES, BOARD AND CARE HOMES, AND ASSISTED LIVING FACILITIES

8. The authority citation for 24 CFR part 232 continues to read as follows:

Authority: 12 U.S.C. 1715b, 1715w; 42 U.S.C. 3535(d).

9. Throughout part 232, the word “mortgagor” is revised to read “borrower” wherever it appears.

10. Revise § 232.1 to read as follows:

**§ 232.1 Eligibility requirements.**

All of the requirements, except § 200.5, set forth in 24 CFR part 200 subpart A, apply to project mortgages insured under Section 232 of the National Housing Act (12 U.S.C. 1715w), as amended.

11. Redesignate § 232.3 as § 232.7 and add a new § 232.3 to read as follows:

**§ 232.3 Eligible borrower.**

For mortgages originated after *[a date of one year after the effective date of the final rule to be inserted at the final rule stage]*, the borrower shall be a single asset entity acceptable to the Commissioner, as limited by the applicable section of the Act, and shall possess the powers necessary and incidental to operating the project, except that the Commissioner may approve a non-single asset borrower entity under such circumstances, terms, and conditions determined and specified as acceptable to the Commissioner.

12. Add new §§ 232.9 and 232.11 to read as follows:

**§ 232.9 Mortgaged property.**

*Mortgaged property* includes all of Borrower’s interests in property, real, personal, or mixed, covered by the mortgage or mortgages securing the note endorsed for insurance or held by the Secretary, as further defined in the mortgage documents.

**§ 232.11 Establishment and maintenance of long-term debt service reserve account.**

To be eligible for insurance under this part, and except with respect to Supplemental Loans to Finance Purchase and Installation of Fire Safety Equipment (subpart C of this part), the borrower must establish at final closing and maintain throughout the term of the mortgage a long-term debt service reserve account. This long-term debt service reserve account may be financed as part of the initial mortgage amount, provided that the maximum mortgage amount as otherwise calculated is not thereby exceeded. The amount required to be initially placed in the long-term debt service reserve account and the minimum long-term balance to be maintained in that account will be determined during underwriting and separately identified in the firm commitment. Although HUD may, when appropriate to avert a mortgage insurance claim, permit the balance to fall below the required minimum long-term balance, the borrower may not take

any distribution of mortgaged property except when both the long-term debt service reserve account is funded at the minimal long-term level and such distribution is otherwise permissible.

**Subpart B—Contract Rights and Obligations**

13. Revise § 232.251 to read as follows:

**§ 232.251 Other applicable regulations.**

(a) *Cross-reference.* (1) All of the provisions, except § 207.258b, of 24 CFR part 207, subpart B, relating to mortgages insured under section 207 of the National Housing Act, apply to mortgages insured under section 232 of the Act.

(2) For the purposes of this subpart, all references in 24 CFR part 207 to section 207 of the Act shall be construed to refer to section 232 of the Act.

(3) Unless otherwise specified in this part, the regulations in this subpart B apply to all mortgages insured under section 232 of the Act.

(b) [Reserved]

14. Add new §§ 232.254 and 232.256, to read as follows:

**§ 232.254 Withdrawal of project funds, including for repayments of advances from the borrower, operator, or management agent.**

(a) *General.* Borrower may make and take distributions of mortgaged property, as set forth in the mortgage loan transactional documents, to the extent and as permitted by the law of the applicable jurisdiction, provided that, upon each calculation of borrower surplus cash, which calculation shall be made no less frequently than semi-annually, borrower must demonstrate positive surplus cash, or to the extent surplus cash is negative, repay any distributions taken during such calculation period within 30 days or within such shorter period as may be required by HUD. Borrower shall be deemed to have taken distributions to the extent that surplus cash is negative unless, in conjunction with the calculation of surplus cash, borrower provides to HUD documentation evidencing, to HUD’s reasonable satisfaction, a lesser amount of total distributions. To the extent that the provisions of this paragraph (a) are inconsistent with the provisions in a borrower’s existing transactional loan documents, including without limitation any HUD-required regulatory agreement, the provisions of the transactional loan documents shall apply.

