



**Housing Justice Center**  
**Public Interest Legal Advocates**

## **HUD PERMITS PREMATURE OPT OUTS OF STATE FINANCE AGENCY SECTION 8 SET ASIDE PROJECTS**

The HUD policy at issue here permits owner opt-outs contrary to the terms of the Section 8 contracts and potentially affects nearly 58,000 Section 8 units in 637 projects in 26 states. HUD's original implementation of the Section 8 legislation included a State Finance Agency Set aside program, in which HUD entered into Annual Contributions Contracts with the state agencies and the agencies then entered into Section 8 Housing Assistance Payment Contracts with developers whose developments were being financed with state agency mortgages. The HAP contracts were unique in that they ran for 5 year terms which were automatically renewed for up to 40 years unless both parties agreed in writing to non-renewal at one of the 5 year termination dates. So many of these contracts have run for 35 years or more without being renewed under the federal legislation permitting renewal of expiring contracts, potentially with rents marked up to market.

Until 1980, the HAP contracts included this language: "the total contract term for any unit...shall not exceed ... a period terminating on the date of the last payment of principal due on the permanent financing." Over the years, many projects refinanced, with no change in the Section 8 HAP contract. The language changed in 1980, and the projects with the initial language are referred to as "old reg projects."

But in 2002, HUD's General Counsel opined that the quoted language meant that the HAP contract automatically terminated upon prepayment – which would include the final payment of principle on the contract. To address the fact that many owners and agencies had continued as if nothing had changed in spite of the prepayment, HUD concluded that in those cases, there was an implied contract with the same terms as the original. The original, of course, required both parties to agree to a termination. HUD, nevertheless immediately began pushing a policy under which an owner with a prepaid state mortgage could terminate at any time with the required one year notice, without agency approval. HUD attempted repeatedly to make this policy official, and agencies and advocates repeatedly resisted, pointing out the logical inconsistency. Opponents of the HUD policy pointed out that HUD had repeatedly approved refinancings and also argued that if the HAP language had intended a prepayment to terminate the HAP, it would have read: "a period terminating on ~~the date of~~ the last payment of principal ~~due~~ on the permanent financing." A pre-payment is not a payment of "principal due;" that's why it is a "pre" –payment. The "term" referred to is obviously the parties' expectation at the time of execution of the contract as to the maturity date. What HUD was attempting to graft on to this "term" provision is a "termination" provision, triggered by an event not contemplated at the time of execution.

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At worst, the HAP language is ambiguous. In construing ambiguous contracts, courts “give effect to the mutual intentions of the parties.” *NRM Corp. v. Hercules, Inc.*, 758 F.2d 676, 681 (D.C. Cir. 1985); *Mesa Air Group v. DOT*, 87 F.3d 498, 503 (D.C. Cir. 1996). HUD is not a party to these contracts and its opinions and current intentions are simply not legally relevant.

Until last year, the agencies and advocates prevailed. In the 2014 update of the Section 8 Renewal Guide, HUD added Chapter 16, which permits owners to opt out of these contracts if the original state financing has been prepaid. While all of these projects will be on their final 5 year term, the HUD policy is not as big a disaster as it was in 2002. It nevertheless will permit opt outs to which owners are pretty obviously not legally entitled. The HUD Section 8 database indicates that 637 project with 57,895 units have old regulation contracts. Not all of these are potentially affected – in some cases state agencies have taken steps to lock owners into the original contract.

The Housing Justice Center is anxious to challenge any such opt out, so call Jack Cann or email at [jcann@hjcmmn.org](mailto:jcann@hjcmmn.org) if you become aware of one.

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