HOSPITAL MORTGAGE INSURANCE PROGRAM

SECTION 242 OF THE NATIONAL HOUSING ACT

APPLICANT'S GUIDE

PRE-APPLICATION

OFFICE OF HOSPITAL FACILITIES
FEBRUARY 2014

Note:

This document is designed to be printed double-sided.

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Contents within asterisks have been changed in 4165.1 REV-1, CHG-1, 2/7/14

INTRODUCTION

Section 242 of the National Housing Act enables the affordable financing of hospital projects by reducing the cost of capital and significantly enhancing the credit of hospitals that qualify for mortgage insurance. The program improves access to quality health care, reduces the cost of hospital care, supports HUD's community development mission, and contributes revenues to the General Insurance Fund. Currently, hospitals in HUD's Section 242 portfolio range from small rural facilities to some of the nation's top urban teaching hospitals.

Through the Section 242 program, lenders may apply for hospital mortgage insurance, supplemental loans, or refinancing. However, potential applicants are asked to first contact HUD and submit pre-application materials for preliminary review before proceeding to the application stage. Because of the comprehensive nature of the application and the rigor of qualifications required by the Section 242 program, HUD performs an analysis of pre-application materials to determine whether or not potential mortgagors meet the minimum criteria for HUD Section 242 Mortgage Insurance.

Passing this preliminary phase does not assure that an application will be approved; however, the pre-application process enables HUD to determine minimum eligibility requirements before a hospital and its lender commit substantial time, expense, and effort to prepare a complete application.

When reviewing applications for mortgage insurance, HUD's main objectives are to evaluate the need, financial feasibility, and risk of proposed hospital projects. When deciding whether or not to approve a loan, HUD considers a large number of factors, and expects complete applications to contain sufficient information and supporting data to enable informed decisions.

ABOUT THE OFFICE OF HOSPITAL FACILITIES

The Office of Hospital Facilities (OHF) is an office within the Office of Healthcare Programs (OHP) that handles the national operations of the Section 242 Mortgage Insurance Program for Hospitals. The office is centralized in HUD Headquarters in Washington, DC, and performs day-to-day program operations with support from the Office of Architecture and Engineering (OAE). HUD field offices assist OHF in performing loan closings.

The Director of the OHF is responsible for overall program management of the Section 242 Program. The Director oversees the development of Section 242 program policies and procedures, as well as two Divisions that handle underwriting and asset management, respectively.

PRE-APPLICATION PROCESS CHECKLIST

As mentioned in the Introduction to this guide, the purpose of the Preliminary Review is to identify any obvious factors that would cause an application to be rejected, before a hospital and its lender expend the resources needed to prepare an application and before HUD expends resources to review it. The Preliminary Review focuses on statutory eligibility, market need, financial strength, and any other known factors that have the potential to cause an application to be rejected. HUD performs this review at no cost to the lender.

If HUD's review identifies no problems, the next step in the process is a Pre-Application Meeting. The Pre-Application Meeting is an opportunity for the potential mortgagee and mortgagor to summarize the proposed project, for HUD to summarize the application process, and for issues that could affect the eligibility or underwriting of the proposed loan to be identified and discussed.

Following the meeting, HUD may (1) invite the lender to submit an application or (2) identify issues that must be resolved before a full application will be accepted for processing. HUD's participation in a Pre-Application Meeting should in no way be construed as an indication that a subsequent application will be approved.

If HUD does not receive a complete application within one year following the date of the preliminary review letter, another Preliminary Review may be required, at HUD's discretion, before the application process may proceed.

The checklist on the following pages presents the pre-application steps from initial contact through Preliminary Review and Pre-Application Meeting to the submission of the application. It is in a step-by-step format that can be used as a planning tool by both the lender and HUD.

SECTION 242 HOSPITAL MORTGAGE INSURANCE
PRE-APPLICATION PROCESS CHECKLIST

HOSPITAL/CONTACT/PHONE: ______________________________

MORTGAGE BANK/CONTACT/PHONE: ______________________________

HUD ACCOUNT EXECUTIVE/PHONE: ______________________________

ACTION OFFICE	TRIGGER	ACTION	INFORMATION NEEDED TO COMPLETE THIS STEP	DATE ACTION PLANNED & COMPLETED
Potential Applicant (Banker) or Hospital		Contact HUD about possibility of FHA financing. (Note: If the hospital is already a HUD client, all preliminary steps will normally be handled by the client's Account Executive.)	• Hospital name and location • General project description	
HUD	Initial inquiry	Provide program information verbally, by referring to web page, and by sending additional materials. Obtain project information by phone or e-mail; if hospital is clearly not a Section 242 candidate, explain why.	During initial contact, HUD should try to understand the project and evaluate the hospital and project against key minimum eligibility requirements described in the Preliminary Review Templates in this Appendix.	
HUD	Initial contact indicates hospital may be a candidate for Section 242 financing	Request preliminary information. If initial contact was with a hospital, encourage hospital to retain a mortgage lender as a first step. Refer hospital to consult the list of active Section 242 lenders posted on the HUD website.	Direct the applicant to: • Preliminary Review Template • Applicant Data Request (Excel file)	
Applicant	HUD requests preliminary information	Provide preliminary information to HUD as defined within the Preliminary Review Template in the Applicant's Guide.	Completed Preliminary Review Template with Required Attachments	
HUD	Receipt of preliminary information from applicant	Perform review of submitted materials	Preliminary review materials submitted by applicant.	

ACTION OFFICE	TRIGGER	ACTION	INFORMATION NEEDED TO COMPLETE THIS STEP	DATE ACTION PLANNED & COMPLETED
HUD	Review of applicant's preliminary review submission	If information was missing from the submission, or if the information requires clarification, HUD will request this from the applicant.		
Applicant	Request for information from HUD	Applicant responds to HUD's questions.		
HUD	Applicant's response to follow-up questions received by HUD	HUD completes preliminary review.		
HUD	*Negative* outcome of preliminary review	If serious issues are identified in preliminary review, HUD informs applicant. Possible outcomes: • Hospital is determined not to be a candidate for Section 242 • Hospital is informed of actions needed to resolve issues (may range from obtaining additional information to waiting a year for financial performance to improve).		
HUD	*Positive* outcome of preliminary review	If all indications are positive, or if only manageable issues remain from the preliminary review, HUD informs applicant of the positive result in the Preliminary Review Letter. The letter includes potential credit and/or eligibility issues that need to be addressed at the Pre-Application Meeting. An Account Executive (AE) and Client Service Team (CST) are designated.		
HUD & Applicant	Notification from HUD that minimum criteria are met	Schedule Pre-Application Meeting.	List of Pre-Application Meeting participants	

ACTION OFFICE	TRIGGER	ACTION	INFORMATION NEEDED TO COMPLETE THIS STEP	DATE ACTION PLANNED & COMPLETED
HUD & Applicant	Pre-Application Meeting scheduled	Conduct Pre-Application Meeting.	Topics to be covered include, but are not limited to: • Issues identified in the Preliminary Review Letter • Hospital Overview • Project Description • Legal Matters • Architectural and Engineering Matters • Project and Financing timeline • Environmental Review • Application Process and Timing	
HUD	Pre-Application Meeting completed	HUD decides whether and on what conditions to invite an application. In uncomplicated cases, the decision is communicated by phone shortly after the meeting. A letter follows the phone call, and (if positive) lists additional credit and/or eligibility concerns that need to be addressed during the application review process. If negative, the letter explains why the applicant is not invited to apply.		
Applicant	Application invited by HUD*	Decide whether and on what schedule to proceed with application; notify HUD of target date for submission of complete application.		
Applicant	Decision to proceed with application	Prepare all application materials called for in Applicant's Guide and in accordance with technical requirements in Handbook. Update AE on progress against schedule, monthly or as changes occur. Bring issues or questions to AE as they arise. Bring design issues and questions to assigned OAE representative and AE.		

ACTION OFFICE	TRIGGER	ACTION	INFORMATION NEEDED TO COMPLETE THIS STEP	DATE ACTION PLANNED & COMPLETED
HUD	Notification that applicant is preparing application	Provide technical assistance to applicant as application is prepared; provide documented responses applicant can rely on.		
Applicant	Application completed	Send application to HUD as directed by AE and application submission instructions included with the letter that followed the Pre-Application Meeting.		

*Applicant can submit an application without invitation. However, resolution of all preliminary issues before applying is strongly recommended.