(b) *Definition.* Borrower surplus cash means any cash remaining in the Borrower’s accounts after:

(1) The payment of:

(i) All sums due or currently required to be paid under the terms of any mortgage or note insured or held by the Secretary;

(ii) All amounts required to be deposited in the project’s reserve fund for replacements, long-term debt service reserve account, or residual receipts account; and

(iii) All project obligations of the borrower other than the insured mortgage, unless funds for payment are set aside or deferment of payment has been approved by the Secretary; and

(2) The segregation of:

(i) An amount equal to the aggregate of all special funds required to be maintained by the project, including the long-term debt service escrow account;

(ii) Any tenant security deposits held; and

(iii) All other accrued items payable by borrower within 30 days after the end of the annual or semi-annual fiscal period for which surplus cash is calculated.

**§ 232.256 Leases.**

A borrower may not lease any portion of the project or enter into any other agreement with an operator without HUD’s prior written consent.

15. Revise the introductory text of § 232.903, and § 232.903(c) and (d) to read as follows:

**§ 232.903 Maximum mortgage limitations.**

Notwithstanding the maximum mortgage limitations set forth in § 200.15 of this chapter, a mortgage within the limits set forth in this section shall be eligible for insurance under this subpart.

\* \* \* \* \*

(c) *Project to be refinanced—additional limit.* (1) In addition to meeting the requirements of paragraphs (a) and (b) of this section, if the Project is to be refinanced by the insured mortgage, the maximum mortgage amount must not exceed the cost to refinance the existing indebtedness. For the purposes of this requirement:

(i) The Project shall not have changed ownership, or

(ii) The Project shall have been sold to a purchaser who has an identity of interest with the seller (as defined by the Commissioner).

(2) The existing indebtedness will consist of the following items, the eligibility and amounts of which must be determined by the Commissioner:

(i) The amount required to pay off the existing indebtedness;

(ii) The amount of the initial deposit for the reserve fund for replacements;

(iii) Reasonable and customary legal, organization, title, and recording expenses, including mortgagee fees under § 232.15;

(iv) The estimated repair costs, if any;

(v) Architect's and engineer's fees, municipal inspection fees, and any other required professional or inspection fees;

(vi) The amount of any debt service reserve account required by the Commissioner.

(d) *Project to be acquired—additional limit.* In addition to meeting the requirements of paragraphs (a) and (b) of this section, if the project is to be acquired by the borrower and the purchase price is to be financed with the insured mortgage, the maximum amount must not exceed 85 percent for a profit-motivated borrower and 90 percent for a private nonprofit borrower of the cost of acquisition as determined by the Commissioner. The cost of acquisition shall consist of the following items, to the extent that each item (except for item numbered (1)) is paid by the purchaser separately from the purchase price. The eligibility and amounts of these items must be determined in accordance with standards established by the Commissioner.

(1) Purchase price is indicated in the purchase agreement;

(2) An amount for the initial deposit to the reserve fund for replacements;

(3) Reasonable and customary legal, organizational, title, and recording expenses, including mortgagee fees under § 232.15;

(4) The estimated repair cost, if any;

(5) Architect's and engineer's fees, municipal inspection fees, and any other required professional or inspection fees;

(6) The amount of any debt service reserve account required by the Commissioner.

16. Add new subpart F to read as follows:

**Subpart F—Eligible Operators and Facilities and Restrictions on Fund Distributions**

Sec.

232.1001 Scope.

232.1003 Definitions.

232.1005 Treatment of project operating accounts.

232.1007 Operating expenses.

232.1009 Payments to borrower principals prohibited.

232.1011 Financial reports.

232.1013 Leases.

232.1015 Management agents.

232.1017 Restrictions on deposit, withdrawal, and distribution of funds, and repayment of advances.

232.1019 Prompt notification to HUD and mortgagee of circumstances placing the value of the security at risk.

**Subpart F—Eligible Operators and Facilities and Restrictions on Fund Distributions**

**§ 232.1001 Scope.**

This subpart establishes requirements applicable to the operators of healthcare facilities and the facilities under this part.

**§ 232.1003 Definitions.**

The following definitions apply throughout this part.

*Identity-of-interest projects* refers to those projects that are operated by a licensed operator and/or managed by a management agent who shares an identity of interest with the ownership entity.

