

## **Ordering for a New Draft Guide PCNA, or is it CNA?**

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I knew it was coming, but just like the blooming of spring the exact date was unpredictable. To make it more fun I started an informal office pool and I penciled in May 1<sup>st</sup> as the date it would arrive. And it was nearly two weeks early! The “it” I am talking about is our first request for proposal for a “new” Draft MAP Guide PCNA Version 2015!

HUD issued the Draft MAP Guide on February 28, 2015. Based upon comments made by HUD at the Eastern Lenders Conference, we can expect the “Final” version of the MAP Guide to be issued prior to Labor Day. With this anticipated release timeframe, we would expect lenders to consider preparing applications for the new Section 223(f) FHA mortgage insurance approximately 90 to 120 days in advance. But lender analysts need to understand this is not like ordering a previous PCNA report; this is a multipart due diligence study.

I hope this paper assists MAP lenders on where to start, and that it sheds light on the information needed from your borrower in order to facilitate a fee quotation under the new guidance. So let me go through the scopes of work required under the new Draft MAP Guide Chapter 5:

### Scope of Work #1: Capital Needs Assessment

The new capital needs assessment is basically the same as the PCNA under current interpretation of the MAP Guide. One of the many positive changes in the proposed Draft MAP Guide included less prescriptive language regarding intrusive (forensic) investigations. While these studies may be necessary in older properties, the 30-year qualifier was removed from guidance. Also, lenders need to be aware that upon release of HUD’s CNA e-Tool platform the method of reporting will change dramatically, but rest easy for now as the release date is largely unknown. Information needed to accurately quote the capital needs assessment would mostly remain as it currently stands:

- Description of asset (size, age, configuration)
- Description of federal involvement outside of mortgage insurance
- Description of past significant capital improvements or renovations

### Scope of Work #2: Lender’s Construction Analyst Review (if necessary)

One of the fundamental differences between the new 223(f) capital needs assessment and the previous PCNA is the proposed increase to the Non-Critical Repair limits. While at first blush this seems like a welcome change, dilemma resides in quoting professional services as to what amount of repair is necessary at a given property. Is the sponsor predicting few repairs or do they want to leverage the maximum amount possible with heavy repairs to reduce future ADRR and IDRR amounts? This is a question of great importance as it defines the property as a Level 1, Level 2, or Level 3 repair project. This International Building Code Existing Building definition will define the deliverables and duties of both the development team and the third-party consultant. For example, a

Level 1 repair project will have minimal documentation and review requirements; however, Level 2 and Level 3 projects feature increased design submission and review requirements. Information needed to assemble an accurate quote would be:

- Description of proposed retrofits or repairs
- Notification if a General Contractor and Architect are already engaged by the borrower

#### Scope of Work #3: ASHRAE Level 2 Energy Audit

If the property is greater than 10 years of age, an ASHRAE Level II Energy Audit is required. Per proposed guidance, these studies need to be performed by highly qualified and accredited building scientists. Fortunately for MAP Lenders, third-party firms experienced with the HUD RAD program have worked out the kinks of these studies. However, ordering these services presents a new subset of terms, acronyms, questions and information the MAP lender will need to prepare. Information necessary to provide a free quotation for an ASHRAE Level II energy audit include:

- Description of asset (size, age, configuration)
- Description of unit configuration (number, size, configuration of units)
- Description of utility configuration (water, sewer, electric, gas, other)

#### Scope of Work #4: Statement of Energy Performance (SEP)

All properties will require a SEP generated from the EPA's ENERGY STAR Portfolio Manager® system. The benchmarking process by itself is not difficult; however, obtaining and processing the data necessary for benchmarking presents concerns. The benchmarking process requires 12-months of entire property energy use, including both resident use and property use. This presents significant problems with properties featuring individually metered water, gas, and electric utilities. For example, a master metered, 100 unit building would likely have three (3) utility meters, one each for water/sewer, electricity and gas, resulting in 36 data entry points (12 months consumption multiplied by 3 meters); however, an individually metered, 100 unit property would likely have up to 300 utility meters, resulting in 3,600 data entry points for any given year. In the second individually metered scenario, both access and processing of the data is exponentially more difficult. With this in mind, when ordering a SEP, MAP lenders are going to have to be familiar with some new terms and requests for data, including:

- Description of utility configuration (water, sewer, electric, gas, other)
- Description of utility metering/billing arrangements
- Understand the timing limitations based upon availability of data

The above discussion of four (4) scopes of work offer some challenges for the industry as well as potential "chicken or the egg" scenarios, namely:

- a. Scope 1: Beware that upon release of HUD's CNA e-Tool platform the method of reporting will change dramatically. What this means is lenders and borrowers are going to need to be flexible if, and when, HUD says all data must be entered into this new on-line system. Make sure your third party provider is knowledgeable of the tool and has the ability (and, just as importantly, the willingness) to populate the system.

- b. Scope 2: More often than not, the Non-Critical construction items are not known up front. Also, with higher repair level allowances under the new Section 223(f), we expect Non-Critical Repairs to be a blending of Owner Elected Improvements and Needs Assessor identified repairs. But not knowing if a property will be a Level 1 or a Level 3 repair at the outset presents a dilemma for the MAP lenders. Does a lender treat these ancillary reviews as a secondary technical scope quoted after completion of the PCNA, or do lenders request a proposal for worst case scenario in order to have escrow arrangements established? Also, beware that the effort, personnel, and time commitment between a 223(f) Level 1 project and a 223(f) Level 3 project will vary significantly.
- c. Scope 3: The draft MAP Guide requires the final scope of repairs incorporate economically feasible green upgrades if the MAP lender seeks underwriting of reduced expenses. This integration of studies and disciplines requires communication, and lenders need to be aware that if separate firms are selected for the studies, or if third parties sub-contract parts of the assessment, there may be a bulky and reiterative process in scoping Non-Critical repairs.
- d. Scope 4: This task requires advanced cooperation from the property owner in obtaining energy consumption data. Master metered properties, while not as common and typified by the unitary elderly midrise, present less complexity. Contrarily, the more common individually metered properties can present significant timing delays with obtaining individual tenant utility data. Also, be aware that a low SEP score (under 60) could drive additional Non-Critical Repairs, affecting Scope 1, 2 and 3 of the assessment.

So there you have it, the typical new Section 223(f) capital needs assessment scope of work and the four (4) components of the study. I hope that readers understand this new Draft MAP Guide capital needs assessment quartet requires a conductor. Someone who knows what is needed, the timing associated with each task and, most importantly, the interconnectivity of each study. Let D3G be your conductor to the new MAP Guide capital needs assessment.