REQUIRED DOCUMENTATION FOR A PRELIMINARY REVIEW
SECTION 242 MORTGAGE INSURANCE

HOSPITAL:	**Name:** **Address:**
FHA APPROVED LENDER:	**Name:** **Firm:** **Address:** **Email:** **Telephone Number:**

This Preliminary Review Template has been prepared for use by hospitals and mortgage lenders interested in applying for Section 242 mortgage insurance. Information submitted will be used by Office of Hospital Facilities (OHF) staff to perform an initial review of a hospital's qualifications under the Section 242 Program. If you are applying for Section 241 or 242/223(f) mortgage insurance, please use the corresponding template prepared for those specific programs.

OHF performs a Preliminary Review to evaluate hospitals and proposed projects against OHF's minimum eligibility criteria and to identify any obvious factors that would cause an application to be rejected, before the applicant expends resources to prepare an application. The Section 242 Preliminary Review focuses on statutory eligibility, market need, financial strength, and any other known factors that have the potential to cause an application to be rejected.

A complete submission includes this completed Preliminary Review Template and the items described in the List of Attachments. Please keep your responses on the Preliminary Review Template brief, and provide more detailed information in the Attachments. Once complete, submit an electronic copy of the package (via email) and two hard copies to OHF. Submit complete packages, including the email copy, to:

Underwriting Division Director
Office of Hospital Facilities
Department of Housing and Urban Development
451 7th Street SW, Room 2247
Washington, DC 20410
hospitals@hud.gov

If you have questions concerning this form or the attachments, please contact HUD at (202) 708-0599 or hospitals@hud.gov, attn: Underwriting Division Director, OHF. Additional information can also be found on the OHF website at www.hud.gov/healthcare.

SECTION 242 PRELIMINARY REVIEW TEMPLATE

A. PROVIDE A BRIEF DESCRIPTION OF THE FOLLOWING (LIMIT RESPONSE TO ONE PAGE):

- The Hospital
- The Project
- Service Area and Competition

A completed Draft Application for Hospital Project Mortgage Insurance form (HUD Form 92013) should be provided.

As part of your response, please note the total square footage of the (1) existing hospital, (2) the renovated/replaced/new hospital following project completion, and (3) major off-site facilities (medical office buildings, clinics, etc).

B. CLEARLY DESCRIBE THE OWNERSHIP STRUCTURE OF THE HOSPITAL

The description of the ownership structure should include, but not necessarily be limited to, the following: affiliates, subsidiaries, corporate parent, and other entities listed on the consolidated audited financial statements.

List and describe the assets (real estate, operations, and organizations) which will be included as collateral for the proposed mortgage. The assets should include those necessary to operate the hospital, including off-site properties (such as clinics and MOBs), as well as other major assets. OHF generally does not entertain asset exclusions from proposed mortgages; however, the subject is open to discussion. If exclusions are proposed, describe the assets you propose to exclude (the name of the legal entities, if applicable), list the net book value of the assets, and discuss why those assets should be excluded.

C. SECTION 242 STATUTORY ELIGIBILITY CRITERIA

Patient Day Rule

Section 242 is designed for acute care hospitals. OHF uses the patient day calculation to determine whether the hospital is an acute care facility. If more than 50 percent of the hospital's patient days are in ineligible categories (described below), the hospital will not qualify for the Section 242 Program.

Patient days assignable to chronic convalescent and rest, drug and alcoholic, epileptic, mentally deficient, mental, nervous and mental, and/or tuberculosis are **ineligible** patient days. Included in the **ineligible** patient day category are patient days attributable to skilled nursing, intermediate care, convalescent care, rehabilitation, and psychiatric care.

Please state whether the hospital meets the patient day rule and provide your calculations.

For Hospitals that provide a significant level of outpatient services, OHF allows applicants to use an adjusted patient day calculation to determine eligibility. See Handbook 4615.1 APPENDIX 1 for details.

Loan-to-Value Requirement (LTV)

Hospitals must demonstrate no more than a 90 percent LTV ratio to be eligible for FHA mortgage insurance.

Calculate LTV based on the proposed project costs from the HUD Form 92013. LTV is calculated using the formula below. Also included is guidance for calculating Net PPE, a component of Total Estimated Replacement Cost.

LTV = (Total Mortgage Amount) / (Total Estimated Replacement Cost)

Total Mortgage Amount – From Section D, Line 8 of Form 92013

Total Estimated Replacement Cost – From Section C, Line 32 of Form 92013.

Net PPE – From Section C, Line 30 of Form 92013 (based upon the book value of the mortgagor’s property, plant, and equipment from its latest financial audit. Net PPE should not include equipment secured by leases nor real estate or other property that will be excluded from the collateral). If the value of the hospital’s Net PPE is projected to be written-down following construction (common with replacement facilities in rural communities, the Net PPE should be reduced by the total amount to be written-down. If portions of the facility will be demolished, please also subtract the approximate book value of that portion of the property from the calculation. OHF uses the residual value when calculating LTV.

Please note that if the hospital does not own its property in fee simple, and is only able to grant the lender a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV.

- If the hospital maintains a 99-year lease on the property, or maintains a 50-year lease with the option to renew for at least 49 years, the value is discounted by 5 percent
- If the hospital maintains a lease of 50 years or greater, but does not meet the requirement above, the value is discounted by 90 percent
- If a hospital maintains a lease of less than 50 years, the project is not eligible

LTV may also be met by providing an appraisal of the property to be mortgaged prepared by a qualified health care appraiser, approved by HUD and licensed in the State in which the hospital is located. The appraisal must be prepared in accordance with OHF guidelines. Please contact the OHF Underwriting Division Director for details.

D. EQUITY CONTRIBUTION AND WORKING CAPITAL

Hospitals must have sufficient days cash on hand to make any required cash equity contribution at the closing of a Section 242 loan and to maintain sufficient working capital to operate post-closing. If an equity contribution is needed to meet LTV, or if the hospital plans to provide additional equity to support the project, please note the source of the contribution. Describe how much unrestricted cash and investments the Hospital maintains, and its current levels of working capital.

E. START-UP HOSPITALS

OHF requires that start-up hospitals and their sponsors demonstrate that the project has sufficient start-up capital, fills a market need, and has a viable physician recruitment plan. If this proposal is for a start-up hospital, please complete the "Start-Up Hospital Preliminary Review Report Supplement" in addition to this Preliminary Review Template. Please contact the OHF Underwriting Division Director for details.

F. MINIMUM FINANCIAL CRITERIA

Minimum Requirement for the Aggregate Operating Margin

Hospitals with an aggregate operating margin of greater than 0.00 percent, when calculated from the three most recent audited financial statements, are eligible for Section 242 mortgage insurance. The formula for the aggregate operating margin is below:

$$\frac{\textbf{Operating Income (Year 1) + Operating Income (Year 2) + Operating Income (Year 3)}}{\textbf{Total Operating Revenue (Year 1) + Total Operating Revenue (Year 2) + Total Operating Revenue (Year 3)}}$$

Operating revenue is the revenue from the core patient care operations of the hospital. It includes revenues from the provision of patient care, transfers from temporarily restricted accounts that are used for current operating expenses, and patient-related activities such as the operation of the cafeteria and parking facilities. OHF's calculation of *operating revenue* excludes sources of revenue (contributions, grants, and investment income) that are not reliable sources of future revenue. *Operating income* equals *operating revenue* minus *operating expenses*.

Please provide your calculations of the operating margin for the last three completed fiscal years, below. Also include the calculation of the aggregate operating margin. The calculations should exclude the operations of affiliates/subsidiaries/business lines that will not be collateral for the insured mortgage.

Aggregate operating margin for last 3 years $\geq$ 0.0

	FY 20__	FY 20__	FY 20__	Aggregate
Operating Margin				

If the hospital does not meet the Operating Margin criterion, but has undergone a financial turnaround that has resulted in a positive operating margin in the most recent year, the hospital may be eligible for Section 242 mortgage insurance. This exception to the Operating Margin criterion requires that the hospital demonstrate a positive operating margin in the most recent year (as demonstrated in the audited financial statements) at the time of application and that the hospital demonstrate two years of positive operations (as demonstrated by two audits) at the time of OHF's commitment to insure. Please contact the OHF Underwriting Division Director for more details.

Note: Start-Up Hospitals are not subject to the Operating Margin criterion.

Minimum Requirement for the Debt Service Coverage Ratio

Hospitals with an average debt service coverage ratio above 1.25, calculated from the three most recent audited financial statements, are eligible for Section 242 mortgage insurance. The formula for the debt service coverage ratio is below:

$$\frac{\textbf{(Excess of Revenues Over Expenses) + Interest Expense + Depreciation Expense + Amortization Expense}}{\textbf{Current Portion of Long-Term Debt (Prior Year, Including Capital Leases) + Interest Expense}}$$

The debt service coverage ratio (DSC) is based upon the hospital's "excess of revenues over expenses" (or in the case of for-profit organizations, "net income") as it appears in the hospital's audited financial statements. Please provide the average DSC ratio for the last three completed fiscal years in the space provided.