*Management agent* means an entity that, pursuant to a contract with the operator or borrower, manages matters related to the project, subject to limitations set forth in § 232.1015.

*Operator* means a single asset entity acceptable to the Commissioner, and shall possess the powers necessary and incidental to operating the healthcare facility, except that the Commissioner may approve a non-single asset entity under such circumstances, terms, and conditions determined and specified as acceptable to the Commissioner.

*Owner operator* means an owner who operates its own project and does not lease the project or otherwise contract with an eligible operator. In that instance, the borrower entity and the operating entity are the exact same legal entity, and the owner operator must comply with regulatory provisions governing the use of funds for both operators and borrowers in § 232.254, § 232.1005, and § 232.1017.

*Project* means any and all assets of whatever nature or wherever situated related to the insured mortgage loan, including without limitation the mortgaged property, any site improvements, and any collateral owned by operators securing the insured mortgage loan.

**§ 232.1005 Treatment of project operating accounts.**

(a) All accounts deriving from the operation of the property, including operator accounts and including all funds received from any source or derived from the operation of the facility, are project assets subject to control under the insured mortgage loan's transactional documents, including, without limitation, the operator's regulatory agreement. Funds generated by the operation of the

healthcare facility shall be deposited into a federally insured bank account in the name of the single asset operator of the facility, provided that an account held in an institution acceptable to the Government National Mortgage Association may have a balance that exceeds the amount to which such insurance is limited. If the borrower is not also the operator, any of owner's project-related funds shall be deposited into a federally insured bank account in the name of the single asset borrower.

(b) An operator must not allow funds attributable to the healthcare facility to be commingled with funds attributable to another healthcare facility or any other business unless approved by HUD. Any centralized accounting system involving project funds must have prior HUD approval and must clearly delineate which portion of the funds in an account are attributable to the particular facility.

(c) Except to the extent that the healthcare facility maintains positive working capital, an operator may not advance or otherwise use funds attributable to the operator's business at a project under this part to pay expenses attributable to any other project or business without the advance written approval of HUD.

**§ 232.1007 Operating expenses.**

Goods and services purchased or acquired in connection with the Project shall be reasonable and necessary for the operation or maintenance of the Project, and the costs of such goods and services incurred by the borrower or operator shall not exceed amounts normally paid for such goods or services in the area where the services are rendered or the goods are furnished, except as otherwise approved by HUD.

**§ 232.1009 Payments to borrower principals prohibited.**

No principal of the borrower entity may receive a salary or any payment of funds derived from operation of the project, other than from permissible distributions, except as approved by HUD.

**§ 232.1011 Financial reports.**

Within 90 days following the end of each entity's fiscal year, the borrower must provide HUD an audited annual financial report based on an examination of its books and records, in such form and substance required by HUD in accordance with 24 CFR 5.801 and 200.36. Operators must submit financial statements quarterly within 30 days of the date of the end of each fiscal quarter, setting forth both quarterly and

fiscal year-to-date information in accordance with 24 CFR 5.801(c)(4).

**§ 232.1013 Leases.**

Except to enter into resident agreements in the standard course of operating the healthcare facility, an operator may not lease or sublease any portion of the project without HUD's prior written approval.

**§ 232.1015 Management agents.**

(a) An operator or borrower may, with the prior written approval of HUD, execute a management agent agreement setting forth the duties and procedures for matters related to the management of the project. Both the management agent and the management agent agreement must be acceptable to HUD and approved in writing by HUD.

(b) An operator or borrower may not enter into any agreement that provides for a management agent to have rights to or claims on funds owed to the operator.

(c) Management agent fees may not be renegotiated without HUD's written approval once the management agent agreement has been executed.

(d) HUD may approve an identity of interest between a management agent and a borrower or operator only to the extent that the goods and services provided benefit the project and if the operator clearly establishes that the amounts paid to the identity-of-interest management agent for goods and services provided to the healthcare facility are not in excess of amounts that would be charged by an independent management agent.

