

July 11, 2014

TO: Rural Development State Directors  
Rural Development Managers  
Area Directors

ATTENTION: Multi-Family Housing  
Program Directors

FROM: Tony Hernandez  
Administrator  
Housing and Community Facilities Programs

SUBJECT: Prepayment Incentives Processing Guidance

The purpose of this Unnumbered Letter is to provide guidance on prepayment incentive offers.

Rural Development is sensitive to the need to provide prepayment incentives to maintain affordable housing in the communities with the greatest need. Rural Development recognizes that incentives provide a relatively inexpensive way of providing long-term affordable housing to support low and very-low income rural Americans.

However, as a result of the rescission in the FY 2013 budget and continued funding limitations in the FY 2014 budget, we are facing many challenges in meeting multi-family funding needs. This challenge is particularly acute in the Rental Assistance (RA) program. As Rural Development looks for ways to manage the RA program, it is becoming increasingly difficult to provide needed RA to renew agreements for the benefit of existing tenants.

In light of this difficulty, the use of additional RA to protect rent overburdened tenants or provide new units of RA to Rural Development multi-family properties as an incentive to remain in the Section 515 program presents a significant challenge to Rural Development. Therefore, the Office of Multi-Family Housing is putting in place certain measures to ensure that the award of prepayment incentives does not preclude existing program needs, especially in the RA program. These measures are an interim step while we process permanent changes to the regulation to incorporate a more effective process for developing and distributing equitable prepayment incentives.

EXPIRATION DATE:  
January 31, 2015

FILING INSTRUCTIONS:  
Housing Programs

State offices should continue to accept all eligible prepayment applications. The process for eligible applications for prepayment where the borrower *is not* seeking any incentives remains the same. In situations when the borrower will not accept any incentives offered by the Agency, as stated in writing by the borrower, the borrower may take the next step in the prepayment process.

Per CFR 3560.656 Incentive Offers, the Agency may offer the following incentives:

- 1) The Agency may increase the borrower's annual return on equity;
- 2) The Agency may agree to convert projects without interest credit or with Plan I interest credit to Plan II interest credit or increase the interest credit subsidy for loans with Section 8 assistance to lower the interest rate on the loan and make basic rents more financially feasible;
- 3) The Agency may offer additional rental assistance or an increase in assistance;
- 4) The Agency may make an equity loan to the borrower;
- 5) The Agency will offer rental assistance to protect tenants from rent overburden caused by any rent increase as a result of a borrower's acceptance of an incentive offer or tenants who are currently overburdened; and
- 6) In housing projects with project-based Section 8 assistance, the Agency may permit the borrower to receive rents in excess of the amounts determined necessary by the Agency to defray the cost of long-term repair or maintenance of such a project.

Because of the funding situation, incentives (3), (4), and (5) shall not be offered to borrowers without the concurrence of the National Office. Concurrence from the National Office must be received prior to the states' formulation of the general offer to the borrower seeking to prepay. In order to offer incentives (3), (4) and (5), the state office must provide the National Office a justification that includes an explanation for the need to specifically offer RA incentives to retain that project and the importance of the affordable housing it provides in its community. Since additional equity loans may require additional RA to pay for the additional debt service, incentive (4) should only be offered when it is financially feasible without additional RA. As long as RA funding to a property does not increase as an immediate or future result of the offer, state offices may make specific incentives offers (1), (2), and (6) in accordance with CFR 3560.656 and with the State Director's approval.

For specific offers that require prior National Office concurrence, the state office should forward their recommendation(s) to the National Office along with the name(s) of the owner(s), project name(s), borrower ID and loan number(s) and total project units in these application(s).

All complete Prepayment Applications submitted by qualified borrowers should be processed via the MFH PRE-TRAC System to generate the General Incentive Offer.

Should you have any questions regarding the offering of incentives to prevent prepayment, please contact Tiffany Tietz at 616.942.4111 extension 126 [or tiffany.tietz@wdc.usda.gov](mailto:tiffany.tietz@wdc.usda.gov), of the Preservation and Direct Loan Division,