Average DSC for last 3 years $\geq$ 1.25

	FY 20__	FY 20__	FY 20__	Average
DSC				

When the hospital's proposal includes refinancing existing debt with proceeds from the Section 242 loan, OHF may use (at its discretion) an estimate of projected interest rate(s) in lieu of the historical interest rate(s) when calculating the DSC ratio for prior periods. In cases where the projected interest rate is used, the hospital must demonstrate a 1.4x debt service coverage ratio.

If the hospital does not meet the DSC criterion, but has undergone a financial turnaround that has resulted in a debt service coverage ratio of 1.4x in the most recent year, the hospital may be eligible for Section 242 mortgage insurance. This exception to the DSC criterion requires that the hospital demonstrate a debt service coverage ratio of 1.4x in the most recent year (as demonstrated in the audited financial statements) at the time of application. Please contact the OHF Underwriting Division Director for more details.

Note: Start-Up Hospitals are not subject to the DSC criterion.

State and Local Government Support / Tax Support

If the hospital is the recipient of tax revenues, revenues from state-wide hospital assessments, or appropriations (common for critical access hospitals and safety net facilities), please describe the nature, authority, and future reliability of the support. Identify and describe the statutes, legislation, or referenda that created the support.

If the revenue is provided by an assessment program or appropriation, please list historical net receipts (last five years) and future anticipated receipts. Is the revenue guaranteed to be delivered to the hospital by state law? If the support is set to expire, or is expected to be renewed, please indicate so. Please describe the future reliability of the revenue source.

If the revenue is tax support, under what circumstances could the tax support be revoked? What action would be required to revoke or diminish the support? What entity collects the tax? Are there restrictions on the use of tax proceeds? Please describe community support for the tax including (if appropriate) election results. Has the tax support recently been renewed, or will it be renewed, by referendum, contract, resolution, or other action by the hospital or local agency? Will the tax automatically "sunset"? Is there any indication that the support may be reduced or discontinued?

G. COMPLIANCE WITH STATE AND FEDERAL STATUTES AND REGULATIONS

In order to be eligible for the Section 242 Program, the hospital must be in substantial compliance with federal and state regulations governing the operation and reimbursement of hospitals. Is the Hospital under investigation by any state or federal agency for statutory or regulatory violations?

H. REFINANCING COMPONENT

Purpose and Nature of the Debt

If there is a refinancing component to the project, please answer the following questions and provide the information requested about each debt issue to be refinanced:

1) Indicate the unpaid principal balance of each issue to be refinanced and the interest rate(s) on the debt. Include the total outstanding balance of the debt in Section D, Line 2 (Land Indebtedness) of Form 92013.

2) Please describe the nature of the debt (i.e. variable or fixed rate, taxable or tax-exempt, maturity date, prepayment or termination costs). Please describe any special characteristics of the debt (for example, the use of swaps).

3) Please provide the Official Statement(s) for the debt issue(s) (or other information that documents the sources and uses of funds, and the project description) to be refinanced.

   If the issue(s) included a refinancing component as a use of funds, please provide the Official Statement (or other documentation) for the original issue that was refinanced. In order to refinance debt with mortgage proceeds, the original issuance of the debt must be tied to the acquisition, construction, or rehabilitation of a capital asset.

4) When was construction on the capital project(s) funded with proceeds from the debt issuance completed? Debt associated with structures completed fewer than two years prior to submission of the Section 242 application is not eligible to be refinanced.

Limit on Refinancing

The construction component of the project must total 20 percent of the mortgage amount or greater. The amount from Section C, Line 11 of Form 92013 must be greater than or equal to 20 percent of the mortgage amount. Of the amount from Section C, Line 11 of Form 92013, up to one-half (50%) may be for the cost of new equipment.

If the construction component is less than 20 percent of the mortgage amount, the project may still qualify for Section 242/223(f) mortgage insurance. Please contact the OHF Underwriting Division Director for more information.

I. PHYSICIAN OWNERSHIP

If physician ownership is present, please describe. Physician-owned facilities must comply with the Federal Physician Self-Referral Prohibition laws and anti-kickback prohibitions (including updated rules concerning physician ownership in the Patient Protection and Affordable Care Act). Experienced hospital counsel will be required to provide an acceptable legal opinion as to compliance with the aforementioned rules. In addition, investor-owned hospitals are reviewed for their impact on existing healthcare providers, particularly those providing uncompensated care.

J. FIRST LIEN

Is the hospital able to grant a first lien on hospital property, plant, equipment, and receivables to its FHA lender? OHF requires that the lender have a first lien position on property, plant, equipment, receivables, and revenues.

Please address the following four questions:

1) Is all of the hospital's real estate owned in fee simple? If the hospital is only able to grant a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV. Please see Section C.

2) Does local government allow the lender to have a first mortgage lien on the property?
3) Does the hospital have a current or planned receivables financing program?
4) Are there other challenges that prevent the hospital from granting a first lien on its property, plant, equipment, receivables and/or revenue?

K. COMMENCEMENT OF CONSTRUCTION

OHF limits the amount of site preparation performed prior to submission of a Section 242 application. Indicate whether site preparation or other construction has begun, or is planned to begin, prior to application submission.

L. STATE CERTIFICATE OF NEED APPLICATION STATUS

In order to be eligible for Section 242 mortgage insurance, state Certificate of Need (CON) requirements must be met. Does the project require a CON? If so, has the application process begun? Describe the current status of the process and indicate the expected date of CON approval.

M. MORTGAGE ORIGINATOR

Please identify the mortgage originator and note the experience of the firm and individual representing the firm with the Section 242 program. Please note attendance at Section 242 Training sessions and the number of applications submitted within the past three years. If the hospital has not selected a firm, OHF can provide a list of originators who are active in the program.

LIST OF ATTACHMENTS

Please include the following attachments with the submission:

Attachment 1: Provide a draft HUD Form 92013.

Attachment 2: Include a chart showing the organizational structure (include the hospital, all affiliates, subsidiaries, and parent organizations). On the chart, note what real estate, operations, and organizations will and will not be included as collateral for the proposed mortgage.

Attachment 3: Provide the hospital's utilization statistics for the three most recent, completed fiscal years, and the interim period for the current fiscal year. Using the data for the most recently completed fiscal year, include a worksheet showing a detailed breakdown of patient days, and the calculations of the patient day rule. If the project will change the hospital's patient day distribution (for example, if a skilled nursing facility is to be added to the hospital as part of the project), then the patient day rule calculation should be made based upon this change.

Attachment 4: Provide a worksheet showing the calculation of LTV. Please provide a separate schedule listing the assets (and corresponding book values) of the property, plant, and equipment that will be secured under the proposed mortgage. These values should be entered in Section C, Lines 30 and 31 of Form 92013. When providing an estimate for Net PPE, please exclude property, plant or equipment not included as collateral in the proposed mortgage, such as equipment secured by other lenders (e.g., equipment under lease).

Attachment 5: Provide copies of the audited financial statements for the last five years, and interim financial statements for the most recent interim period (as well as data for the prior year's interim period, for comparative purposes). Provide both consolidated and consolidating financial statements, if applicable. If the hospital is the recipient of tax revenues, please provide the legal documents (statutes, referenda, etc.) authorizing or describing the tax.

Attachment 6: Provide in a separate worksheet the calculation of the historical aggregate operating margin and the historical average debt service coverage ratio. Provide details of calculations. Please include on a separate schedule a breakdown of "other operating revenue" for each of the last three complete fiscal years (and for the most recent interim period). "Other operating revenue" is typically reported following Net Patient Service Revenue in the audited financial statements.

<u>Attachment 7</u>: If there is a refinancing component to the project, please provide the Official Statements or other information that documents the sources/uses of funds and project descriptions for the prior issues.

<u>Attachment 8</u>: Provide an electronic copy of the completed Applicant Data Request. Please carefully review the instructions and submit a complete response. The Applicant Data Request (an excel document) may be found on the OHF website.

REQUIRED DOCUMENTATION FOR A PRELIMINARY REVIEW
SECTION 241 MORTGAGE INSURANCE

HOSPITAL: **Name:**
Address:

FHA APPROVED LENDER: **Name:**
Firm:
Address:
Email:
Telephone Number:

This Preliminary Review Template has been prepared for use by hospitals and mortgage lenders interested in applying for Section 241 mortgage insurance. Information submitted will be used by Office of Hospital Facilities (OHF) staff to perform an initial review of a hospital's qualifications under the Section 241 Program. If you are applying for Section 242 or 242/223(f) mortgage insurance, please use the corresponding template prepared for those specific programs.

OHF performs a Preliminary Review to evaluate hospitals and proposed projects against OHF's minimum eligibility criteria and to identify any obvious factors that would cause an application to be rejected, before the applicant expends resources to prepare an application. The Section 241 Preliminary Review focuses on financial strength and any other known factors that have the potential to cause an application to be rejected.

A complete submission includes this completed Preliminary Review Template and the items described in the List of Attachments. Please keep your responses on the Preliminary Review Template brief, and provide more detailed information in the Attachments. Once complete, submit an electronic copy of the package (via email) and two hard copies to OHF. Submit complete packages, including the email copy, to:

Underwriting Division Director
Office of Hospital Facilities
Department of Housing and Urban Development
451 7th Street SW, Room 2247
Washington, DC 20410
hospitals @hud.gov

If you have questions concerning this form or the attachments, please contact HUD at (202) 708-0599 or hospitals@hud.gov, attn: Underwriting Division Director, OHF. Additional information can also be found on the OHF website at www.hud.gov/healthcare.

SECTION 241 PRELIMINARY REVIEW TEMPLATE

A. PROVIDE A BRIEF DESCRIPTION OF THE PROPOSED PROJECT:

A completed Draft Application for Hospital Project Mortgage Insurance form (HUD Form 92013) should be provided.

As part of your response, please note the total square footage of the (1) existing hospital, (2) the renovated/replaced/new hospital following project completion, and (3) major off-site facilities (medical office buildings, clinics, etc).

B. CLEARLY DESCRIBE THE OWNERSHIP STRUCTURE OF THE HOSPITAL

The description of the ownership structure should include, but not necessarily be limited to, the following: affiliates, subsidiaries, corporate parent, and other entities listed on the consolidated audited financial statements. A chart or graph showing the ownership structure should also be provided.

List and describe the assets (real estate, operations, and organizations) which are included as collateral for the existing mortgage(s). List and describe the assets that are currently excluded. Include the net book value of those assets. Discuss any changes proposed as part of the new proposal.

C. STATUTORY ELIGIBILITY CRITERIA

Patient Day Rule

The program is designed for acute care hospitals. OHF uses the patient day calculation to determine whether the hospital is an acute care facility. If more than 50 percent of the hospital's patient days are in ineligible categories (described below), the hospital will not qualify for the Section 242 Program.

Patient days assignable to chronic convalescent and rest, drug and alcoholic, epileptic, mentally deficient, mental, nervous and mental, and/or tuberculosis are **ineligible** patient days. Included in the **ineligible** patient day category are patient days attributable to skilled nursing, intermediate care, convalescent care, rehabilitation, and psychiatric care.

For hospitals that provide a significant level of outpatient services, OHF allows applicants to use an adjusted patient day calculation to determine eligibility. Please see Handbook 4615.1 APPENDIX 1 for details.

If the hospital originally qualified for Section 242 financing based on the patient day exemption for critical access hospitals, then it does not need to demonstrate compliance with the patient day rule to qualify for a Section 241 financing.

Loan-to-Value Requirement (LTV)

Hospitals must demonstrate no more than a 90 percent LTV ratio to be eligible.

Calculate LTV based on the proposed project costs from the HUD Form 92013. LTV is calculated using the formula below:

LTV = (Total Mortgage Amount(s) / (Total Estimated Replacement Cost)

Total Mortgage Amount – Includes the amount of the proposed mortgage (from Section D, Line 8 of Form 92013), plus the unpaid principal balance of the hospital's existing Section 242 and 241 mortgages.

Total Estimated Replacement Cost – From Section C, Line 32 of Form 92013.

Net PPE (used in the calculation of Total Estimated Replacement Cost) – From Section C, Line 30 of Form 92013 (based upon the book value of the mortgagor's property, plant, and equipment in its latest financial audit. Net PPE should not include equipment secured by leases nor real estate or other property that is excluded from the collateral). If the value of the hospital's Net PPE is projected to be written-down following construction, the Net PPE should be reduced by the total amount to be written-down. If portions of the facility will be demolished, please also subtract the approximate book value of that portion of the property from the calculation. OHF uses the residual value when calculating LTV.

Section 241 mortgage amounts, when added to the unpaid principal balance of the outstanding indebtedness relating to the property, may not exceed 90 percent of the estimated replacement cost of the property following completion of the Section 241 project.

Please note that if the hospital does not own its property in fee simple, and is only able to grant the lender a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV.

- If the hospital maintains a 99-year lease on the property, or maintains a 50-year lease with the option to renew for at least 49 years, the value is discounted by 5 percent
- If the hospital maintains a lease of 50 years or greater, but does not meet the requirement above, the value is discounted by 90 percent
- If a hospital maintains a lease of less than 50 years, the project is not eligible

LTV may also be met by providing an appraisal of the property to be mortgaged prepared by a qualified health care appraiser, approved by HUD and licensed in the State in which the hospital is located. The appraisal must be prepared in accordance with OHF guidelines. Please contact OHF's Underwriting Division Director for details.

D. EQUITY CONTRIBUTION AND WORKING CAPITAL

Hospitals must have sufficient days cash on hand to make the required cash equity contribution at the closing of a Section 241 loan and to maintain sufficient working capital to operate post-closing. *Section 241 mortgage amounts, when added to the unpaid principal balance of the outstanding indebtedness relating to the property, may not exceed 90 percent of the estimated replacement cost of the property following completion of the Section 241 project.*

Your Account Executive will evaluate the hospital's current cash position in order to determine whether the hospital maintains sufficient cash on hand to meet OHF's underwriting guidelines. Please provide any information you consider helpful in this analysis.

E. MINIMUM FINANCIAL CRITERIA

Minimum Requirement for the Aggregate Operating Margin and Average Debt Service Coverage Ratio.

Hospitals with an aggregate operating margin of greater than 0.00 percent and an average debt service coverage ratio of 1.25x, when calculated from the three most recent audited financial statements, are eligible for Section 241 mortgage insurance.

Your Account Executive will use data that the hospital has provided as part of its ongoing reporting requirements for its existing mortgages in order to calculate these minimum financial criteria.

State and Local Government Support / Tax Support

If the hospital is the recipient of tax revenues, revenues from irregular state-wide hospital assessments, or appropriations (common for critical access hospitals and safety net facilities), please describe the nature, authority, and future reliability of the support. Identify and describe the statutes, legislation, or referenda that created the support.

If the revenue is provided by an assessment program or appropriation, please list historical net receipts (last five years) and future anticipated receipts. Is the revenue guaranteed to be delivered to the hospital by state law? If the support is set to expire, or is expected to be renewed, please indicate so. Please describe the future reliability of the revenue source.

If the support is tax support, under what circumstances could the tax support be revoked? What action would be required to revoke or diminish the support? What entity collects the tax? Are there restrictions on the use of tax proceeds? Please describe community support for the tax including (if appropriate) election results. Has the tax support recently been renewed, or will it be renewed, by referendum, contract, resolution, or other action by the hospital or local agency? Will the tax automatically "sunset"? Is there any indication that the support may be reduced or discontinued?

F. COMPLIANCE WITH STATE AND FEDERAL STATUTES AND REGULATIONS

In order to be eligible for the Section 241 Program, the hospital must be in substantial compliance with federal and state regulations governing the operation and reimbursement of hospitals. Is the hospital under investigation by any state or federal agency for statutory or regulatory violations?

G. REFINANCING COMPONENT

In rare circumstances Section 241 loans may include debt refinancing. If this is the case, please contact your Account Executive for program requirements.

H. COMPLIANCE WITH EXISTING REGULATORY AGREEMENT(S), AND FINAL ENDORSEMENT OF PRIOR MORTGAGE(S)

Is the hospital in compliance with its existing Regulatory Agreement and Rider to the Regulatory Agreement? Hospitals must also be willing to accept the most recent version of OHF's standard covenants in order to be eligible for Section 241 mortgage insurance.

Have the hospital's existing mortgages reached final endorsement? Hospitals must meet final endorsement requirements on existing loans in order to initially endorse a new loan.

I. PHYSICAN OWNERSHIP

If physician ownership is present, please describe. Physician-owned facilities must comply with the Federal Physician Self-Referral Prohibition laws and anti-kickback prohibitions (including updated rules concerning physician ownership in the Patient Protection and Affordable Care Act). Experienced hospital counsel will be required to provide an acceptable legal opinion as to compliance with the aforementioned rules. In addition, investor-owned hospitals are reviewed for their impact on existing healthcare providers, particularly those providing uncompensated care.

J. FIRST LIEN

Is the hospital able to grant a first lien on hospital property, plant, equipment, and receivables to its FHA lender? OHF requires that the lender have a first lien position on property, plant, equipment, receivables, and revenues. If the hospital is only able to grant a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV. Please see Section C.

K. COMMENCEMENT OF CONSTRUCTION

OHF limits the amount of site preparation performed prior to submission of a Section 241 application. Indicate whether site preparation or other construction has begun, or is planned to begin, prior to application submission.

L. STATE CERTIFICATE OF NEED APPLICATION STATUS

In order to be eligible for Section 241 mortgage insurance, state Certificate of Need (CON) requirements must be met. Does the project require a CON? If so, has the application process begun? Describe the current status of the process and indicate the expected date of CON approval.

M. MORTGAGE ORIGINATOR

Please identify the mortgage originator and note the experience of the firm and individual representing the firm with the Section 242 program. Please note attendance at Section 242 Training sessions and the number of applications submitted within the past three years. If the hospital has not selected a firm, OHF can provide a list of originators who are active in the program.

LIST OF ATTACHMENTS

Please include the following attachments with the submission:

Attachment 1: Provide a draft HUD Form 92013.

Attachment 2: Include a chart showing the organizational structure (include the hospital, all affiliates, subsidiaries, and parent organizations). On the chart, note what real estate, operations, and organizations will and will not be included as collateral for the proposed mortgage.

Attachment 3: Provide the hospital's utilization statistics for the three most recent, completed fiscal years, and the interim period for the current fiscal year. Using the data for the most recently completed fiscal year, include a worksheet showing a detailed breakdown of patient days, and the calculations of the patient day rule. If the proposed project will change the existing mortgagor's patient day distribution (for example, if a skilled nursing facility is added to the mortgagor), then the patient day rule calculation should be made based upon this change.

Attachment 4: Provide a worksheet showing the calculation of LTV. Please provide a separate schedule listing the assets (and corresponding book values) of the property, plant, and equipment that will be secured under the proposed mortgage. These values should be entered in Section C, Lines 30 and 31 of Form 92013. When providing an estimate for Net PPE, please exclude property, plant or equipment not included as collateral in the proposed mortgage, such as equipment secured by other lenders (e.g., equipment under lease).

Attachment 5: Provide a certification from the hospital's Chief Financial Officer that the hospital is in compliance with its existing Regulatory Agreement and Rider to the Regulatory Agreement.

Attachment 6: Provide an electronic copy of the completed Applicant Data Request. Please carefully review the instructions and submit a complete response. The Applicant Data Request (an excel document) may be found on the OHF website.

REQUIRED DOCUMENTATION FOR A PRELIMINARY REVIEW
SECTION 242/223(F) MORTGAGE INSURANCE

HOSPITAL:	**Name:** **Address:**
FHA APPROVED LENDER:	**Name:** **Firm:** **Address:** **Email:** **Telephone Number:**

This Preliminary Review Template has been prepared for use by hospitals and mortgage lenders interested in applying for Section 242/223(f) mortgage insurance. Information submitted will be used by Office of Hospital Facilities (OHF) staff to perform an initial review of a hospital's qualifications under the Section 242/223(f) Program. If you are applying for Section 241 or 242 mortgage insurance, please use the corresponding template prepared for those specific programs.

OHF performs a Preliminary Review to evaluate hospitals and proposed projects against OHF's minimum eligibility criteria and to identify any obvious factors that would cause an application to be rejected, before the applicant expends resources to prepare an application. The Section 242/223(f) Preliminary Review focuses on statutory and regulatory eligibility, market need, financial strength, and any other known factors that have the potential to cause an application to be rejected.

A complete submission includes this completed Preliminary Review Template and the items described in the List of Attachments. Please keep your responses on the Preliminary Review Template brief, and provide more detailed information in the Attachments. Once complete, submit an electronic copy of the package (via email) and two hard copies to OHF. Submit complete packages, including the email copy, to:

Underwriting Division Director
Office of Hospital Facilities
Department of Housing and Urban Development
451 7th Street SW, Room 2247
Washington, DC 20410
hospitals@hud.gov

If you have questions concerning this form or the attachments, please contact HUD at (202) 708-0599 or hospitals@hud.gov, attn: Underwriting Division Director, OHF. Additional information can also be found on the OHF website at www.hud.gov/healthcare.

SECTION 242/223(F) PRELIMINARY REVIEW TEMPLATE

A. PROVIDE A BRIEF DESCRIPTION OF THE FOLLOWING (LIMIT RESPONSE TO ONE PAGE):

- The Hospital
- The Project and/or the Acquisition (if applicable)
- Service Area
- Competition

A completed Draft Application for Hospital Project Mortgage Insurance form (HUD Form 92013) should be provided. The outstanding debt to be refinanced should be included in Section D, Line 2 of Form 92013.

As part of your response, please note the total square footage of the (1) existing hospital, (2) the renovated/replaced/new hospital following project completion, and (3) off-site facilities (medical office buildings, clinics, etc).

B. CLEARLY DESCRIBE THE OWNERSHIP STRUCTURE OF THE HOSPITAL

The description of the ownership structure should include, but not necessarily be limited to, the following: affiliates, subsidiaries, corporate parent, and other entities listed on the consolidated audited financial statements. A chart or graph showing the ownership structure should also be provided.

List and describe the assets (real estate, operations, and organizations) which will be included as collateral for the proposed mortgage. The assets should include those necessary to operate the hospital, including off-site properties (such as clinics and MOBs), as well as other major assets. OHF generally does not entertain asset exclusions from proposed mortgages; however, the subject is open to discussion. If exclusions are proposed, describe the assets you propose to exclude (the name of the legal entities, if applicable), list the net book value of the assets, and discuss why those assets should be excluded.

C. SECTION 242/223(F) STATUTORY ELIGIBILITY CRITERIA

Patient Day Rule

Section 242 is designed for acute care hospitals. OHF uses the patient day calculation to determine whether the hospital is an acute care facility. If more than 50 percent of the hospital's patient days are in ineligible categories (described below), the hospital will not qualify for the Program.

Patient days assignable to chronic convalescent and rest, drug and alcoholic, epileptic, mentally deficient, mental, nervous and mental, and/or tuberculosis are **ineligible** patient days. Included in the **ineligible** patient day category are patient days attributable to skilled nursing, intermediate care, convalescent care, rehabilitation, and psychiatric care.

For Hospitals that provide a significant level of outpatient services, OHF allows applicants to use an adjusted patient day calculation to determine eligibility. Please see Handbook 4615.1 APPENDIX 1 for details.

Please state whether the hospital meets the patient day rule and provide your calculations.

Loan-to-Value Requirement (LTV)

Hospitals must demonstrate no more than a 90 percent LTV ratio to be eligible for FHA mortgage insurance.

Calculate LTV based on the proposed project costs from the HUD Form 92013. LTV is calculated using the formula below. Also included is guidance for calculating Net PPE, a component of Total Estimated Replacement Cost.

LTV = (Total Mortgage Amount) / (Total Estimated Replacement Cost)

Total Mortgage Amount – From Section D, Line 8 of Form 92013 (includes the amount of the proposed mortgage).

Total Estimated Replacement Cost – From Section C, Line 32 of Form 92013.

Net PPE – From Section C, Line 30 of Form 92013 (based upon the book value of the mortgagor's property, plant, and equipment from its latest financial audit. Net PPE should not include equipment secured by leases nor other real estate or property that will be excluded from the collateral). If the book value of the hospital's Net PPE will be written-down following construction (common with replacement facilities), the Net PPE should be reduced by the total amount to be written-down. If portions of the facility will be demolished, please also subtract the approximate book value of that portion of the property from the calculation. OHF uses the residual value when calculating LTV.

Please note that if the hospital does not own its property in fee simple, and is only able to grant the lender a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV.

- If the hospital maintains a 99-year lease on the property, or maintains a 50-year lease with the option to renew for at least 49 years, the value is discounted by 5 percent
- If the hospital maintains a lease of 50 years or greater, but does not meet the requirement above, the value is discounted by 90 percent
- If a hospital maintains a lease of less than 50 years, the project is not eligible

LTV may also be met by providing an appraisal of the property to be mortgaged prepared by a qualified health care appraiser, approved by HUD and licensed in the State in which the hospital is located. The appraisal must be prepared in accordance with OHF guidelines. Please contact the OHF Underwriting Division Director for details.

D. EQUITY CONTRIBUTION AND WORKING CAPITAL

Hospitals must have sufficient reserves to make any required cash equity contribution at closing of a Section 242/223(f) loan and to maintain sufficient working capital to operate post-closing. If an equity contribution is needed to meet LTV, or if the hospital plans to provide additional equity, please note the source of the contribution. Describe how much unrestricted cash and investments the Hospital has, and its current levels of working capital.

E. MINIMUM FINANCIAL CRITERIA

Minimum Requirement for the Aggregate Operating Margin

Hospitals with an aggregate operating margin of greater than 0.00 percent, calculated from the three most recent audited financial statements, are eligible for Section 242/223(f) mortgage insurance. The formula for the aggregate operating margin is below:

$$\frac{\textbf{Operating Income (Year 1) + Operating Income (Year 2) + Operating Income (Year 3)}}{\textbf{Total Operating Revenue (Year 1) + Total Operating Revenue (Year 2) + Total Operating Revenue (Year 3)}}$$

Operating revenue is the revenue from the core patient care operations of the hospital. It includes revenues from the provision of patient care, transfers from temporarily restricted accounts that are used for current operating expenses, and patient-related activities such as the operation of the cafeteria and parking facilities. OHF's calculation of *operating revenue* excludes sources of revenue (contributions, grants, and investment income) that are not reliable sources of future revenue. *Operating income* equals *operating revenue* minus *operating expenses*.

Please provide your calculations of the operating margin for the last three completed fiscal years, below. Also include the calculation of the aggregate operating margin. The calculations should exclude the operations of affiliates/subsidiaries/business lines that will not be collateral for the insured mortgage.

Aggregate operating margin for last 3 years ≥ 0.0

	FY 20__	FY 20__	FY 20__	Aggregate
Operating Margin				

If the hospital does not meet the Operating Margin criterion, but the hospital's performance in one of the three years used in the calculation was affected by exceptional, one-time events that substantially altered financial performance, the hospital may be eligible for Section 242/223(f) mortgage insurance. Please contact the OHF Underwriting Division Director for more details.

Minimum Requirement for the Debt Service Coverage Ratio

Hospitals with an average debt service coverage (DSC) ratio above 1.40, calculated from the three most recent audited financial statements, are eligible for Section 242/223(f) mortgage insurance. The formula for the DSC ratio is below:

$$\frac{\textbf{(Excess of Revenues Over Expenses) + Interest Expense + Depreciation Expense + Amortization Expense}}{\textbf{Current Portion of Long-Term Debt (Prior Year, Including Capital Leases) + Interest Expense}}$$

The DSC ratio is based upon the hospital's "excess of revenues over expenses" (or in the case of for-profit organizations, "net income") as it appears in the hospital's audited financial statements. Please provide the average DSC ratio for the last three completed fiscal years in the space provided.

Average DSC for last 3 years $\geq$ 1.40

	FY 20__	FY 20__	FY 20__	Average
DSC				

If the hospital does not meet the DSC criterion, but the hospital's performance in one of the three years used in the calculation was affected by exceptional, one-time events that substantially altered financial performance, the hospital may be eligible for Section 242/223(f) mortgage insurance. Please contact the OHF Underwriting Division Director for more details.

Note:

1) If the operating margin and DSC criteria are not met, OHF will recast these ratios for prior periods by applying its estimate of the projected interest rate at the time the mortgage is expected to close in lieu of the historical rate(s).

State and Local Government Support / Tax Support

If the hospital is the recipient of tax revenues, revenues from state-wide hospital assessments, or appropriations (common for critical access hospitals and safety net facilities), please describe the nature, authority, and future reliability of the support. Identify and describe the statutes, legislation, or referenda that created the support.

If the revenue is provided by an assessment program or appropriation, please list historical net receipts (last five years) and future anticipated receipts. Is the revenue guaranteed to be delivered to the hospital by state law? If the support is set to expire, or is expected to be renewed, please indicate so. Please describe the future reliability of the revenue source.

If the revenue is tax support, under what circumstances could the tax support be revoked? What action would be required to revoke or diminish the support? What entity collects the tax? Are there restrictions on the use of tax proceeds? Please describe community support for the tax including (if appropriate) election results. Has the tax support recently been renewed, or will it be renewed, by referendum, contract, resolution, or other action by the hospital or local agency? Will the tax automatically "sunset"? Is there any indication that the support may be reduced or discontinued?

F. COMPLIANCE WITH STATE AND FEDERAL STATUTES AND REGULATIONS

In order to be eligible for financing, the hospital must be in compliance with federal and state regulations governing the operation and reimbursement of hospitals. Is the Hospital under investigation by any state or federal agency for statutory or regulatory violations?

G. REFINANCING COMPONENT

Purpose and Nature of the Debt

Please answer the following questions and provide the information requested about each debt issue that will be refinanced with mortgage proceeds:

1) Indicate the unpaid principal balance of each issue to be refinanced and the interest rate(s) on the existing debt. Include the total outstanding balance of the debt in Section D, Line 2 (Refinanced Capital Debt) of Form 92013.

2) What is the estimated interest rate and term of the proposed loan?

3) Please describe the nature of the debt (i.e. variable or fixed rate, taxable or tax-exempt, maturity date, prepayment or termination costs). Please describe any special characteristics of the debt (for example, the use of swaps).

4) Please provide the Official Statement(s) for the debt issue(s) (or other information that documents the sources and uses of funds, and the project description) to be refinanced. If the issue(s) included a refinancing component as a use of funds, please provide the Official Statement (or other documentation) for the original issue that was refinanced. In order to refinance debt with mortgage proceeds, the original issuance of the debt must be tied to the acquisition, construction, or rehabilitation of a capital asset.

5) When was construction on the capital project(s) funded with proceeds from the debt issuance completed? Debt associated with structures completed less than two years prior to submission of the Section 242/223(f) application may not be eligible to be refinanced.

Limit on Construction

Loans insured under Section 242/223(f) may include a construction component (hard costs). However, if there are hard costs, such costs must total less than 20 percent of the loan amount. That is, Section C, Line 11 of the Form 92013 must be less than 20 percent of Section D, Line 8 of the 92013.

H. IS THERE A NEED FOR THE REFINANCING?

The hospital must demonstrate that it has a need to refinance so that it can continue to provide needed healthcare services to its community. Please see the Section 242/223(f) Preliminary Review Supplement for more information.

I. PHYSICIAN OWNERSHIP

If physician ownership is present, please describe. Physician-owned facilities must comply with the Federal Physician Self-Referral Prohibition laws and anti-kickback prohibitions (including updated rules concerning physician ownership in the Patient Protection and Affordable Care Act). Experienced hospital counsel will be required to provide an acceptable legal opinion as to compliance with the aforementioned rules. In addition, investor-owned hospitals are reviewed for their impact on existing healthcare providers, particularly those providing uncompensated care.

J. FIRST LIEN

Is the hospital able to grant a first lien on hospital property, plant, equipment, and receivables to its FHA lender? OHF requires that the lender have a first lien position on property, plant, equipment, receivables, and revenues.

Please address the following four questions:

1) Is all of the hospital's real estate owned in fee simple? If the hospital is only able to grant a mortgage on a leasehold interest, OHF discounts the value of the property when calculating LTV. Please see Section C.
2) Does local government allow the lender to have a first mortgage lien on the property?
3) Does the hospital have a current or planned receivables financing program?
4) Are there other challenges that prevent the lender from having a first lien on the hospital's property, plant, equipment, receivables and/or revenue?

K. COMMENCEMENT OF CONSTRUCTION

OHF limits the amount of site preparation performed prior to submission of a Section 242/223(f) application. If there is a construction component to the project, indicate whether site preparation or other construction has begun, or is planned to begin, prior to application submission.

L. STATE CERTIFICATE OF NEED APPLICATION STATUS

In order to be eligible for Section 242/223(f) mortgage insurance, state Certificate of Need (CON) requirements must be met. Does the project require a CON? If so, has the application process begun? Describe the current status of the process and indicate the expected date of CON approval.

M. MORTGAGE ORIGINATOR

Please identify the mortgage originator and note the experience of the firm and individual representing the firm with the Section 242 program. Please note attendance at Section 242 Training sessions and the number of applications submitted within the past three years. If the hospital has not selected a firm, OHF can provide a list of originators who are active in the program.

LIST OF ATTACHMENTS

Please include the following attachments with the submission:

Attachment 1: Provide a draft HUD Form 92013.

Attachment 2: Include a chart showing the organizational structure (include the hospital, all affiliates, subsidiaries, and parent organizations). On the chart, note what real estate, operations, and organizations will and will not be included as collateral for the proposed mortgage.

Attachment 3: Provide the hospital's utilization statistics for the three most recent, completed fiscal years, and the interim period for the current fiscal year. Using the data for the most recently completed fiscal year, include a worksheet showing a detailed breakdown of patient days, and the calculations of the patient day rule.

Attachment 4: Provide a worksheet showing the calculation of LTV. Please provide a separate schedule listing the assets (and corresponding book values) of the property, plant, and equipment that will be secured under the proposed mortgage. These values should be entered in Section C, Lines 30 and 31 of Form 92013. When providing an estimate for Net PPE, please exclude property, plant or equipment not included as collateral in the proposed mortgage, such as equipment secured by other lenders (e.g., equipment under lease).

Attachment 5: Provide copies of the audited financial statements for the last five years, and interim financial statements for the most recent interim period (as well as data for the prior year's interim period, for comparative purposes). Provide both consolidated and consolidating financial statements, if applicable. If the hospital is the recipient of tax revenues, please provide the legal documents (statutes, referenda, etc.) authorizing or describing the tax.

Attachment 6: Provide in a separate worksheet the calculation of the historical aggregate operating margin and the historical average DSC ratio. Provide details of calculations. Please include on a separate schedule a breakdown of "other operating revenue" for each of the last three complete fiscal years (and for the most recent interim period). "Other operating revenue" is typically reported following Net Patient Service Revenue in the audited financial statements.

Attachment 7: Provide the Official Statements or other information that documents the sources/uses of funds and project descriptions for the debt issues to be refinanced through Section 242/223(f).

Attachment 8: Provide an electronic copy of the completed Applicant Data Request. Please carefully review the instructions and submit a complete response. The Applicant Data Request (an excel document) may be found on the OHF website.

PRELIMINARY REVIEW REPORT -START-UP HOSPITAL SUPPLEMENT

[INSERT DATE]

HOSPITAL: **Name:**
Address:

FHA APPROVED LENDER: **Name:**
Firm:
Address:
Email:
Telephone Number:

DOCUMENTS PROVIDED:

___ Any available draft cash flow statements
___ Any available draft forecast income statements and balance sheets
___ Any available demand statistics (admissions, outpatient visit, and surgeries), payor mix, bad debt/charity assumptions, and medical staff recruiting budget
___ 2% of mortgage in lieu of AMPO on HUD Form 92013 Hospitals, line D.5 (for-profit hospitals only)
___ Initial operating capital defined on HUD Form 92013 Hospitals, line D.6
___ Resumes of key management personnel
___ Business Plan including draft Medical Staff recruiting plan

ARE MINIMUM FINANCIAL CRITERIA MET?

Average operating margin for first 3 years $\geq$ 0.00

	1st Year	2nd Year	3rd Year	Average
Operating Margin				

Average Debt Service Coverage (DSC) for first 3 years > 1.4

	1st Year	2nd Year	3rd Year	Average
DSC				

Initial Operating Capital = to HUD requirements?

In the case of a new hospital or a hospital expansion, HUD shall establish, on a case-by-case basis, the amount of initial operating capital, if any, that must be deposited in cash or a letter of credit (or combination) to be available to the new hospital upon commencement of operations. *If a letter of credit is used, it cannot be backed by the mortgagor or the mortgagor's property and it must be irrevocable. The letter of credit must be issued by, or the liquid assets escrow must be placed with, a financial institution that:

- Has assets of not less than $1,000,000,000;
- Is organized under the laws of the United States or a state thereof and is regulated and examined by the Comptroller of the Currency, the Federal Deposit Insurance Corporation, or the Federal Reserve Board; and
- Has a long-term bank deposit rating of A-1 or better by Moody's Investor Service or A+ or better by Standard and Poor's.*

Generally, the initial operating capital other than AMPO (not-for-profit only) shall not be borrowed funds unless HUD determines that there are offsetting financial strengths to compensate for the risk associated with borrowing. What initial operating capital is available for this project?

	Pre-Opening Expenses	**First Day Inventory & Non-Capital Items**	**First 6 Months of Cash Expenses**	**First 6 Months of Debt Payments**	**2% of Mortgage Amount in lieu of AMPO (Project Capital)**	**Total Initial Operating Capital**
Initial Operating Capital						

<u>IS THE HOSPITAL NEEDED?</u>

Revisions to the Hospital Mortgage insurance Program Final Rule published in the Federal Register on November 28, 2007 (77 FR 67524, the 2008 Final Rule) provide guidance concerning the definition of market need. <u>Generally, Section 242 insurance may support start-up hospitals only if existing hospital capacity or services are clearly not adequate to meet the needs of the population in the service area.</u> The Market Need approval process entails a determination of the market need of the proposal and stresses the impact of the proposed facility on, and its relationship to, other healthcare facilities and services, particularly hospitals that have a disproportionate share of Medicaid and uninsured patients or provide a substantial amount of charity care. Other factors which require review include the number and percentage of any excess beds and demographic projections. Are there any special conditions or considerations that should be taken into account concerning the need for this particular hospital?

<u>DOES HOSPITAL MANAGEMENT HAVE SUCCESSFUL PAST EXPERIENCE WITH START-UP HOSPITALS?</u>

Please provide a narrative describing the management team's start-up hospital experience and, if possible, the financial performance of the hospitals they started.

IS THE ORGANIZATION THAT PROPOSES THE START-UP HOSPITAL NEW AND/OR DEPENDENT ON ONE OR A FEW INDIVIDUALS FOR CONTINUITY AND SUCCESS?

Section 242.10 of title 24 of the Code of Federal Regulations requires all hospitals to demonstrate continuity of organization commensurate with the 25 year term of the mortgage loan and makes particular note of new organizations, or those whose continuity is necessarily dependent upon an individual or individuals because of the increased risk the program has experienced with such owner/operators. If the answer to the above question is yes, please provide a narrative explaining what steps have been taken to ensure continuity or organization for the life of the loan and the degree to which the community has participated in and is solidly behind the project.

WILL THE HOSPITAL BE ABLE TO RECRUIT ENOUGH MOTIVATED PHYSICIANS TO ACHIEVE BUSINESS PLAN DEMAND STATISTICS AND POSITIVE CASH FLOW FOR THE FIRST YEAR OF OPERATION?

Please describe how the medical staff recruiting plan and recruiting budget support the business plan in terms of defining and funding searches for the types and numbers of physicians to be recruited and providing the lead time necessary to recruit each physician.

PRELIMINARY REVIEW REPORT -223(F) REFINANCING SUPPLEMENT

HOSPITAL: **Name:**
Address:

FHA APPROVED LENDER: **Name:**
Firm:
Address:
Email:
Telephone Number:

This Preliminary Review Supplement has been prepared for use by hospitals and mortgage lenders interested in applying for Section 242/223(f) mortgage insurance. This document supplements the Section 242/223(f) Preliminary Review Template. Both documents must be submitted in order for the Office of Hospital Facilities (OHF) to complete a Preliminary Review for a proposed Section 242/223(f) transaction.

Completion of this Supplement requires that the Lender certify circumstances related to the Hospital and its proposed financing, and provide documentation supporting those certifications.

Eight separate certifications are included on the following pages. To meet the minimum eligibility requirements, the Lender must sign the first (1) certification (**§242.16(A)(3)(VI)(A))** and three of the remaining seven (3 of 7) certifications (**§242.16(A)(3)(VI)(B)(1-7)).**

OHF will rely primarily on the Lender's certification as evidence that the criteria are met. However, supporting documentation must be included with each certification and will be reviewed by OHF for reasonableness.

§ 242.16(A)(3)(VI)(A) CERTIFICATION: THERE ARE LIMITED COMPARABLE AFFORDABLE REFINANCING VEHICLES AVAILABLE TO THE HOSPITAL

Hospital Name and Location ____

Instructions:

Please attach to this certification a statement that includes a brief description of alternatives to the Section 242/223(f) program that were considered, and explain why those alternatives are not appropriate for the Hospital. Attach to this statement any data that further supports or confirms the representations made in the statement (collectively, the "Statement").

Certification:

As demonstrated in the attached Statement, and relying upon information (such as audited financial statements and supporting schedules) provided by the Hospital, Lender hereby certifies that there are limited comparable affordable financing vehicles available to the above Hospital.

Certified by (Lender Signature) ____ **Date** ________________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(1) CERTIFICATION: THE PROPOSED REFINANCING WOULD REDUCE THE HOSPITAL'S TOTAL OPERATING EXPENSES BY AT LEAST 0.25 PERCENT

Hospital Name and Location ____

Instructions:

In the event that the Hospital is refinancing from a fixed rate issue, the Lender must use "total operating expenses" from the Hospital's most recent audited financial statement. When calculating the projected reduction in total operating expenses, the Lender must adjust the interest expense line item in the audit.

In the event that the Hospital is refinancing from a variable rate, the Lender may recast the interest expense line item in the most recent audit to reflect future changes in interest rates over the next 10 years, to arrive at an average interest expense. This recast is allowed in order to accommodate those hospitals that currently have low variable interest rates but would like to obtain a fixed interest rate through the Section 242/223(f) program.

Whether the current financing has a variable or fixed rate, the HUD mortgage insurance premium and expenses associated with the current financing as well as fees related to the refinancing portion of the transaction (such as pre-payment penalties) must be considered when calculating the reduction in total operating expenses, in addition to the interest expense. The Lender may, however, exclude the portion of the proposed loan related to the construction project (if one is proposed as part of the financing), including the associated financing expenses and fees, when projecting future total operating expenses.

In order to document that the criterion is met, the Lender must provide calculations of the existing and projected total operating expenses with the Preliminary Review submission. The Lender must also describe the information and sources (such as audits and supporting schedules) upon which the certification is based.

Certification:

Lender hereby certifies that, using estimates of current and future interest rates that it considers reasonable and justifiable, and relying upon information (such as audited financial statements and supporting schedules) provided by the Hospital, the proposed financing will reduce the Hospital's total operating expenses by at least 0.25%.

Certified by (Lender Signature) ______________________________ **Date** ____________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(2) CERTIFICATION: THE INTEREST RATE OF THE PROPOSED REFINANCING WOULD BE AT LEAST 0.5 PERCENTAGE POINTS LESS THAN THE INTEREST RATE ON THE DEBT TO BE REFINANCED

Hospital Name and Location ____

Instructions:

If the Hospital seeks to refinance multiple debt instruments at varying interest rates, a weighted average of all debt interest rates must be used to establish an overall current interest rate.

To document the criterion is met, the Lender must include calculations of the average interest rate (if necessary) with the Preliminary Review submission, and provide an estimate for the projected interest rate within the Preliminary Review Template. The Lender must also describe the information and sources upon which the certification is based.

Certification:

Lender hereby certifies that, using estimates of current and future interest rates that it considers reasonable and justifiable, and relying upon information on the current financing provided by the Hospital, the interest rate on the proposed financing will be at least 0.5 percentage points less than the interest rate on the debt to be refinanced.

Certified by (Lender Signature) ______________________________ **Date** ____________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(3) CERTIFICATION: THE INTEREST RATE ON THE DEBT THAT THE HOSPITAL PROPOSES TO REFINANCE HAS INCREASED BY AT LEAST ONE PERCENTAGE POINT AT ANY TIME SINCE JANUARY 1, 2008, OR IS VERY LIKELY TO INCREASE BY AT LEAST ONE PERCENTAGE POINT WITHIN ONE YEAR OF THE DATE OF APPLICATION

Hospital Name and Location ____

Instructions:

In order to demonstrate that the interest rate is very likely to increase by at least one percentage point a year after the date of application, the Lender must include a reference to a specific event (such as an expiration of a credit facility or downgrade of a credit enhancement facility) that is very likely to take place.

If the increase has occurred, the Lender must provide documentation of that increase.

Note:

If reliance on this certification is necessary for the Hospital to be eligible for Section 242/223f, and the increase in interest rate has not occurred, then HUD will not consider issuing a commitment for the proposed project until the applicant provides compelling evidence that the rate will increase.

Certification:

The Lender hereby certifies that, relying upon information and evidence provided by the Hospital, the interest rate on the debt that the Hospital proposes to refinance has increased by at least one percentage point at any time since January 1, 2008, or is very likely to increase by at least one percentage point within one year of the date of application.

Certified by (Lender Signature) ______________________________ **Date** ____________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(4) CERTIFICATION: THE HOSPITAL'S ANNUAL TOTAL DEBT SERVICE IS IN EXCESS OF 3.4 PERCENT OF TOTAL OPERATING REVENUES, BASED ON ITS MOST RECENT AUDITED FINANCIAL STATEMENT

Hospital Name and Location ____

Instructions:

In order to document that the Hospital meets this criterion, the Lender must base the calculation of annual total debt service on the average interest expense and principal payments on all of the proposed mortgagor's long-term debt during the last three completed (audited) fiscal years, and provide those calculations as part of the Preliminary Review submission. The Lender must also describe the information and sources upon which the certification is based.

Certification:

The Lender hereby certifies that, relying upon the most recent audited financial statements and other information provided by the Hospital, the Hospital's annual total debt service is in excess of 3.4 percent of total operating revenues.

Certified by (Lender Signature) ______________________________ **Date** ____________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(5) CERTIFICATION: THE HOSPITAL HAS EXPERIENCED A WITHDRAWAL OR EXPIRATION OF ITS CREDIT ENHANCEMENT FACILITY, OR THE LENDER PROVIDING ITS CREDIT ENHANCEMENT FACILITY HAS BEEN DOWNGRADED, OR THE HOSPITAL CAN DEMONSTRATE THAT ONE OF THESE EVENTS IS IMMINENT

Hospital Name and Location ____

Instructions:

In order to meet this criterion, the Lender must provide documentation showing that one of these events (or a similarly detrimental event) has occurred, or is imminent. If the Lender provides this certification based upon the occurrence of a similarly detrimental event, the Lender must provide documentation of that event.

Note:

In any event, if reliance on this certification is necessary for the Hospital to be eligible for Section 242/223f, HUD will not consider issuing a commitment for the proposed project until the applicant provides date-certain evidence of the past or future occurrence of such an event.

Certification:

The Lender hereby certifies that, relying upon information and evidence provided by the Hospital:

- ☐ the Hospital has experienced a withdrawal or expiration of its credit enhancement facility;
- ☐ the Lender providing its credit enhancement facility has been downgraded;
- ☐ the Hospital can demonstrate that one of these events is imminent; or
- ☐ a similarly detrimental event has occurred or is imminent:

Certified by (Lender Signature) ______________________________ **Date** ____________

Name/Title (Print) ____

Company ____

§ 242.16(A)(3)(VI)(B)(6) CERTIFICATION: THE HOSPITAL IS PARTY TO COVENANTS ON ITS EXISTING FINANCING THAT ARE SUBSTANTIALLY MORE RESTRICTIVE THAN THE SECTION 242 MORTGAGE COVENANTS

Hospital Name and Location ____

Instructions:

In order to demonstrate that this criterion is met, the Lender must attach a statement that includes the text of the relevant existing covenants and describes with specificity how those covenants are more restrictive than HUD's current standard covenants.

Certification:

The Lender hereby certifies that, after review of covenants (of the current financing(s)) provided by the Hospital, the Hospital is party to the attached described covenants on its existing financing(s) that are substantially more restrictive than HUD's standard covenants for the Hospital Mortgage Insurance Program.

Certified by (Lender Signature) ____ **Date** ________________

Name/Title (Print) ____

Company ____

242.16(A)(3)(VI)(B)(7) CERTIFICATION: THERE ARE OTHER CIRCUMSTANCES THAT DEMONSTRATE THAT THE HOSPITAL'S FINANCIAL PERFORMANCE WOULD BE MATERIALLY IMPROVED BY REFINANCING ITS EXISTING CAPITAL DEBT

Hospital Name and Location ____

Requirements:

In order to meet this criterion, documentation must be provided that demonstrates:

1) The refinancing will improve the Hospital's three year aggregate operating margin (based on the audited financial statements for the last three years) by at least 0.25 percentage points or greater, or
2) The refinancing will improve the Hospital's operating income (based on the most recent year's audited financial statements) by $500,000 or greater, or
3) Annual debt service (based on the average interest expense and principal payments on the debt during the last three completed (audited) fiscal years) will be reduced by 10% or more, or
4) The Hospital would benefit from refinancing a variable rate issue into the safety of a fixed rate issue.

Instructions:

In the event that the Hospital is refinancing from a fixed rate issue, the Lender must calculate the projected metrics (operating margin, operating income, and annual debt service) using methods consistent with guidance provided by HUD.

The Lender may exclude the portion of the loan related to the construction project and the financing expenses and fees related to that construction project (if one is proposed as part of the financing) when projecting the metrics.

The HUD mortgage insurance premium and expenses associated with the current financing, as well as fees related to the refinancing portion of the transaction (such as pre-payment penalties), must be considered when calculating the metrics.

In order to document that the Hospital meets this criterion, the Lender must provide calculations of the metrics described above. The Lender must also describe the information and sources upon which the certification is based.

HUD may accept other evidence that the financing will materially improve the Hospital's financial performance in the event that it does not meet the three metrics above. In this event, please contact the Office of Hospital Facilities' Underwriting Director for details.

Certification:

The Lender hereby certifies that, using estimates of current and future interest rates that it considers reasonable and justifiable, and relying upon information (such as audited financial statements, supporting schedules, and facts and circumstances concerning the existing financing(s)) provided by the Hospital, there are other circumstances that demonstrate that the Hospital's financial performance would be materially improved by refinancing its existing capital debt.

Certified by (Lender Signature) ____ **Date** ________________

Name/Title (Print) ____

Company ____