**§ 232.1017 Restrictions on deposit, withdrawal, and distribution of funds, and repayment of advances.**

(a) *Deposit of funds.* An operator must deposit all revenue the operator receives directly or indirectly in connection with the operation of the healthcare facility in a separate, segregated account. The account must be with a financial institution whose deposits are insured by an agency of the Federal Government, *provided* that an account held in an institution acceptable to the Government National Mortgage Association may have a balance that exceeds the amount to which such insurance is limited.

(b) *Withdrawals of funds.* Operators, whether or not an operator is also the borrower, shall at all times maintain positive working capital for the healthcare facility. If a quarterly financial statement, required pursuant to § 232.1011, demonstrates negative working capital for the healthcare facility, the operator must cure such

violation or HUD may pursue such remedies as set forth in the insured mortgage loan's transactional documents.

**§ 232.1019 Prompt notification to HUD and mortgagee of circumstances placing the value of the security at risk.**

(a) HUD and the mortgagee shall be informed of any notification of any failure to comply with governmental requirements including the following:

(1) The licensed operator of a project shall promptly provide the mortgagee and HUD with a copy of any notification that has placed the licensure, a provider funding source, and/or the ability to admit new residents at risk, and any responses to those notices, provided that HUD may determine certain information to be exempt from this requirement based upon severity level. Such required information shall include, but is not limited to, the following types of notices and responses:

(i) The operator shall deliver to HUD and the mortgagee electronically, within 48 hours after the date of receipt, copies of any and all notices, reports, surveys, and other correspondence (regardless of form) received by the operator from any governmental authority that includes any statement, finding, or assertion that:

(A) The operator or the project is or may be in violation of (or default under) any of the permits and approvals or any governmental requirements applicable thereto;

(B) Any of the permits and approvals is to be terminated, limited in any way, or not renewed;

(C) Any civil money penalty (other than a de minimis amount) is being or may be imposed; or

(D) The operator or the project is subject to any governmental investigation or inquiry involving fraud.

(ii) The operator shall also deliver to HUD and the mortgagee, simultaneously with delivery to any governmental authority, any and all responses given by or on behalf of the operator to any of the foregoing and shall provide to HUD and the mortgagee, promptly upon request, such additional information relating to any of the foregoing as HUD or the mortgagee may request. The receipt by HUD and/or the mortgagee of notices, reports, surveys, correspondence, and other information shall not in any way impose any obligation or liability on HUD, the mortgagee, or their respective agents, representatives, or designees to take (or refrain from taking) any action; and HUD, the mortgagee, and their respective agents, representatives, and designees shall have no liability for any

failure to act thereon or as a result thereof.

(2) The operator shall provide additional and ongoing information as requested by the borrower, mortgagee, or HUD pertaining to matters related to that risk. Controlling documents between or among any of the parties may provide further requirements with respect to such notification and communication.

(b) This section is applicable to all operators on the effective date of this regulation.

Dated: April 12, 2012.

**Carol J. Galante,**

*Acting Assistant Secretary for Housing—  
Federal Housing Commissioner.*

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**DEPARTMENT OF DEFENSE**

**Department of the Army, Corps of Engineers**

**33 CFR Part 334**

**Meloy Channel, U.S. Coast Guard Base Miami Beach, FL; Restricted Area**

**AGENCY:** United States Army Corps of Engineers, Department of Defense.

**ACTION:** Notice of proposed rulemaking and request for comments.

**SUMMARY:** The U.S. Army Corps of Engineers (Corps) is proposing to amend its regulations to establish a new restricted area in the waters surrounding the U.S. Coast Guard Base Miami Beach, Florida (Base Miami Beach). Base Miami Beach is composed of multiple U.S. Coast Guard (USCG) units, both land and waterside. The facility has one of the highest operational tempos in the USCG for both routine and emergency operations. The amendment to the regulations is necessary to enhance the USCG's ability to secure their shoreline to counter postulated threats against their personnel, equipment, cutters and facilities by providing stand-off corridors encompassing the waters immediately contiguous to Base Miami Beach. The amendment will also serve to protect the general public from injury or property damage during routine and emergency USCG operations and provide an explosive safety arc buffer during periodic transfer of ammunitions between units, including cutters.

**DATES:** Written comments must be submitted on or before June 4, 2012.

**ADDRESSES:** You may submit comments, identified by docket number COE-2012-0009, by any of the following methods: