

**DEPARTMENT OF AGRICULTURE****Rural Housing Service****Rural Business-Cooperative Service****Rural Utilities Service****Farm Service Agency****7 CFR Parts 1980 and 3555**

RIN 0575-AC18

**Reengineering of the Section 502 Guaranteed Rural Housing (GRH) Program**

**AGENCY:** Rural Housing Service, Rural Business Cooperative Service, Farm Service Agency, USDA.

**ACTION:** Proposed rule.

**SUMMARY:** The Rural Housing Service proposes to streamline and reengineer its regulations for the administration of its Guaranteed Rural Housing (GRH) Program. This action is taken to reduce regulations, improve customer service, and improve the Agency's ability to achieve greater efficiency, flexibility, and effectiveness in managing the program. The effect of this action is to provide better service, reduce program vulnerability, and reduce Federal regulations.

**DATES:** Written or e-mail comments must be received on or before February 14, 2000. The comment period for information collections under the Paperwork Reduction Act of 1995 continues through February 14, 2000.

**ADDRESSES:** Submit written comments via the U.S. Postal Service, in duplicate, to the Regulations and Paperwork Management Branch, Attention: Tracy Gillin, Rural Development, U.S. Department of Agriculture, Stop 0742, 1400 Independence Avenue, S.W., Washington, DC 20250-0742. Submit written comments via Federal Express Mail, in duplicate, to the Regulations and Paperwork Management Branch, Attention: Tracy Gillin, USDA—Rural Development, 3rd Floor, 300 E. St., SW., Washington, DC 20546. Also, comments may be submitted via the Internet by addressing them to "comments@rus.usda.gov" and must contain the word "GRH" in the subject line. All comments will be available for public inspection during regular work hours at the 300 E. St., SW. address listed above.

**FOR FURTHER INFORMATION CONTACT:**

Dean Daetwyler, Senior Loan Specialist, Single Family Housing Guaranteed Loan Division, RHS, Stop 0784, Room 2250, South Agriculture Building, 1400 Independence Avenue, S.W.,

Washington, DC 20250, telephone (202) 720-1480.

**SUPPLEMENTARY INFORMATION:****Classification**

This rule has been determined to be significant and was reviewed by the Office of Management and Budget (OMB) under Executive Order 12866.

**Executive Order 12988**

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. If this proposed rule is adopted: (1) Unless otherwise specifically provided, all State and local laws and regulations that are in conflict with this rule will be preempted; (2) no retroactive effect will be given to this rule except as specifically prescribed in the rule; (3) administrative proceedings of the Rural Housing Service (RHS) and the National Appeals Division (7 CFR part 11) must be exhausted before bringing suit.

The Agency is making regulatory improvements to a more seasoned loan program and is eliminating unnecessary administrative matters from the CFR. The Agency is also developing a customer and user friendly handbook which will clarify the regulation and provide clear and definitive guidance for program beneficiaries. These actions will not only benefit the Agency, but also participating lenders, their agents, and potential homeowners.

**Unfunded Mandates Reform Act**

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Public Law 104-4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, the Agency generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with "Federal mandates" that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of \$100 million or more in any one year. When such a statement is needed for a rule, section 205 of the UMRA generally requires the Agency to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule.

This rule contains no Federal mandates (under the regulatory provisions of Title II of the UMRA) for State, local, and tribal governments or the private sector. Therefore, this rule is not subject to the requirements of sections 202 and 205 of the UMRA.

**National Partnership for Reinventing Government**

This regulatory action is being taken as part of the National Partnership for Reinventing Government (NPR) to reduce and eliminate unnecessary regulations and improve those that remain in force. Currently, the administration of the GRH program is guided by a regulation totaling 36 pages in the Code of Federal Regulations (CFR). The Agency has committed itself to meet the true spirit and intent of NPR and has undertaken a massive effort to completely reinvent and reengineer its regulatory process. In the new rule, administrative matters have been eliminated and remaining text has been completely revised to be consistent, simple, and clear. The Agency will publish a handbook to provide lenders, servicers, and field staff with the administrative guidance needed to effectively and efficiently administer the program. The handbook will not be published in the **Federal Register** but will be available upon request to the public. The Agency estimates the final rule will cover approximately 23 pages in the CFR, for a 36 percent reduction in published material.

**Environmental Impact Statement**

This document has been reviewed in accordance with 7 CFR part 1940, subpart G, "Environmental Program." It is the determination of the Agency that the proposed action does not constitute a major Federal action significantly affecting the quality of the human environment and in accordance with the National Environmental Policy Act of 1969, neither an Environmental Assessment nor an Environmental Impact Statement is required.

**Regulatory Flexibility Act**

This proposed rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601-612). The undersigned has determined and certified by signature of this document that this rule will not have a significant economic impact on a number of small entities. The Agency does not regulate small entities through the GRH program. The lender makes the loan to the applicant and the Agency guarantees the loan against potential loss providing the loan meets certain conditions. Requirements of the lenders are consistent with industry standards.

**Programs Affected**

This program is listed in the Catalog of Federal Domestic Assistance under Number 10.410, Very-low to Moderate Income Housing Loans (Section 502 Rural Housing Loans).

### Intergovernmental Consultation

This program is not subject to the provisions of Executive Order 12372 which require intergovernmental consultation with State and local officials. (See the Notice related to 7 CFR part 3015, subpart V, at 48 FR 29112, June 24, 1983; 49 FR 22675, May 31, 1984; 50 FR 14088, April 10, 1985).

### Implementation Proposal

When the Agency publishes this proposed rule in final, it will remove 7 CFR part 1980, subpart D, "Rural Housing Loans," from the CFR.

After the effective date of the final rule, the Single Family Housing Guaranteed Rural Housing program will be guided by 7 CFR part 3555. All provisions of the regulation will be effective 30 days after publication of the Final Rule except for the requirement for Homeownership Education which will take effect 6 months after the publication of the Final Rule.

The handbook will provide lenders, servicers, and field personnel with the administrative guidance needed to effectively and efficiently administer the program.

### Background Information

On April 17, 1991, the Agency first published a final rule (56 FR 15748-81) implementing the Guaranteed Rural Housing program. The program was authorized under the Cranston-Gonzalez National Affordable Housing Act (Pub. L. 101-625).

After completing notice and comment rulemaking procedures, the Agency published another final rule on May 22, 1995, incorporating needed changes to encourage greater program participation, make the program more user friendly, and improve the success of the program.

Now that the program has been in effect for several years, the Agency is able to better reflect on the effectiveness and efficiencies of the GRH program and recognizes the need to focus on making the program even more effective, streamline processes, reduce costs to the taxpayer, and increase the level of customer service.

### Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995, the Agency will seek Office of Management and Budget (OMB) approval of reporting and recordkeeping requirements contained in this regulation.

Guaranteed Rural Housing (GRH) loans are made by private lenders to individuals and households for the purpose of acquiring or constructing a single family residence in a rural area. Eligibility for this program includes low

and moderate income families or persons whose income does not exceed 115 percent of the median income for the area, as determined by the Secretary.

The information requested by the Agency includes borrower financial information such as household income, assets and liabilities, and monthly expenses. All information collected is vital for the Agency to determine if borrowers qualify for and assure they receive all assistance for which they are eligible. Information requested on lenders is required to ensure that lenders are eligible to participate in the GRH program. Lender requirements are in compliance with OMB Circular A-129.

*Estimate of Burden:* Public reporting burden for this collection of information is estimated to average 25 minutes per response.

*Respondents:* Individuals or households and Business or other non-profit.

*Estimated number of respondents:* 44,830.

*Estimated Number of Responses per Respondent:* 5.68

*Estimated Total Annual Burden on Respondents:* 89,849 hours.

The GRH loan program has grown from a \$100 million program in 1991 to its current funding level of \$3 billion. Both the number of borrowers served and the number of lenders participating have increased since the program's inception. The reporting burden has increased consistent with the growth of the program; however, the cost to the consumer has been reduced by 6% since 1998 and dovetails an 11% reduction in reporting burden from 1995.

Copies of this information collection can be obtained from Tracy Gillin, Regulations and Paperwork Management Branch, Support Services Division, Rural Development, at (202) 692-0039.

Comments are invited on: (a) Whether the proposed collection of information is necessary for the proper performance of the functions of the Agency, including whether the information will have practical utility; (b) the accuracy of the Agency's estimate of the burden of the proposed collection of information including the validity of the methodology and assumptions used; (c) ways to enhance the quality, utility, and clarity of the information to be collected; and (d) ways to minimize the burden of collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

All responses with regard to paperwork burden will be summarized, included in the request for OMB approval, and will be a matter of public record. Please send written comments on the information collection aspect of the rule to the Desk Officer for Agriculture, Office of Information Regulatory Affairs, Office of Management and Budget, Washington, DC 20503 and to Tracy Gillin, Regulations and Paperwork Management Branch, U.S. Department of Agriculture, Rural Development, STOP 0742, 1400 Independence Ave., SW, Washington, DC 20250-0742. A comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication of this rule.

### Public Burden in the Handbook

The Agency is currently developing the proposed Handbook while aggressively analyzing all existing burden imposed upon the public to obtain and retain guaranteed single family housing program assistance.

The proposed Handbook will be available for public comment with regard only to its information collection requirements on or about March 1, 2000. The Agency will publish a Notice in the **Federal Register**, with a 60 day comment period, when the Handbook is available with its specific information collection requirements.

### Summary of Enhancements To Improve Program Success

The major changes to enhance the Guaranteed Rural Housing Program are discussed below in general order of appearance in the regulation, not necessarily based on order of importance.

#### Subpart A—General

The definition section will be expanded to clarify terms used in the regulation. The definition of "qualified alien" will be revised in accordance with the definition provided in section 431 of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Pub. L. 104-193. Section 402 of PRWORA provides that an alien who is not a "qualified alien" is not eligible for Federal public benefit. Section 401 of Act, in part, provides an exception for non-qualified aliens who were receiving assistance at the time of enactment under any program under title V of the Housing Act of 1949. The Agency has determined that guaranteed single family housing loans are a Federal benefit generally unavailable to non-qualified aliens. If a non-qualified alien had received a guaranteed single

family housing loan prior to the enactment of the Act, however, the Agency would continue to honor the guarantee and service the loan in accordance with the proposed rule. The Act also precludes qualified aliens from "federal means tested public benefits" for five years after they become qualified aliens. The Agency, however, considers the guaranteed single family housing loan program to be a discretionary, rather than a mandatory, assistance program that does not constitute a "federal means-tested public benefit" subject to this further restriction.

The definition of "Veteran's preference" has been updated to include Persian War era veterans in accordance with section 101 of title 38, as amended by the Persian Gulf War Veterans' Benefits Act of 1991, Pub. L. 102-25.

Most existing definitions have minor editorial revisions, but are not substantially revised.

#### *Subpart B—Lender Participation*

The section on lender participation was modified to provide additional guidance on how to become an approved Agency lender. The proposed regulation clarifies that a lender approved as a supervised or nonsupervised mortgagee by the United States Department of Housing and Urban Development (HUD), must also have direct endorsement authority from HUD for the submission of applications for Federal Mortgage Insurance to be eligible as an Agency approved lender.

The proposed regulation further clarifies that a lender approved as a supervised or nonsupervised mortgagee by the United States Department of Veterans Affairs (VA), must also be authorized to close loans on an Automatic Basis, as prescribed by VA, to be eligible as an Agency approved lender. These VA lenders have staff underwriters and have proven that they are capable of approving and closing loans per required guidelines. The application process for all lenders will be streamlined, and the Agency and its customers will realize improved loan quality.

Lenders who do not meet the requirements to become an approved Agency lender under the proposed regulation, may still be able to participate as a broker or correspondent mortgagee by processing loans through an Agency-approved lender. These lenders must submit loans through an approved Agency lender who will be responsible for underwriting the loan and ensuring program requirements are met. The guarantee will be issued in the name of the approved lender.

The Agency proposes to include other Federally supervised lenders, including those who are members of the Federal Reserve System, and those supervised by the Federal Deposit Insurance Corporation (FDIC), National Credit Union Administration (NCUA), or Office of the Thrift Supervision, as eligible lenders. These lenders will be required to provide documentation of their ability to process, underwrite and service single family loans to become an approved Agency lender. The Agency will assume that lenders approved under other Federal programs have the ability to originate and service single family housing loans.

Reporting requirements by lenders and their agents have been moved to the program participation section of the proposed regulation. This section was streamlined and contains only policy dealing with reporting to the Agency by lenders and their agents.

The Agency further proposes to require approved lenders to maintain a fidelity and omissions policy, listing the Agency as the loss payee, with a copy provided to the Agency. This will protect the Agency against the potential for fraud and mistakes made by the lender.

The Agency is also considering requiring in the final rule that approved lenders have computer systems that comply with year 2000 technology. The Agency is specifically interested in comments on such an eligibility requirement, the potential vulnerability to the servicing of a guaranteed portfolio with systems that are not year 2000 compliant, the potential vulnerability to the Agency, and the requirement's impact on lenders participation in the program.

#### *Subpart C—Loan Requirements*

##### *Interest Rate*

Agency regulations currently include a maximum interest rate which a lender can charge GRH customers. The maximum rate authorized is the greater of the rate for loans guaranteed by VA or the current Fannie Mae rate, described as the Fannie Mae 90-day Actual/Actual yield for a 30 year fixed rate conventional mortgage loan plus 60 basis points.

Lenders generally utilize the VA rate as it is higher than the Fannie Mae rate and allows a lender to adequately price the product. Lenders who do not offer loans guaranteed by VA generally do not participate in the GRH program since 60 basis points over the Fannie Mae rate does not adequately price this mortgage product. The Agency continues to receive comments that the current

regulatory standards are not feasible. Participating lenders contend that the mortgage market is so competitive, that the customer receives a more favorable interest rate than that established in our regulations making the limit unnecessary. In addition, the process is burdensome to lenders and the Agency to verify the Fannie Mae rate each time a loan is presented for guarantee. The Agency agrees that competitive forces in the marketplace help ensure that our customers receive the best interest rate. However, the Agency is concerned that in very rural markets, where there is not sufficient competition, that rural families may be subjected to higher interest rates than if no maximum were prescribed in GRH regulations.

Section 502(h)(6) of the Housing Act of 1949, as amended, requires the interest rate for guaranteed loans to be fixed over the term of the loan and not exceed the rate for loans guaranteed under 38 U.S.C. chapter 37 (Housing and Small Business Loans) or comparable loans in the area that are not guaranteed. At this time, the interest rate for loans made under 38 U.S.C. chapter 37 is a negotiated rate of interest with no maximum limitation. The rate is negotiated between the lender and borrower. In most areas, competition in the mortgage industry ensures that loan customers receive the lowest possible interest rate. However, in rural areas where there is little or no competition, and no comparable loans in the area which are not guaranteed, the Agency believes that an interest rate cap is necessary to ensure that our customers are not charged an excessive rate of interest. Therefore, the Agency is proposing to continue with a maximum interest rate for the GRH program. The rate cap will be set so as not to impact or impede upon lender participation in areas where competition exists; however, will ensure that customers in other areas are not subject to higher rates than should be offered for this mortgage product. The maximum allowable interest rate will be based upon current market factors and established with sufficient flexibility so that lenders can adequately price this mortgage product. The Agency intends to publish the rate by notice in the **Federal Register**. This will provide the Agency with flexibility to change the rate quickly if an adjustment were necessary to react to changes in market conditions. If the rate were included in the rule, it would take approximately a year to make any revisions to the rate. This timeframe could have an adverse affect on the delivery of GRH assistance. For example, if a higher rate were

necessary, lenders would not offer this mortgage product and homeownership opportunities for many rural families would be halted until the Agency could promulgate another rule. Conversely, if the market becomes so competitive that a lower rate were appropriate, rural families in many remote rural areas without adequate market competition could be faced with higher than necessary interest rates. At this time, if the Agency were to establish a maximum GRH interest rate, it would be no more than 125 basis points over the Fannie Mae 90-day Actual/Actual yield requirements, rounded to the nearest eighth of a percent.

The Agency is particularly interested in comments regarding this section. The Agency recognizes in order to attract and maintain lenders who will provide homeownership opportunities for low- and moderate income families in rural America, flexibility and simplicity is needed. However, the Agency still has a responsibility to ensure that its customers are treated equitably and not subject to interest rates that are excessive because market competition does not exist. The lowest possible interest rate helps to ensure the success of the homeowner and reduces risks to both the Agency and Lender. We believe the proposed language meets these objectives and we encourage suggestions or alternative methods to meet these goals.

#### Interest Assistance

The proposed regulation more clearly defines the eligibility criteria for existing borrowers with subsidized guaranteed loans approved between April 17, 1991, and September 30, 1991. The Agency proposes no change from the current regulation which provides that a customer should contact their lender when they have had a \$100 monthly increase in household income. The Agency has considered changing this policy to a 10% increase in household income similar to our direct loan program. However, lenders and loan servicers have stated that since so few interest assistance accounts exist such a minor change would be more confusing than beneficial. The Agency is particularly interested in comments regarding this section and whether the current policy should be continued or a "10% change" policy would benefit lenders and homeowners. A chart is included in the regulation to be used to determine the amount of interest assistance paid by the Government and the amount of the borrower's payment. The chart, which is currently Exhibit D of the existing regulation, was expanded by adding floor rate percentages for

borrowers whose income is between 80% and 115% of the median income.

The Agency currently pays a fee to the lender for processing an Interest Assistance Agreement renewal. The amount of the fee will be included in the handbook and the Agency's annual funding notice published in the **Federal Register** so that the Agency can make changes to the fee so as to keep up with costs in accordance with industry market factors.

#### Recapture

Recapture is defined as the amount of interest assistance to be repaid the Agency when the borrower transfers title or ceases to occupy the property. The Agency currently refers to recapture as "Equity Sharing" but will change the term to "Recapture" in the proposed regulation. The recapture formula has been changed to limit recapture to 50 percent of value appreciation or the amount of payment assistance received, whichever is less. Currently, the Agency can recapture the entire amount of subsidy granted to a borrower up to the value of the property. By changing the recapture formula, the Agency will be able to recognize improvements the customer made to the property, thereby providing the customer with incentive to maintain and improve their home without losing all of their equity.

The circumstances when borrowers are required to repay payment assistance have been clarified, including situations involving an assumption of a guaranteed loan.

#### Application for and Issuance of the Loan Note Guarantee

The Agency has changed the guarantee fee charged to the Lender from 1 percent of 90 percent of the principal amount advanced (.9 percent of the loan amount) to 1 percent of the full amount of the loan (1 percent of the loan amount). This change will improve consistency with industry standards and will assist the Agency in lowering the subsidy cost of the program.

#### Subpart D—Underwriting the Applicant Eligible Applicant

Current Agency regulations preclude the eligibility of current homeowners for the GRH program unless their current home is deficient. This policy was adopted when the GRH program was first authorized and funds were limited. The policy has precluded many rural families from relocating or upgrading their current housing. The Agency is now proposing to eliminate the requirement that the applicant's current home must be deficient to qualify for a

GRH loan. This will expand the eligibility of current homeowners and allow these potential customers to sell their current home and upgrade their housing. These existing homes will then provide homeownership opportunities for many other rural families, especially those in areas where housing is limited. Since the Agency does not communicate directly with many of the potential program customers, the Agency is interested in knowing if the proposed change in regulations will have a positive impact on rural homeownership. As such, the Agency is particularly interested in receiving comments on this issue.

#### Credit Qualifications

Credit qualifications will be revised to improve clarity and further define what constitutes an unacceptable credit history. This action will make the GRH program more consistent with the direct program and with industry standards.

- Incidents of more than one payment being 30 days or more late within the last 12 months has been changed to incidents of 3 or more payments late within the last 12 months.

- Incidents of rent payments being paid 30 days or more late within the last three years has been changed to incidents of rent payments being paid 30 days or more late within the last two years.

- Incidents where a foreclosure has been completed within the last 36 months has been adopted as an indicator of unacceptable credit. Previously, foreclosures had been listed as a category not to be considered as unacceptable credit, provided that the foreclosure was completed 12 months before the date of an application. The timeframe acceptable to the Agency for prior foreclosure incidents was increased from 12 months to 36 months due to risk associated with applicants with this type of credit history.

- The Agency has revised the section dealing with collection accounts by adding that if the collection account was paid in full within the last six months, it is considered an indicator of unacceptable credit. The purpose of this change is to discourage applicants from paying off collection accounts at the time of application only in order to qualify for Agency assistance.

- For non-Agency debts written off within the last 36 months, the Agency added the language "unless the account was paid in full at least 12 months ago." The purpose of this change was to discourage applicants paying in full debts previously written off only in order to qualify for Agency assistance.

The provision, under the current regulation, stating that "No History" of credit transactions is an acceptable credit history, has been deleted from the proposed regulation. The Agency feels that a lack of credit history should not automatically be considered acceptable credit. A recent study indicated that the highest delinquency rate in the first year of homeownership was attributed to customers who had no credit history prior to obtaining an Agency loan. This was particularly evident in customers who had resided with family prior to obtaining a mortgage loan and had no credit experience on their own. Based upon this study, the Agency does not believe that a lender evaluating an application from a family who has no experience in paying financial obligations can document that the customer has the capacity to repay the proposed loan. The handbook will clarify that "no credit history" on a credit report will not automatically be a reason to deny a loan since many creditors, such as landlords, utility companies, small department stores, and doctors, do not report to credit repositories. Detailed guidance concerning the evaluation of credit will be given to lenders in the handbook. The Agency feels that changes to the credit requirements and guidelines will assist lenders in evaluating applicants, help to ensure the success of the customer, and reduce risks to the Agency.

The provision to allow a lender to consider mitigating circumstances to establish a borrower's intent for good credit will be amended to be more consistent with the direct single family housing loan program and the private mortgage industry. Such flexibility will be added to cover the situation where a loan will significantly reduce the applicant's shelter costs and enhance debt repayment ability. The Agency hopes to benefit otherwise eligible applicants who have adverse credit due to high current shelter costs. The provision also will specify that mitigating circumstances will not be considered to provide loan assistance when the applicant is delinquent on a Federal debt or other Government outstanding judgment against the applicant in a Federal court, other than the United States Tax Court. These exceptions are based on statutory prohibitions in 31 U.S.C. 3720B and 28 U.S.C. 3201(e), respectively. The current provision for consideration of an applicant's justifiable dispute concerning goods or services as a mitigating circumstance also will be deleted as unnecessary. The broad

mitigating factor for circumstances of a temporary nature would cover this situation. The Agency is particularly interested in receiving comments on this issue, especially as to the parameters of when adverse credit may be mitigated.

#### Homeownership Education

The Agency is adopting a mandatory homeownership education requirement for first time homebuyers who have not previously owned a home, as authorized by 502(e)(4) of title V of the Housing Act of 1949. This will ensure that first-time homebuyers are adequately prepared for the obligations of homeownership. The Agency feels that this requirement will assist customers in understanding the responsibilities and demands of homeownership.

The Agency strongly believes that homeownership education is necessary for all first time homeowners. This is consistent with the direction of the lending industry and helps ensure the success of the homeowner and program while having the added benefit of minimizing losses to the Government and lender. However, the Agency recognizes the impact of this requirement upon the lending community and recognizes that in some cases, there may be a cost for this service and that the cost will generally be paid by the potential homeowner. The cost of homeownership education is an eligible loan purpose and can be included in the loan provided the appraised value of the property supports the inclusion of this fee. Alternatively, the cost may be paid directly by the applicant.

The Agency intends to establish minimum parameters for homeownership education in accordance with the standards currently being developed by the American Homeowner Education and Counseling Institute. The Agency believes there are two methods to ensure that homeownership education is provided. One method would be for the lender to maintain a list of acceptable providers of homeownership education and provide such list to potential clients. The lender would be responsible for ensuring that the providers met Agency requirements. A certification from the service provider would be required before the loan could be approved. An alternative method would be for the lender to provide the service, and if any costs are involved, each applicant would be charged the same fee. The Agency is particularly interested in comments on the parameters of an acceptable homeownership education program, whether one or both options

should be offered to lenders, alternative methods, and potential costs of such service. This rule will be amended to incorporate the standards as established.

#### Net Family Assets

A definition has been added for net family assets. Clarification as to which assets must be included in the calculation of annual income as well as assets which are not included in the calculation are included in the proposed regulation. The requirements of the Agency are consistent with the requirement of the U.S. Department of Housing and Urban Development in accordance with 24 CFR 5.603.

#### Subpart E—Underwriting the Property Ownership Requirements

The Agency proposes to increase the unexpired term on a secured leasehold interest from 40 years to 45 years before a guarantee will be considered. In the event of a foreclosure, leasehold interests must also be fully marketable in the area. The requirement for a lease to have an unexpired term of one and one-half times the term of the mortgage is considered to be industry standard, so that, in the event of a foreclosure, the loan will be fully marketable. This requirement helps to protect the lender as well as the Government. Should the term of the lease be less than the term of a 30 year mortgage, the value of the property would not be fully marketable and the value of the property would be decreased, thereby increasing the potential amount of a loss. Certain exceptions are provided on properties located on American Indian restricted lands due to the unique nature of securing loans in these areas.

#### Special Requirements for Condominiums

As the Agency does not approve subdivisions and condominiums, the proposed regulation stipulates that condominiums must be in a project approved or accepted by HUD, VA, Fannie Mae, or the Federal Home Loan Mortgage Corporation (Freddie Mac).

#### Special Requirements for Community Trust Lands

Language has been added to the proposed regulation outlining the requirements for guaranteed loans for dwellings on land owned by a community land trust. The Agency may guarantee a loan in these areas provided that any restrictions imposed by the community land trust are first reviewed and accepted by the Agency and that the requirements imposed by the community land trust automatically terminate upon foreclosure or

acceptance by the lender of a deed in lieu of foreclosure case. The Agency is concerned about possible discriminating language in community land trust restrictions. Current regulations do not address community land trusts.

#### Special Requirements for Planned Unit Developments

Clarification on loans for dwellings in Planned Unit Developments (PUD) have been added to the regulation. Such loans may be guaranteed if PUD meets all of the Agency's requirements and those of HUD, VA, Fannie Mae, or Freddie Mac. This issue is not addressed in the current regulation.

#### Special Requirements for Manufactured Homes

The Agency added a provision requiring the dealer-contractor to provide a warranty in accordance with 7 CFR part 1924, subpart A, identifying the unit by serial number. The dealer-contractor is also required to certify that the unit has not sustained any hidden damage during transportation and that the permanent foundation complies with plans and specifications. If the unit was manufactured in separate sections, the dealer-contractor must certify that the sections were properly joined and sealed per manufacturer's specifications. The dealer-contractor must also provide the applicant with a copy of all manufacturer's warranties. These provisions are similar to those in the direct 502 program and were added to protect the financial interests of the applicant, the lender, and the Government and to ensure that the dwelling is of acceptable quality.

To maintain consistency with the direct 502 program, the Agency will continue to finance only new manufactured homes that meet or exceed Agency thermal standards. The Agency has received comments regarding consideration of financing existing manufactured housing stock, not originally financed with an Agency loan. However, the Agency believes that cost to retrofit an existing manufactured home so it can meet Agency thermal standards is cost prohibitive and not in the best interest of the customer. The Agency is also concerned about other lender's experiences with higher losses on existing manufactured homes. Additionally, according to HUD research, as published in the "Ninth Report to Congress on the Manufactured Housing Program," manufactured homes over a 10 year exposure period are 5 times more likely to suffer structural failure as compared to a conventionally built home. HUD is expected to begin a review of the

manufactured construction code this year. After HUD completes this process and the Agency reviews its findings, the Agency will re-consider financing existing manufactured housing.

#### Subpart F—Regular Servicing

##### Servicing Responsibilities

The section on servicing has been expanded to include lender responsibilities. Language was added to allow the Agency to require a lender to transfer its loan servicing activities to another approved lender if the servicing lender fails to provide acceptable servicing.

##### Required Servicing Actions

The Agency wants to provide flexibility to lenders that do not have the capacity to escrow taxes and insurance. The Agency will allow these lenders the opportunity to submit a plan to the Agency for approval to ensure that the customer pays tax and insurance obligations. The lender, however, must accept ultimate responsibility for the payment of taxes and insurance which come due prior to liquidation of an account. This provision is intended to help expand the program into more rural areas with smaller lenders without escrow capabilities, while still protecting the borrower's interest.

A section on insurance has also been added and encompasses both the requirements for homeowners insurance and flood insurance on properties located in Special Flood Hazard Areas. This consolidated section on insurance eliminates the need for the current section of the regulation devoted to flood or mudslide hazard areas.

The Agency has added the requirement that the lender must notify a credit repository of each new guaranteed loan and must report to the credit repository all accounts that become more than 30 calendar days past due. This is consistent with industry standards. The current regulation only requires a lender to report a loan to a credit repository when payments become three payments delinquent and it does not require a lender to report new guaranteed loans.

##### Borrower Actions Requiring Lender Approval

Language has been added to allow a lender to consent to a lease of mineral rights as long as the security property remains suitable for a residence, the Government's interest will not be adversely affected, and Agency environmental requirements are met.

Additionally, the Agency proposes to allow a lender to consent to certain

transactions affecting the security property such as the sale or exchange of a portion of the security property, granting of a right-of-way across the property, or granting a partial release of the security property provided the transaction meets certain conditions to protect the lender and the Government's interests.

Under the current regulation, mineral leases and partial releases were not addressed. Under the proposed regulation, guidance is provided on allowing mineral leases and partial releases. This will give the lender more flexibility in servicing its guaranteed portfolio, while still protecting the Government's interest.

##### Transfer and Assumptions

The Agency has reorganized and clarified this section. A section on transfers, without triggering the due-on-sale clause, has been added to allow the transfer of property to a spouse or children not resulting from the death of a borrower, transfer to a relative, joint tenant, tenants by the entirety resulting from the death of a borrower, or transfer to an ex-spouse resulting from a divorce decree, legal separation agreement, or property settlement agreement. The addition of this section is in accordance with § 341 of the Garn-St Germain Depository Institutions Act of 1982 (Pub. L. 97-320).

#### Subpart G—Servicing Accounts With Repayment Problems

A section was added to the proposed regulation to clarify that lenders may enter into a forbearance agreement provided it includes a reasonable plan for bringing the account current.

The Agency eliminated the requirement for a lender to obtain prior Agency approval for protective advances. The Agency feels that lenders need the ability to immediately procure certain services to protect their interests as well as the interest of the Government. The time it takes a lender to obtain Agency approval for protective advances can increase exposure and could result in a higher cost to the Agency in the event of a loss. However, protective advances are to be used only to pay for emergency expenses necessary to protect the security property. Lenders will be allowed to provide a protective advance only to pay for emergency repairs needed to protect the security property only if the borrower is unable to secure an additional loan to pay these costs or if the borrower has abandoned the property. Additionally, a lender may advance funds to pay real estate taxes, local assessments, and hazard or flood

insurance premiums that are past due in order to protect the lender's interest. Only acceptable protective advances will be eligible for loss claim reimbursement. Specific guidance will be provided in the handbook to assist lenders in determining an acceptable protective advance.

#### Liquidation

A section on bankruptcy was added to inform lenders of the Agency's expectations in reasonably servicing an account in bankruptcy. The expectations of the Agency include: (a) The suspension of collection and foreclosure actions in accordance with the requirements of the Bankruptcy Code; and (b) when possible in a Chapter 7 bankruptcy, a reaffirmation agreement signed by the borrower and approved by the bankruptcy court prior to discharge, if the lender decides to continue with the borrower. Additionally, the lender may accept conveyance of the security property by the trustee in the bankruptcy if the bankruptcy court has approved the transaction and the lender will acquire title free and clear of all liens and encumbrances except the lender's liens.

The voluntary liquidation section has been enhanced to clarify that a lender may accept a request from a borrower to voluntarily liquidate the security property by way of refinancing or sale providing the price reflects at least the property's value as determined by a current market appraisal. The lender may also accept a deed in lieu of foreclosure unless the anticipated costs for selling the property, including any costs required to make the property salable, exceed the property's appraised value.

To ensure the Agency is in compliance with the Debt Collection Act and the Department of Treasury and Office of Management and Budget Circulars, a section was added to the proposed regulation to require the lender to report to the IRS and credit reporting agencies any debt that is settled through liquidation.

#### *Subpart H—Collecting on the Guarantee*

The section of the current regulation addressing loss payments has been broken down into several parts in order to clarify the Agency's policy on collection on the guarantee.

The Agency will no longer require lenders to submit a property disposition plan for approval prior to disposing of Real Estate Owned (REO) properties. However, the Agency will provide specific guidance in the handbook for disposition of REO property, sales price determinations, and price reductions.

By providing clear guidance to lenders for REO property disposition, the Agency feels that the efficiency and timeliness of the loss claim process will be enhanced, which in turn will reduce loss claim costs. This will also reduce unnecessary paperwork burden on the public. The Agency will monitor lender REO property disposition performance during servicing reviews.

The Agency has added a section on net recovery value. The section explains the difference between actual net recovery value and anticipated net recovery value. The difference between these two concepts is important to the lender in filing a claim for a loss under the terms of the guarantee. If the property has been sold at foreclosure or out of the lender's inventory, actual net recovery value is determined. However, if the property remains in the lender's inventory, the anticipated net recovery value is used in the loss claim calculation.

Current regulations allow a lender up to 6 months from the date they acquired the property to sell the property from inventory. The date acquired is considered the date of the foreclosure sale and does not take into account any applicable redemption period. If the property remains unsold after 6 months from the date of the foreclosure, a lender is required to submit a loss claim based on a liquidation appraisal. The change to this requirement will allow a lender 90 days to market the property after any required redemption period. Redemption periods vary from State to State and on average are approximately 6 months in length. This change will allow lenders in all States equal time to dispose of REO property, as some States have laws which provide a redemption period to allow a homeowner to redeem their property after a foreclosure sale.

If the property is located on Native American Indian trust or restricted land, the lender must notify the Agency if the property has not sold within 12 months of the foreclosure sale or from the end of any applicable redemption period, whichever is later. This extended time frame allows the lender extra flexibility to dispose of the REO due to restriction, which must be addressed when such properties are acquired.

#### List of Subjects

##### *7 CFR Part 1980*

Home improvement, Loan Programs-Housing and community development, Mortgage insurance, Mortgages, Rural areas.

##### *7 CFR Part 3555*

Administrative practice and procedure, Conflict of interests, Credit, Environmental impact statements, Equal credit opportunity, Fair Housing, Flood insurance, Home improvement, Housing, Loan programs-Housing and community development, Low and moderate income housing, Manufactured homes, Mortgage insurance, Mortgages, Rural areas, Subsidies.

For the reasons set forth in the preamble, Chapters XVIII and XXXV, title 7, Code of Federal Regulations are proposed to be amended as follows:

#### **CHAPTER XVIII—RURAL HOUSING SERVICE, RURAL BUSINESS-COOPERATIVE SERVICE, RURAL UTILITIES SERVICE, AND FARM SERVICE AGENCY, DEPARTMENT OF AGRICULTURE**

##### **PART 1980—GENERAL**

1. The authority citation for part 1980 continues to read as follows:

**Authority:** 5 U.S.C. 301; 7 U.S.C. 1989; 42 U.S.C. 1480.

##### **Subpart D—[Removed and Reserved]**

2. Subpart D of part 1980 is removed and reserved.

#### **CHAPTER XXXV—RURAL HOUSING SERVICE, DEPARTMENT OF AGRICULTURE**

3. Part 3555, consisting of subparts A through H, is added to read as follows:

#### **PART 3555—GUARANTEED RURAL HOUSING LOAN PROGRAM**

##### **Subpart A—General**

Sec.

- 3555.1 Applicability.
- 3555.2 Purpose.
- 3555.3 Civil Rights.
- 3555.4 Mediation and appeals.
- 3555.5 Environmental requirements.
- 3555.6 State and local law.
- 3555.7 Exception authority.
- 3555.8 Conflict of interest.
- 3555.9 Enforcement.
- 3555.10 Definitions.
- 3555.11–3555.50 [Reserved]

##### **Subpart B—Lender Participation**

- 3555.51 Lender eligibility.
- 3555.52 Lender approval.
- 3555.53 Contracting for loan origination.
- 3555.54 Sale of loans to approved lenders.
- 3555.55–3555.100 [Reserved]

##### **Subpart C—Loan Requirements**

- 3555.101 Loan purposes.
- 3555.102 Loan restrictions.
- 3555.103 Maximum loan amount.
- 3555.104 Loan terms.
- 3555.105 Interest assistance.
- 3555.106 Recapture.
- 3555.107 Application for and issuance of the loan guarantee.
- 3555.108–3555.150 [Reserved]



**Subpart D—Underwriting the Applicant**

- 3555.151 Eligibility requirements.  
 3555.152 Calculation of income and assets.  
 3555.153–3555.200 [Reserved]

**Subpart E—Underwriting the Property**

- 3555.201 Site requirements.  
 3555.202 Dwelling requirements.  
 3555.203 Ownership requirements.  
 3555.204 Security requirements.  
 3555.205 Special requirements for condominiums.  
 3555.206 Special requirements for community land trusts.  
 3555.207 Special requirements for Planned Unit Developments.  
 3555.208 Special requirements for manufactured homes.  
 3555.209–3555.250 [Reserved]

**Subpart F—Regular Servicing**

- 3555.251 Servicing responsibility.  
 3555.252 Required servicing actions.  
 3555.253 Late payment charges.  
 3555.254 Final payments.  
 3555.255 Borrower actions requiring lender approval.  
 3555.256 Transfer and assumptions.  
 3555.257 Unauthorized assistance.  
 3555.258–3555.300 [Reserved]

**Subpart G—Servicing Accounts With Repayment Problems**

- 3555.301 General policy.  
 3555.302 Forbearance.  
 3555.303 Protective advances.  
 3555.304 Reamortization.  
 3555.305 Liquidation.  
 3555.306–3555.350 [Reserved]

**Subpart H—Collecting on the Guarantee**

- 3555.351 Loan guarantee limits.  
 3555.352 Loss covered by the guarantee.  
 3555.353 Net recovery value.  
 3555.354 Loss claim procedures.  
 3555.355 Reducing or denying the claim.  
 3555.356 Future recovery.  
 3555.357–3555.400 [Reserved]

**Authority:** 5 U.S.C. 301; 42 U.S.C. 1471 *et seq.*

**Subpart A—General****§ 3555.1 Applicability.**

This part sets forth policies for the Guaranteed Rural Housing Loan Program operated by the Rural Housing Service. It addresses the requirements of section 502(h) of the Housing Act of 1949, as amended, and includes policies regarding originating, servicing, holding and liquidating guaranteed loans. Any provision regarding the expenditure of funds under this part is contingent upon the availability of funds.

**§ 3555.2 Purpose.**

The purpose of the guaranteed rural housing loan program is to provide low- and moderate-income persons who will live in rural areas with an opportunity to own adequate but modest, decent, safe, and sanitary dwellings and related facilities. The program offers persons

who do not currently own adequate housing the opportunity to acquire, build, rehabilitate, improve, or relocate dwellings in rural areas. The program provides guarantees only for qualified loans that a lender would not make without a guarantee.

**§ 3555.3 Civil rights.**

The Agency, lenders, and their agents must administer the program fairly, and in accordance with both the letter and the spirit of all equal opportunity, equal credit opportunity and fair housing legislation, and applicable executive orders. Loan guarantees, services, and benefits provided under this part shall not be denied to any person based on race, color, national origin, sex, religion, marital status, familial status, age (provided the applicant has the capacity to enter into a binding contract), handicap, receipt of income from public assistance, sexual orientation, or because the applicant has, in good faith, exercised any right under the Consumer Credit Protection Act (15 U.S.C. 1601 *et seq.*). All activities under this part shall be accomplished in accordance with the Fair Housing Act (42 U.S.C. 3601–3620), and Executive Order 11063 as amended by Executive Order 12259, as applicable. The Agency's civil rights compliance requirements are provided in 7 CFR 1901, subpart E.

**§ 3555.4 Mediation and appeals.**

Whenever the Agency makes a decision that will adversely affect a participant, the participant may proceed with alternative dispute resolution including mediation and a USDA National Appeals Division hearing in accordance with part 11 of this title. The participant also may request an informal review of the situation with the decision maker. Except when the adverse decision applies to a loss claim, the applicant or borrower and the lender must participate jointly in the appeal process. Decisions made by the lender cannot be appealed unless concurrence by the Agency was required by this subpart and obtained by the lender.

**§ 3555.5 Environmental requirements.**

(a) *Policy.* The Agency will consider environmental quality as equal with economic, social, and other relevant factors in program development and decision-making processes. The Agency will take into account potential environmental impacts of proposed projects by working with applicants, other Federal agencies, American Indian tribes, State and local governments, and interested citizens and organizations in order to formulate actions that advance the program's goals in a manner that

will protect, enhance, and restore environmental quality.

(b) *Regulatory references.* Loan processing and servicing actions under this part will be completed in accordance with the requirements of part 1940, subpart G of this title, which addresses environmental requirements; part 1924, subpart A of this title, which addresses lead-based paint requirements; and part 1806, subpart B of this title, which addresses flood insurance.

**(c) Agency responsibilities.**

Responsibility for compliance with the National Environmental Policy Act and with the Agency's environmental regulations rests with the Agency, not the guaranteed lender.

(d) *Lender and applicant responsibilities.* (1) On an as needed basis, lenders and applicants will assist the Agency in obtaining such information as the Agency needs to complete its environmental review and to cooperate in the resolution of environmental problems.

(2) Lenders will become familiar with Agency environmental requirements, so they can advise applicants and reduce the probability of unacceptable applications being submitted to the Agency.

(3) The applicant must obtain flood insurance offered under the National Flood Insurance Act of 1968 if the dwelling is located in an area identified by FEMA as having special flood hazards.

(4) The lender must determine whether the dwelling is located in a special flood hazard area, and if so, ensure that the borrower maintains acceptable flood insurance throughout the term of the loan.

**§ 3555.6 State and local law.**

Lenders will comply with applicable State and local laws and regulations, including the laws of American Indian tribes. Supplemental guidance will be issued in the case of any conflict with or significant differences from provisions of this part.

**§ 3555.7 Exception authority.**

The Administrator of the Agency, or a designee, may make an exception to any requirement or provision of this part or to address any omissions in this part, when the Administrator determines that application of the requirement or provision, or failure to take action in the case of an omission, would adversely affect the Government's interest.

**§ 3555.8 Conflict of interest.**

(a) *Applicant or borrower responsibility.* The applicant or



borrower must disclose to the lender any prohibited relationship or association with any Rural Development employee, and the lender must disclose that information to the Agency.

(b) *Lender responsibility.* The lender must disclose to the Agency any prohibited relationship or association it, or any of its employees, has with any Rural Development employee.

(c) *Prohibited relationships and associations.* Prohibited relationships and associations include the following:

(1) Immediate family members, including parents and children, whether related by blood or marriage, and any household residents;

(2) Close relatives, including grandmother, grandfather, aunt, uncle, sister, brother, niece, nephew, granddaughter, grandson, or first cousin, whether related by blood or marriage;

(3) Immediate working relationships, including coworkers in the same office, subordinates, and immediate supervisors; and

(4) Close business associations, including business partnerships, joint ventures, or closely-held corporations.

(d) *Result of disclosure.* Disclosure of prohibited relationships and associations under this section will not result in applicant, borrower or lender ineligibility. Disclosures may result in reassignment of Rural Development employees with regard to the loan guarantee in question so that no prohibited relationships or associations exist between the Rural Development employees responsible for loan guarantee transactions and lenders, borrowers, or applicants.

#### **§ 3555.9 Enforcement.**

The Agency will take such actions as are appropriate and necessary to enforce the provisions of these regulations. Such actions will include, but not be limited to, reduction of the loss claim payment; termination of the guarantee agreement or any loan servicing agreement; suspension and debarment of participation in this or other Agency programs; and any other appropriate administrative, civil, or criminal actions.

#### **§ 3555.10 Definitions.**

The definitions in this section apply to this part.

*Acceleration.* Demand for immediate repayment of the entire balance of a debt if the covenants in the promissory note, assumption agreement, or security instruments are breached.

*Adjusted income.* Income from all household members, which is used to determine whether an applicant is income-eligible for a guaranteed loan, or

interest assistance, if applicable. Adjusted income provides for deductions to account for varying household circumstances and expenses. See § 3555.152 for a complete description of adjusted income.

*Agency.* The Rural Housing Service of the U.S. Department of Agriculture, or its successor agency, formerly the Rural Housing and Community Development Service, a successor agency to the Farmers Home Administration.

*Agency employee.* Any employee of the Rural Housing Service, or any employee of the Rural Development mission area who carries out section 502 guaranteed loan program functions.

*Alien.* See "Qualified alien."

*American Indian Restricted Land.* Land or any interest in land which is held by an individual American Indian or tribe, including any band, rancheria, colony, pueblo, group, community or nation of Indians or Alaska Natives, and is subject to Federal restrictions against alienation or encumbrance.

*Amortized payment.* Equal monthly payments under a fully amortized mortgage loan that provides for the scheduled payment of interest and principal over the term of the loan.

*Annual income.* The income of all household members from all sources except those listed in § 3555.152(b).

*Applicant.* An individual applying to a lender for a guaranteed loan.

*Area Median Income.* The median income in a specific locality; typically a County or Metropolitan Statistical Area (MSA) as determined by the Department of Housing and Urban Development

*Assumption.* The procedure whereby title to a security property is transferred to an eligible transferee who agrees to assume the obligations of the loan; however, the transferor remains liable.

*Borrower.* An individual who has received a loan guaranteed under the guaranteed rural housing loan program.

*Community land trust.* A private nonprofit community housing development organization that is established to acquire parcels of land, held in perpetuity, primarily for conveyance under long-term ground leases.

*Conditional commitment.* The Agency's agreement that a proposed loan will be guaranteed if all conditions and requirements established by the Agency are met.

*Condominium.* A form of fee ownership of whole units or separate portions of multi-unit buildings under the laws of the State where the property is located which provides the mechanics and facilities for formal filing and recording of a divided interest in real property, where the division is

vertical as well as horizontal. Fee ownership of the units in a multi-unit property and joint ownership of the common areas.

*Dealer-contractor.* A person, firm, partnership, or corporation capable of providing complete services for selling, servicing and developing sites for manufactured homes.

*Debarment.* An action taken under part 3017 of this title or title 48 of the Code of Federal Regulations to exclude a person or entity from participating in Federal programs.

*Deficient housing.* A dwelling that lacks complete plumbing; lacks adequate heating; is dilapidated or structurally unsound; has an overcrowding situation that will be corrected with loan funds; or that is otherwise uninhabitable, unsafe, or poses a health or environmental threat to the occupant or others.

*Disability, person with.* See "Person with a disability."

*Dwelling.* A house, manufactured home, or condominium unit, and related facilities, such as a garage or storage shed.

*Elderly family.* An elderly family consists of one of the following:

(1) A person who is the head, spouse, or sole member of a household and who is 62 years of age or older, or who is disabled, and is an applicant or borrower;

(2) Two or more persons who are living together, at least one of whom is age 62 or older, or disabled, and who is an applicant or borrower; or

(3) Where the deceased borrower or spouse in a household was at least 62 years old or disabled, the surviving household member shall continue to be classified as an elderly household for the purpose of determining adjusted income, even though the surviving members may not meet the definition of an elderly household on their own, provided:

(i) They occupied the dwelling with the deceased household member at the time of the death;

(ii) If one of the surviving household members is the spouse of the deceased household member, the surviving household shall be classified as an elderly family only until the remarriage or death of the surviving spouse; and

(iii) At the time of the death of the deceased household member, the dwelling was financed with a guaranteed Rural Housing loan.

*Escrow account.* An account to which the borrower contributes monthly payments to cover the anticipated costs of real estate taxes, hazard and flood insurance premiums, and other related costs.

*Existing dwelling.* A dwelling that is more than one year old, or less than one year old and covered by an approved ten-year warranty.

*False information.* For the purpose of this part only, information that the borrower or lender knew or should have known was incorrect and that was provided or omitted for the purpose of obtaining assistance.

*FEMA.* The United States Federal Emergency Management Agency.

*FHA.* The Federal Housing Administration of the United States Department of Housing and Urban Development.

*First-time homebuyer.* Individuals who meet any one of the following three criteria are considered first-time homebuyers.

(1) An individual who has had no ownership interest in a principal residence during the three-year period ending on the date of loan closing.

(2) An individual who is a displaced homemaker and who, except for owning a home with a spouse, has had no ownership interest in a principal residence during the three-year period ending on the date of loan closing. Displaced homemakers include any individual who is:

- (i) An adult;
- (ii) Unemployed or underemployed;
- (iii) Experiencing difficulty in obtaining or upgrading employment; and
- (iv) In recent years has worked primarily without remuneration to care for the home and family, but has not worked full-time, full-year in the labor force.

(3) An individual who is a single parent and who, except for owning a home with a spouse, has had no ownership interest in a principal residence during the three-year period ending on the date of loan closing. Single parents include any individual who is:

- (i) Unmarried or legally separated from a spouse; and
- (ii) Has custody or joint custody of one or more children, or is pregnant.

*Floor interest rate.* The rate of interest, determined at the time of loan closing, that the borrower would pay if the note were amortized at the rate corresponding to the borrower's income range as determined in accordance with § 3555.105(b).

*Forbearance agreement.* An agreement between the lender and the borrower providing for temporary suspension of payments or a repayment plan that calls for periodic payments of less than the normal monthly payment, periodic payments at different intervals, etc. to bring the account current.

*Freddie Mac.* Federal Home Loan Mortgage Corporation.

*Full-time student.* A person who carries at least the minimum number of credit hours considered to be full-time by the university, college, or vocational school in which the person is enrolled.

*Funded buydown account.* An escrow account funded by the lender, seller, or through a third party gift, from which monthly payments are released directly to the lender to reduce the amount of interest on a loan, thereby improving an applicant's repayment ability.

*Guaranteed loan.* A loan guaranteed under section 502 of the Housing Act of 1949. Under the guarantee, the owner of the loan note may be reimbursed for all or part of a loss incurred if a borrower defaults on a loan.

*Household.* All persons expected to be living in the dwelling as principal residence, except for live-in aides, foster children, and foster adults.

*Housing Act of 1949.* The Act which, in part, provides the authority for single family housing programs, codified at 42 U.S.C. 1471, *et seq.*

*HUD.* The United States Department of Housing and Urban Development.

*Interest assistance.* Agency assistance available to eligible borrowers that reduces the effective interest rate on the guaranteed loan.

*IRS.* The Internal Revenue Service of the United States Department of the Treasury.

*Lender.* The entity making, holding, or servicing a loan that is guaranteed under the provisions of this part.

*Live-in aide.* A person who lives with an elderly or disabled person and is essential to that person's care and well-being, not obligated for the person's support, and would not be living in the unit except to provide the support services.

*Low-income.* An adjusted income that is greater than the HUD established very low-income limit, but that does not exceed the HUD established low-income limit (generally 80 percent of median income adjusted for household size) for the county or Metropolitan Statistical Area where the property is or will be located.

*Manufactured home.* A structure that is built to Federally Manufactured Home Construction and Safety Standards and the Agency's Thermal Performance Standards. It is transportable in one or more sections, which in the traveling mode is ten-body feet (3.048 meters) or more in width, and when erected on site is 400 or more square feet (37.16 square meters), and which is built on a permanent chassis and designed to be used as a dwelling with or without a permanent foundation

when connected to the required utilities. It is designed and constructed for permanent occupancy by a single family and contains permanent eating, cooking, sleeping, and sanitary facilities. The plumbing, heating, and electrical systems are contained in the structure. A permanent foundation is required.

*Market value.* The value of the property as determined by a current appraisal made in accordance with the Uniform Standards of Professional Appraisal Practices.

*Median income.* The area median income, adjusted for family size, as established by HUD.

*Moderate income.* An adjusted income that is greater than the HUD-established low-income limit, but that does not exceed 115 percent of median income adjusted for household size for the county or Metropolitan Statistical Area where the property is or will be located.

*Modest housing.* A property that is considered modest for the area, with a cost that does not exceed the applicable limit established under section 203 (b) of the National Housing Act (12 U.S.C. 1709). In addition, the property must not be designed for income-producing activities or have an in-ground swimming pool.

*Mortgage.* A form of security instrument or consensual lien on real property including a real estate mortgage and a deed of trust.

*Mortgage Credit Certificates.* A credit to reduce the applicant's Federal income tax liability, which improves an applicant's repayment ability.

*Net family assets.* The value of assets available to a household, as contained in § 3555.152(d).

*Net recovery value.* The amount available to apply to the outstanding principal balance after considering the value of the security property and other amounts recovered, and deducting the costs associated with liquidation, acquisition and sale of the property. Net recovery value is calculated differently depending on the type of disposition, as contained in § 3555.353.

*New dwelling.* A dwelling that is to be constructed, or an already-existing dwelling that is less than one year old and is not covered by an approved ten-year warranty.

*Participant.* For the purpose of appeals, a participant is any individual or entity that has applied for, or whose right to participate in or receive a payment, loan guarantee, or other benefit, is affected by an Agency decision and meets the definition of "participant" in § 11.1 of this title.

*Person with a disability.* Any person who has a physical or mental impairment that substantially limits one or more major life activities, including functions such as caring for one's self, performing manual tasks, walking, seeing, hearing, speaking, breathing, learning and working, has a record of such an impairment, or is regarded as having such an impairment.

*PITI ratio.* The amount to be paid by the borrower for principal, interest, taxes, and insurance (PITI), divided by repayment income. This is often known as the "front-end ratio."

*Planned Unit Development.* For the purpose of this definition, a Condominium is not a Planned Unit Development (PUD). A PUD is a development that has all of the following characteristics:

(1) The individual unit owners own a parcel of land improved with a dwelling. This ownership is not in common with other unit owners;

(2) The development is administered by a homeowners association that owns and is obligated to maintain property and improvements within the development (for example, greenbelts, recreation facilities and parking areas) for the common use and benefit of the unit owners; and

(3) The unit owners have an automatic, nonseverable interest in the homeowners association and pay mandatory assessments.

*Prior lien.* A lien against the security property that is superior in right to the lender's debt instrument.

*Property.* The land, dwelling, and related facilities for which the applicant will use guaranteed funds.

*Qualified alien.* An alien who, at the time the alien applies for, receives, or attempts to receive Federal public benefit, in accordance with the Immigration and Nationality Act, is:

(1) An alien who is lawfully admitted for permanent residence;

(2) An alien who is granted asylum;

(3) A refugee who is admitted to the United States;

(4) An alien who is paroled into the United States for a period of at least 1 year;

(5) An alien whose deportation is being withheld; or

(6) An alien who is granted conditional entry prior to April 1, 1980.

*Real estate taxes.* Taxes and the annual portion of assessments estimated to be due and payable on the property.

*Recapture.* The amount of interest assistance to be repaid when the borrower transfers title or ceases to occupy the property.

*Recipient.* Any person or entity that receives benefits or assistance under the

guaranteed loan program, including a lender that receives a loan guarantee, or a borrower who receives a guaranteed loan or interest assistance.

*REO.* (Real Estate Owned) Real estate that formerly served as security for a guaranteed loan and for which the lender holds title.

*Repayment income.* Used to determine whether an applicant has the ability to make monthly loan payments. Repayment income may include amounts excluded for the purpose of determining adjusted income. See § 3555.152(a) for a complete description of repayment income.

*Rural area:* A rural area is any one of the following:

(1) Open country which is not part of or associated with an urban area.

(2) Any town, village, city, or place, including the immediately adjacent densely settled area, which is not part of or associated with an urban area and which:

(i) Has a population not in excess of 10,000 if it is rural in character; or

(ii) Has a population in excess of 10,000 but not in excess of 20,000, is not contained within a Metropolitan Statistical Area, and has a serious lack of mortgage credit for low-and moderate-income households as determined by the Secretary of Agriculture and the Secretary of HUD.

(3) An area classified as a rural area prior to October 1, 1990 (even if within a Metropolitan Statistical Area), with a population exceeding 10,000, but not in excess of 25,000, which is rural in character, and has a serious lack of mortgage credit for low-and moderate-income families. This is effective through receipt of census data for the year 2000.

*Rural Development.* A mission area within USDA which includes the Rural Housing Service, Rural Utilities Service, and Rural Business-Cooperative Service.

*Scheduled payment.* The monthly installment on a promissory note plus escrow payments, as modified by any interest assistance agreement or forbearance agreement.

*Secured loan.* A loan that is collateralized by property so that in the event of a default on the loan, the property may be sold to pay down the debt.

*Security instrument.* The mortgage or deed of trust that secures the promissory note or assumption agreement.

*Security property.* All the property that serves as collateral for a guaranteed loan.

*Supplemental loan.* A guaranteed loan made in conjunction with a transfer and assumption to provide funds to complete the transaction.

*Suspension.* An action taken under part 3017 of this title or title 48 of the Code of Federal Regulations to exclude a person or entity from participation in Federal programs for a temporary period, pending completion of an investigation of wrongdoing.

*Total debt ratio.* The amount paid by the borrower for PITI and any recurring monthly debt, divided by repayment income. This is often known as the "back-end ratio."

*Unauthorized assistance.* Any guaranteed loan or interest assistance for which there was no regulatory or statutory authorization, or for which the borrower was not eligible.

*United States citizen.* An individual who resides as a citizen in any of the 50 States, the District of Columbia, the Commonwealth of Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, the Commonwealth of the Northern Marianas, the Federated States of Micronesia, the Republic of Palau, or the Republic of the Marshall Islands.

*USDA.* The United States Department of Agriculture.

*VA.* The United States Department of Veterans Affairs.

*Value appreciation.* The current market value of the property minus the balance due prior lienholders (if any), the unpaid balance of the debt, unreimbursed closing costs (if any), principal reduction, the original equity (if any) of the borrower, and the value added by capital improvements.

*Veterans preference.* A preference extended to any person applying for a loan guarantee under this part who served on active duty and has been discharged or released from the active forces on conditions other than dishonorable from the United States Army, Navy, Air Force, Marine Corps, or Coast Guard. The preference applies to the service person, or the family of a deceased serviceperson who died in service before the termination of such war or such period or era. The applicable time frames are:

(1) During the period of April 6, 1917, through March 31, 1921;

(2) During the period of December 7, 1941, through December 31, 1946;

(3) During the period of June 27, 1950, through January 31, 1955;

(4) For a period of more than 180 days, any part of which occurred after January 31, 1955, but on or before May 7, 1975; or

(5) During the period beginning August 2, 1990, and ending the date prescribed by Presidential Proclamation or law.

**§§ 3555.11–3555.50 [Reserved]****Subpart B—Lender Participation****§ 3555.51 Lender eligibility.**

To be approved to participate in the Guaranteed Rural Housing Loan Program, a lender must meet the requirements described in this section.

(a) *Ability to underwrite and service loans.* The lender must have a demonstrated ability to underwrite and service single family loans. A lender will be considered to have such a demonstrated ability if it qualifies as one of the following:

- (1) A State Housing Agency;
- (2) A lender approved as a supervised or nonsupervised mortgagee by the HUD with direct endorsement authority for submission of applications for Federal Housing Mortgage Insurance;
- (3) A lender approved as a supervised or nonsupervised mortgagee by VA with authority to close loans on the automatic basis;
- (4) A lender approved by Fannie Mae for single family loans;
- (5) A lender approved by Freddie Mac for single family loans;
- (6) A Farm Credit System institution that provides documentation of its ability to underwrite and service single family loans;

(7) A lender participating in other Rural Development or Farm Service Agency guaranteed loan programs that provides documentation of its ability to underwrite and service single family loans; or

(8) A Federally-supervised lender that provides documentation of its ability to underwrite and service single family loans. Acceptable sources of supervision include:

- (i) Being a member of the Federal Reserve System;
- (ii) The Federal Deposit Insurance Corporation (FDIC);
- (iii) The National Credit Union Administration (NCUA); or
- (iv) The Office of Thrift Supervision (OTS).

(b) *Program participation requirements.* Lenders and their agents must comply with the following requirements:

- (1) Keep up to date on, and comply with, all Agency regulations;
- (2) Cooperate fully with Agency reporting and monitoring processes;
- (3) Comply with limitations on loan purposes, loan limitations, interest rates, and loan terms;
- (4) Inform the Agency in advance of any sale, transfer, or change of servicers of any Agency guaranteed loan;
- (5) Maintain reasonable and prudent business practices;

(6) Remain responsible for servicing even if servicing has been contracted to a third party;

(7) Use Rural Development, HUD, Fannie Mae, or Freddie Mac forms;

(8) Maintain eligibility under paragraph (a) of this section;

(9) Notify the Agency if there are any material changes in organization or practices;

(10) Remain in good standing, and neither debarred nor suspended from participation in Federal programs;

(11) Notify the Agency in the event of bankruptcy or insolvency of the lender;

(12) Remain free from default and delinquency on any debt owed to the Federal government;

(13) Maintain a fidelity and omissions policy consistent with the volume of loans originated, and listing the Agency as the loss payee; and

(14) Allow the Agency or any Agency's representative access to the lender's records, including on-site reviews of the lender's operation and the operations of any agent of the lender, for the purpose of verifying compliance with Agency regulations and guidelines.

**§ 3555.52 Lender approval.**

(a) *Initial approval.* The lender must apply for and receive approval from the Agency to participate in the program.

(b) *Termination of approval.* Once approved, the lender will remain eligible to participate in the program unless the Agency determines that one of the following has occurred.

(1) *Lapse of any eligibility requirement.* In the event that a lender fails to comply with any of the requirements described in § 3555.51, the lender must notify the Agency immediately. The Agency will determine whether the change warrants termination of the lender's approval.

(2) *Unsatisfactory lender performance or Government convenience.* If the Agency determines that continued lender approval is not in the best interest of the Government, the Agency may terminate the lender's approval.

(3) *Voluntary withdrawal.* The lender may choose to end participation in the program at any time.

(c) *Results of termination of approval or withdrawal from the program.* If the Agency terminates a lender's approval or the lender withdraws from the program, the Agency may:

(1) Require that the lender transfer servicing of its loans to an approved lender; and

(2) Pursue additional actions including, but not limited to, suspension or debarment.

**§ 3555.53 Contracting for loan origination.**

Lenders may contract with brokers, nonapproved lenders, or other loan originators for loan origination services, closing services, or both, provided the loan is transferred immediately after closing to the approved lender to which the guarantee will be issued. The approved lender is responsible for underwriting the loan, obtaining the conditional commitment, and ensuring that the loan is properly closed.

**§ 3555.54 Sale of loans to approved lenders.**

Lenders may sell guaranteed loans only to other Agency approved lenders, Fannie Mae, or Freddie Mac. In such a sale, the purchasing lender acquires all rights of the selling lender under the loan note guarantee, and assumes all of the selling lender's obligations contained in any note, security instrument, or loan note guarantee in connection with the loan purchased. The purchasing lender will be subject to any defenses, claims, or offsets that the Agency would have had against the selling lender if the selling lender had continued to hold the loan. The lender must notify the Agency immediately upon the sale or transfer of servicing of a loan.

**§§ 3555.55–3555.100 [Reserved]****Subpart C—Loan Requirements****§ 3555.101 Loan purposes.**

Guaranteed loan funds must be used to acquire a new or existing dwelling to be used by the applicant as a principal residence.

(a) Loan funds may be used for:

- (1) The construction of a new dwelling;
- (2) The cost of acquisition of an existing dwelling;
- (3) The cost of repairs associated with the acquisition of an existing dwelling; or
- (4) Acquisition and relocation of an existing dwelling.

(b) Loan funds also may be used to pay for the following items.

- (1) Reasonable and customary expenses related to obtaining the loan, including:
  - (i) Legal, architectural, and engineering fees;
  - (ii) Title clearance, title insurance, and loan closing costs;
  - (iii) Transfer taxes and recordation fees;
  - (iv) Appraisal, surveying, environmental, tax monitoring, and technical services;
  - (v) Reasonable and customary lender fees and charges;

(vi) For low-income borrowers only, reasonable and customary loan discount points; and

(vii) Homeownership education, for first-time homebuyers only.

(2) Special design features or equipment when necessary because of a physical disability of the applicant or a member of the household.

(3) Reasonable connection fees, assessments, or the pro rata installment costs for utilities such as water, sewer, electricity and gas for which the borrower is responsible.

(4) The prorated portion of real estate taxes that are due and payable on the property at the time of closing and for the establishment of escrow accounts for real estate taxes, hazard and flood insurance premiums, and related costs.

(5) Purchase and installation of essential equipment in the dwelling, including but not limited to: ranges, refrigerators, washers, and dryers.

(6) Purchase and installation of energy-saving measures.

(7) Site preparation including grading, foundation plantings, seeding or sodding, trees, walks, yard fences, and driveways to a building site.

(8) A supplemental loan to provide funds for seller equity or essential repairs when an existing guaranteed loan is assumed simultaneously.

(c) Refinancing is permitted only in the following situations:

(1) The loan may be used for permanent financing when financing to construct a new dwelling, or to improve an existing dwelling, is arranged as a part of the loan package.

(2) In the case of loans for a site without a dwelling, refinancing is permitted if:

(i) The debt to be refinanced was incurred for the sole purpose of purchasing the site;

(ii) The applicant is unable to acquire adequate housing without refinancing; and

(iii) An appropriate dwelling has been constructed on the site.

**§ 3555.102 Loan restrictions.**

A guarantee will not be issued if loan funds are to be used for:

(a) Purchase of an existing manufactured home, except as provided in § 3555.208(b)(3);

(b) Purchase or improvement of income-producing land or buildings to be used principally for income-producing purposes;

(c) Loan discount points, except as provided in § 3555.101(b)(1)(vi);

(d) Refinancing, except as provided in § 3555.101(c); or

(e) Payments on a lease.

**§ 3555.103 Maximum loan amount.**

The amount of the loan must not exceed the lesser of:

(a) The maximum dollar limitation provided in section 203(b)(2) of the National Housing Act of 1949, (12 U.S.C. 1702); or

(b) The market value of the property.

**§ 3555.104 Loan terms.**

(a) *Interest rate.* The loan must be written at an interest rate that is fixed over the term of the loan and shall be negotiated between the lender and borrower. In no case may the maximum interest rate exceed the maximum rate published by the Agency through a Notice in the **Federal Register**.

(b) *Repayment period.* The loan term will be 30 years.

(c) *Repayment schedule.* Amortized payments will be due and payable monthly.

(d) *Negative amortization.* The loan note must not provide for interest on interest.

**§ 3555.105 Interest assistance.**

Subject to the availability of funds, the Agency may provide interest assistance to eligible borrowers.

(a) *Eligibility for interest assistance.*

(1) Borrowers whose loan was approved as a subsidized guaranteed loan between April 17, 1991, and September 30, 1991, and executed Form RD 1980-12, "Master Interest Assistance and Shared Equity Agreement With Promissory Note," at loan closing, are eligible to receive interest assistance if they:

(i) Have not sold or transferred the property;

(ii) Occupy the property as a principal residence; and

(iii) Qualify for at least \$20.00 per month interest assistance.

(2) If a borrower ceases to receive interest assistance, they must have an adjusted household income that is at or below the applicable low-income limit in order to qualify to receive interest assistance again.

(b) *Floor interest rate.* The floor interest rate is determined by comparing the household's adjusted income to the adjusted median income for the area in which the security property is, or will be, located. The following chart is used to determine the floor interest rate paid by households that receive interest assistance.

PERCENTAGE OF MEDIAN INCOME AND THE FLOOR INTEREST RATE

[Figures are in percents]

When the adjusted income for the household is—		Then the floor interest rate is <sup>1</sup>	High cost area floor interest rate is
Equal to or more than	But less than		
0 .....	60% of adjusted median income .....	3	3
60 .....	65% of adjusted median income .....	4	3
65 .....	70% of adjusted median income .....	5	4
70 .....	75% of adjusted median income .....	6	5
75 .....	80% of adjusted median income .....	7	6
80 .....	90% of adjusted median income .....	8	7
90 .....	100% of adjusted median income .....	9	8
100 .....	110% of adjusted median income .....	10	9
110 .....	115% of adjusted median income .....	11	10
115% of adjusted median income .....		12	11

<sup>1</sup> Or note rate, whichever is less; in no case will the floor interest rate be less than 3 percent.

(c) *High cost area.* (1) A borrower who received a loan in a designated high cost area will be granted an additional 1 percent interest assistance in order to

assist the borrower in obtaining financial assistance.

(2) The change in designation to (or from) a high cost area will not affect existing loans.

(3) A borrower's loan eligibility for high cost designation is determined at the time of issuance of the Conditional Commitment for the loan guarantee.

(d) *Annual interest assistance review.*

(1) The lender must review annually each borrower's eligibility for continued interest assistance and determine the appropriate level of assistance. As part of renewal for interest assistance, borrowers must submit documentation requested for the review, and must continue to occupy the property as a principal residence.

(2) If the renewal is not completed before the expiration date of the existing agreement, the effective date of the renewal will be either the expiration date of the previous agreement if an Agency or lender error caused the delay, or the next due date after the renewal is approved in all other cases.

(3) The borrower must notify the lender whenever household income increases by \$100 or more per month. The household may also report decreases in income of \$100 or more per month and which may result in the borrower being eligible for at least an additional \$20 interest assistance per month. If the change in the household's income will cause the payment for principal and interest to change, the household's interest assistance may be adjusted for a new 12-month period. The new agreement will be effective on the due date following the date the borrower's information is verified by the lender.

(e) *Processing fee.* The Agency will pay the lender a fee for each Interest Assistance Agreement processed, unless the Interest Assistance Agreement was incorrect due to the lender's error.

(f) *Overpayment of interest assistance.* When the lender becomes aware of circumstances that have resulted in an overpayment of interest assistance for any reason, the following actions will be taken:

- (1) The lender must immediately notify the borrower and the Agency;
- (2) The interest assistance agreement will be corrected; and
- (3) A repayment agreement acceptable to the Agency will be reached.

(g) *Cancellation of interest assistance.* The lender must notify the Agency that the borrower no longer qualifies for interest assistance if:

- (1) The borrower ceases to occupy the property;
- (2) The security property is sold or title to the property is transferred; or
- (3) The borrower qualifies for interest assistance of less than \$20 per month.

(h) *Assumed loans.* Loans which were approved as subsidized guaranteed loans between April 17, 1991, and September 30, 1991, and are assumed by a new borrower are not eligible for interest assistance regardless of the income of the new owner.

**§ 3555.106 Recapture.**

Borrowers with guaranteed loans may be required to repay interest assistance. Amounts to be recaptured are due and payable when the borrower transfers title or ceases to occupy the property. If an entity other than the Agency provides assistance to a borrower and requires recapture, the Agency will collect its recapture amounts prior to recapture by the other entity.

(a) *Amount to be recaptured.* The maximum amount to be recaptured is the lesser of:

- (1) The amount of interest assistance received; or
- (2) 50 percent of the value appreciation.

(b) *Assumed loans.* When a loan subject to recapture is assumed, the recapture amount must be paid in full by the seller, unless title is transferred and the loan is assumed under § 3555.256(d). Under this exception, recapture amounts will not be due at the time the loan is assumed; however, when the new borrower transfers title or ceases to occupy the property, all interest assistance subject to recapture before and after the assumption must be paid in full.

**§ 3555.107 Application for and issuance of the loan guarantee.**

(a) *Processing of applications.* In general, the Agency will process loan guarantee applications in the order that completed applications are received.

(1) When funding is not available, applications will be placed on a waiting list, with priority given to applications submitted on behalf of first-time homebuyers.

(2) In the case of applications with equivalent priority status that are received on the same day, preference will be given to those qualifying for veteran's preference.

(b) *Appraisals.* The lender must supply, as part of the application package, a current appraisal of the property for which the guarantee is requested. Appraisals must be conducted in accordance with the Uniform Standards of Professional Appraisal Practices.

(c) *Environmental requirements.* The lender will meet all its responsibilities in accordance with § 3555.5.

(d) *Issuance of a conditional commitment.* The lender must demonstrate that all the general loan, applicant, and site requirements of this part are met before the Agency will issue a conditional commitment.

(e) *Loan guarantee fee.* The lender must pay a fee of up to 1 percent of the loan amount, the cost of which may be passed on to the borrower. Once the

guarantee has been issued, the fee will not be refunded.

(f) *Proper closing.* The lender must ensure that any loan to be guaranteed is properly closed using documents acceptable to the Agency.

(g) *Issuance of the guarantee.* The loan guarantee does not take effect until:

- (1) The lender transmits the required guarantee fee in accordance with § 3555.107(e), the lender certification form provided by the Agency, and loan closing documents to the Agency;
- (2) Any construction or rehabilitation, except exterior development as described in § 3555.202(d) is complete; and
- (3) The Agency issues the loan guarantee document.

**§§ 3555.108–3555.150 [Reserved]****Subpart D—Underwriting the Applicant****§ 3555.151 Eligibility requirements.**

(a) *Income eligibility.* At the time of loan approval, the household's adjusted income must not exceed the applicable moderate-income limit for the area.

(b) *Citizenship status.* Applicants must be United States citizens or qualified aliens, as defined in § 3555.10.

(c) *Principal residence.* Applicants must agree to and have the ability to occupy the dwelling as a principal residence on a permanent basis. The Agency will not guarantee loans for temporary housing.

(d) *Eligibility of current homeowners.* Current homeowners are eligible for guaranteed loans: Provided, that by closing of the guaranteed loan, they do not own nor are they financially responsible for another home or other real property.

(e) *Legal capacity.* Applicants must have the legal capacity to incur the loan obligation, or have a court-appointed guardian or conservator who is empowered to obligate the applicant in real estate matters.

(f) *Suspension or debarment.* Applicants who are suspended or debarred from participation in Federal programs under part 3017 of this title or title 48 of the Code of Federal Regulations are not eligible for loan guarantees.

(g) *Repayment ability.* Applicants must demonstrate adequate repayment ability.

(1) An applicant is considered to have adequate repayment ability when the monthly amount required for payment of principal, interest, taxes, and insurance (PITI) does not exceed 29 percent of the applicant's repayment income, and the monthly amount required to pay PITI plus recurring

monthly debts does not exceed 41 percent of the applicant's repayment income.

(2) Repayment ratios may exceed the percentages specified in paragraph (g)(1) of this section if the lender determines that compensating factors demonstrate that the household has a higher repayment ability and the lender obtains Agency approval.

(3) If an applicant does not meet the repayment ability requirements, the applicant can increase repayment ability by having other household members join the application.

(4) Mortgage Credit Certificates may be considered in determining an applicant's repayment ability.

(5) A funded buydown account may be used to improve repayment ability when all of the following requirements are met.

(i) The interest rate must be bought down to no more than 2 percentage points below the note rate.

(ii) The interest rate paid by the borrower must increase to the note rate within 2 years of loan closing, with an increase of no more than 1 percentage point annually.

(iii) Funds must be placed in an escrow account with monthly releases scheduled directly to the lender.

(iv) Funds must be placed with a Federally- or state-regulated lender.

(v) The escrow account must be fully funded for the buydown period.

(vi) The borrower is not permitted to fund the escrow account and must not be required to repay the funds.

(h) *Credit qualifications.* Applicants must meet the following credit qualifications:

(1) Applicants must have a credit history that indicates reasonable ability and willingness to meet debt obligations. Indicators of unacceptable credit include:

(i) An outstanding judgment obtained by the United States in a Federal court, other than the United States Tax Court;

(ii) A delinquent Federal debt;

(iii) Three or more debt payments more than 30 days late within the last 12 months;

(iv) A foreclosure which has been completed within the last 36 months;

(v) An outstanding Internal Revenue Service (IRS) tax lien or any other outstanding tax liens with no satisfactory arrangement for payment;

(vi) A court-created or court-affirmed obligation or judgment caused by nonpayment that is currently outstanding or has been outstanding within the last 12 months, except for those excluded in paragraph (h)(2) of this section;

(vii) Two or more rent payments paid 30 or more days late within the last two

years. If the applicant has experienced no other credit problems in the past 2 years, only 1 year of rent history will be evaluated. Rent payment history requirements may be waived by the lender if the guaranteed loan will reduce shelter costs significantly and contribute to an improved repayment ability;

(viii) Outstanding collection accounts with a record of irregular payment with no satisfactory arrangements for repayment, or collection accounts that were paid in full within the last 6 months;

(ix) Non-Agency debts written off within the last 36 months unless paid in full at least 12 months ago; and

(x) Agency debts that were debt settled within the last 36 months, or are being considered for debt settlement.

(2) The following will not be considered indicators of unacceptable credit:

(i) A bankruptcy in which debts were discharged more than 36 months prior to the date of application or where an applicant successfully completed a bankruptcy debt restructuring plan and has demonstrated a willingness to meet obligations when due for the 12 months prior to the date of application; and

(ii) A judgment satisfied more than 12 months before the date of application.

(3) The lender may consider mitigating circumstances to establish the borrower's intent for good credit (except when an applicant is delinquent on a Federal debt or has an outstanding judgment obtained by the United States in a Federal Court, other than the United States Tax Court) when the applicant provides documentation that:

(i) The circumstances were of a temporary nature and have been removed; or

(ii) The loan will significantly reduce the applicant's shelter costs, which will result in enhanced debt repayment ability.

(i) *Homeownership education.* The lender must ensure that borrowers who are first-time homebuyers, prior to loan closing, obtain education that adequately prepares them for the obligations of homeownership.

#### **§ 3555.152 Calculation of income and assets.**

(a) *Repayment income.* Repayment income is the annual amount of adequate and dependable income from all sources that those household members who are parties to the promissory note are expected to receive, except for any student financial aid received by household members for tuition, fees, books, equipment, materials, and transportation.

Repayment income is used to determine the applicant's ability to repay a loan.

(b) *Annual income.* Annual income is the income of all household members from all sources, including, but not limited to, net family assets as defined in paragraph (d) of this section except for the following:

(1) Earned income of persons under the age of 18 unless they are an applicant or a spouse of a member of the household;

(2) Payments received for the care of foster children or foster adults;

(3) Amounts granted for, or in reimbursement of, the cost of medical expenses;

(4) Earnings of each full-time student 18 years of age or older, except the head of household or spouse, that are in excess of any amount determined pursuant to 24 CFR 5.609(c);

(5) Temporary, nonrecurring, or sporadic income (including gifts);

(6) Lump sum additions to family assets such as inheritances; capital gains; insurance payments under health, accident, or worker's compensation policies; settlements for personal or property losses; and deferred periodic payments of supplemental security income and Social Security benefits received in a lump sum;

(7) Any earned income tax credit;

(8) Adoption assistance in excess of any amount determined pursuant to 24 CFR 5.609(c);

(9) Amounts received by the family in the form of refunds or rebates under State or local law for property taxes paid on the dwelling;

(10) Amounts paid by a State agency to a family with a developmentally disabled family member living at home to offset the cost of services and equipment needed to keep the developmentally disabled family member at home;

(11) The full amount of any student financial aid; and

(12) Any other revenue exempted by a Federal statute, a list of which is available from any Rural Development office.

(c) *Adjusted income.* Adjusted income is used to determine program eligibility and the amount of payment subsidy, if any, for which the household qualifies. Adjusted income is annual income as defined in paragraph (b) of this section, less any of the following deductions for which the household is eligible.

(1) A reduction for each family member, except the head of household or spouse, who is under 18 years of age, 18 years of age or older with a disability, or a full-time student, the amount of which will be determined pursuant to 24 CFR 5.611.



(2) A deduction of reasonable expenses for the care of a child 12 years of age or under that:

- (i) Enables a family member to work, to actively seek work, or to further a member's education;
- (ii) Are not reimbursed or paid by another source; and
- (iii) In the case of expenses to enable a family member to work, do not exceed the amount of income, including the value of any health benefits, earned by the family member enabled to work.

(3) A deduction of reasonable expenses related to the care of household members with disabilities that:

- (i) Enable a family member to work, to actively seek work, or to further a member's education;
- (ii) Are not reimbursed from insurance or another source; and
- (iii) Are in excess of 3 percent of the household's annual income.

(4) For any elderly family, a deduction in the amount determined pursuant to 24 CFR 5.611.

(5) For elderly and disabled families only, a deduction for household medical expenses that are not reimbursed from insurance or another source and which, in combination with any expenses related to the care of household members with disabilities described in paragraph (c)(3) of this section, are in excess of 3 percent of the household's annual income.

(d) *Net family assets.* Income from net family assets must be included in the calculation of annual income.

(1) Net family assets include the cash value of:

- (i) Equity in real property, other than the dwelling or site;
- (ii) Cash on hand and funds in savings or checking accounts;
- (iii) Amounts in trust accounts that are available to the household;
- (iv) Stocks, bonds, and other forms of capital investments that are accessible to the applicant without retiring or terminating employment;
- (v) Lump sum receipts such as lottery winnings, capital gains, and inheritances;

(vi) Personal property held as an investment; and

(vii) Any value, in excess of the consideration received, for any business or household assets disposed of for less than fair market value during the 2 years preceding the income determination. The value of assets disposed of for less than fair market value shall not be considered if they were disposed of as a result of foreclosure, bankruptcy, or a divorce or separation settlement.

(2) Net family assets do not include:

- (i) Interest in American Indian restricted land;

(ii) Cash on hand which will be used to reduce the amount of the loan;

(iii) The value of necessary items of personal property;

(iv) Assets that are part of the business, trade, or farming operation of any member of the household who is actively engaged in such operation;

(v) Amounts in voluntary retirement plans such as individual retirement accounts (IRAs), 401(k) plans, and Keogh accounts (except at the time interest assistance is initially granted); and

(vi) The value of an irrevocable trust fund or any other trust over which no member of the household has control.

#### §§ 3555.153–3555.200 [Reserved]

### Subpart E—Underwriting the Property

#### § 3555.201 Site requirements.

(a) *Rural areas.* The Agency will only guarantee loans made in rural areas designated by the Agency. However, if a rural area designation is changed to nonrural:

(1) Existing conditional commitments in the former rural area will be honored; and

(2) A supplemental loan may be made in conjunction with a transfer and assumption of a guaranteed loan.

(b) *Site standards.* Sites must be developed in accordance with any standards imposed by a State or local government and must meet all of the following requirements.

(1) The value of the site, excluding the dwelling and any outbuildings, must not exceed 30 percent of the market value of the property, except that if the value of the site is typical for the area and the site is not large enough to subdivide into more than one site under existing zoning ordinances, the 30 percent limitation may be exceeded.

(2) The site must not include farm service buildings, but small outbuildings such as a storage shed may be included.

(3) The site must be contiguous to and have direct access from a street, road, or driveway. Streets and roads must be hard surfaced or all-weather surfaced and arrangements must be in place to ensure that needed maintenance will be provided.

(4) The site must be supported by adequate utilities and water and wastewater disposal systems.

#### § 3555.202 Dwelling requirements.

(a) *Modest dwelling.* Dwellings financed with a guaranteed loan must be considered modest housing for the area as defined in § 3555.10.

(b) *New dwellings.* New dwellings must meet the thermal standards and be

constructed in accordance with certified plans and specifications as described in part 1924, subpart A, of this title. To ensure acceptable construction quality, the lender must obtain:

(1) Documentation of acceptable construction quality and evidence of a 1-year builder's warranty; or

(2) A final inspection report and evidence of a 10-year builder's warranty.

(c) *Existing dwellings.* Existing dwellings must:

- (1) Be structurally sound;
- (2) Be functionally adequate;
- (3) Be in good repair, or to be placed in good repair with loan funds;
- (4) Have adequate and safe electrical, heating, plumbing, water, and wastewater disposal systems;
- (5) Be free of termites and other wood damaging pests and organisms; and

(6) Meet the thermal standards specified in part 1924, subpart A of this title.

(d) *Escrow account for exterior development.* If a dwelling is complete with the exception of exterior development work, the Agency may guarantee the loan if the following conditions are met:

(1) The exterior cannot be completed immediately because of weather conditions;

(2) All unfinished work will be completed within 120 calendar days of loan closing;

(3) The unfinished work will not affect habitability; and

(4) The lender establishes an escrow account at closing funded at 150 percent of the estimated completion cost of the remaining work.

#### § 3555.203 Ownership requirements.

After the loan is closed, the borrower must have an acceptable ownership interest in the property as evidenced by one of the following:

(a) *Fee-simple ownership.* Acceptable fee-simple ownership is evidenced by a fully marketable title with a deed vesting a fee-simple interest in the property to the borrower.

(b) *Secure leasehold interest.* Loans may be guaranteed on leasehold properties if the lender determines that the following conditions are met:

(1) The applicant is unable to obtain fee simple title to the property;

(2) Such leaseholds are fully marketable in the area, except in the case of properties located on American Indian restricted land; and

(3) The lease has an unexpired term of at least 45 years from the date of loan closing, except in the case of properties located on American Indian restricted land where the lease must have an

unexpired term at least equal to the term of the loan.

**§ 3555.204 Security requirements.**

The Agency will only guarantee loans that are adequately secured. A loan will be considered adequately secured only when all of the following requirements are met:

(a) The lender obtains, at closing, a mortgage on all required ownership and leasehold interests in the security property and ensures that the loan is properly closed;

(b) No liens prior to the guaranteed mortgage exist except in conjunction with a supplemental loan for transfer and assumption;

(c) Existing and proposed property improvements are completely on the site and do not encroach on adjoining property; and

(d) All collateral secures the entire loan.

**§ 3555.205 Special requirements for condominiums.**

Loans may be guaranteed for condominium units that meet all of the requirements of this part and the unit is in a project approved or accepted by HUD, Fannie Mae, VA, or Freddie Mac.

**§ 3555.206 Special requirements for community land trusts.**

Loans may be guaranteed for dwellings on land owned by a community land trust if all the requirements of this part are met, and any restrictions imposed by the community land trust on the property or applicant:

(a) Are reviewed and accepted by the Agency before loan closing; and

(b) Automatically and permanently terminate upon foreclosure or acceptance by the lender of a deed in lieu of foreclosure.

**§ 3555.207 Special requirements for Planned Unit Developments.**

Loans may be guaranteed for PUDs that meet all of the requirements of this part, as well as the criteria for PUDs established by HUD, VA, Fannie Mae, or Freddie Mac.

**§ 3555.208 Special requirements for manufactured homes.**

Loans may be guaranteed for manufactured homes if all of the requirements of this part are met.

(a) *Eligible costs.* In addition to the loan purposes described in § 3555.101, the Agency may guarantee a loan used for the following purposes related to manufactured homes when a real estate mortgage covers both the unit and the site:

(1) Purchase of a new manufactured home meeting the requirements of

manufactured housing in § 3555.10, transportation, permanent foundation, and set-up costs of the manufactured home, and purchase of an eligible site if not already owned by the applicant; and

(2) Site development work in accordance with part 1924, subpart A of this title.

(b) *Loan restrictions.* In addition to the loan restrictions contained in § 3555.102, the following loan restrictions also will apply.

(1) A loan will not be guaranteed if it is used to purchase a site without also financing a new unit.

(2) A loan will not be guaranteed if it is used to purchase furniture, including but not limited to: movable articles of personal property such as drapes, beds, bedding, chairs, sofas, divans, lamps, tables, televisions, radios, and stereo sets. Furniture does not include wall-to-wall carpeting, refrigerators, ovens, ranges, washing machines, clothes dryers, heating or cooling equipment, or other similar items.

(3) A loan will not be guaranteed to purchase an existing manufactured home and site unless:

(i) The unit and site are already financed with an Agency direct single family or guaranteed loan;

(ii) The unit and site are being sold from the Agency's inventory; or

(iii) The unit and site are being sold from the lender's inventory, and the loan for which the unit and site served as security was a loan guaranteed by the Agency.

(c) *Dealer-contractors.* No loans will be guaranteed on a manufactured home sold by any entity that is not an Agency-approved dealer-contractor that will provide complete sales, service, and site development services.

(d) *Construction and development.* Unit construction must conform to the Federal Manufactured Home Construction and Safety Standards (FMHCSS) and the Agency's thermal standards in accordance with part 1924, subpart A of this title. The site development and set-up also must conform with that subpart and the manufacturer's requirements for a permanent installation.

(e) *Warranty requirements.* The dealer-contractor must provide a warranty in accordance with the provisions part 1924, subpart A of this title. The warranty must identify the unit by serial number. The dealer-contractor must certify that the manufactured home has sustained no hidden damage during transportation and, if manufactured in separate sections, that the sections were properly joined and sealed according to the

manufacturer's specifications. The data plate, affixed to the inside of the unit, and the certification label, affixed to each transportable section at the tail-light end of each unit, indicates that the manufactured home substantially conforms with the plans and specifications. The dealer-contractor also must furnish the applicant with a copy of all manufacturer's warranties.

**§§ 3555.209–3555.250 [Reserved]**

**Subpart F—Regular Servicing**

**§ 3555.251 Servicing responsibility.**

(a) Lenders must perform those servicing actions that a reasonable and prudent lender would perform in servicing its own portfolio of unguaranteed loans.

(b) The Agency may require a lender to transfer its loan servicing activities to an approved lender if the lender fails to provide acceptable servicing.

(c) A lender may choose to contract with a third party to service its loans, but remains responsible for the quality of the servicing.

**§ 3555.252 Required servicing actions.**

Lender servicing responsibility includes, but is not limited to, the following actions.

(a) *Collecting regularly scheduled payments.* Lender must collect regularly scheduled loan payments and apply them to the borrower's account.

(b) *Payment of taxes and insurance.* Lenders must ensure that real estate taxes, assessments, and flood and hazard insurance premiums for all property that secures a guaranteed loan are paid on schedule.

(1) *Establish escrow account.* Lenders with the capacity to escrow funds must establish escrow accounts for all guaranteed loans for the payment of taxes and insurance. Escrow accounts must be administered in accordance with the Real Estate Settlement and Procedures Act (RESPA) of 1974, and insured by the Federal Deposit Insurance Corporation (FDIC).

(2) *Plan and responsibility of lender to ensure payment.* Lenders that do not have the capacity to escrow funds must obtain Agency approval of a plan for ensuring that the borrower pays such obligations on a timely basis. In addition, such lenders must accept the responsibility for payment of taxes and insurance that come due prior to liquidation. The Agency will not include any taxes or insurance amounts that accrued prior to acceleration in any potential loss claim.

(c) *Insurance.* (1) Until the loan is paid in full, lenders must ensure that borrowers maintain hazard and flood

insurance on property securing guaranteed loans. The insurance must be issued by companies, in amounts, and on terms and conditions acceptable to the Agency. Flood insurance through the National Flood Insurance Program must be maintained for all property located in special flood or mud slide areas identified by FEMA and must be consistent with part 1806, subpart B of this title.

(2) Lenders must ensure that borrowers immediately notify them of any loss or damage to insured property and collect the amount of the loss from the insurance company. Unless the borrower pays off the guaranteed loan using the insurance proceeds, the following requirements must be met.

(i) All repairs and replacements must be planned, performed, and inspected in accordance with Agency construction requirements.

(ii) When insurance funds remain after payments for all repairs, replacements, and other authorized disbursements have been made, the funds must be applied in the following order: prior liens (including past-due property taxes); past-due amounts; protective advances; and released to the borrower if the lender's debt is adequately secured.

(d) *Credit reporting.* The lender must notify a credit repository of each new guaranteed loan, and must report to that repository whenever any account becomes more than 30 calendar days past due.

#### **§ 3555.253 Late payment charges.**

Late payment charges will not be covered by the guarantee and cannot be added to the principal and interest due under any guaranteed note.

(a) *Maximum amount.* The late payment charge must be reasonable and customary for the area.

(b) *Loans with interest assistance.* The lender must not charge a late fee if the only unpaid portion of the borrower's scheduled payment is interest assistance owed by the Agency.

#### **§ 3555.254 Final payments.**

Lenders may release security instruments only after full payment of all amounts owed, including recapture, has been received and verified.

#### **§ 3555.255 Borrower actions requiring lender approval.**

(a) *Mineral leases.* A lender may consent to the lease of mineral rights and subordinate its lien to the lessee's rights and interests in the mineral activity if the security property will remain suitable as a residence, the lender's security interest will not be

adversely affected, and the environmental requirements of part 1940, subpart G, of this title are met. Subordination of guaranteed loans to a mineral lease does not entitle the leaseholder to any proceeds from the sale of the security property.

(1) If the proposed activity is likely to decrease the value of the security property, the lender may consent to the lease only if the borrower assigns 100 percent of the income from the lease to the lender to be applied to reduce principal, and the total rent to be paid is at least equal to the estimated decrease in the market value of the security property.

(2) If the proposed activity is not likely to decrease the value of the security property, the lender may consent to the lease if the borrower agrees to use any damage compensation received from the lessee to repair damage to the site or dwelling, or to assign it to the lender to be applied to reduce principal.

(b) *Partial release of security property.* A lender may consent to transactions affecting a security property, such as selling or exchanging security property or granting of a right-of-way across the security property, and grant a partial release, provided that the following conditions are met.

(1) The borrower will receive adequate compensation.

(i) For sale of security property, the borrower must receive cash in an amount equal to or greater than the value of the security property being sold or interests being conveyed.

(ii) For exchange of security property, the borrower must receive another parcel of property with value equal to or greater than that being disposed of.

(iii) For granting an easement or right-of-way, the borrower must receive benefits that are equal to or greater than the value of the security property being disposed of or interests being conveyed.

(2) An appraisal will be conducted if the most current appraisal is more than 1 year old or if it does not reflect current market value.

(3) The security property, after the transaction is completed, will be an adequate but modest, decent, safe, and sanitary dwelling.

(4) Repayment of the guaranteed debt will not be jeopardized.

(5) When exchange of all or part of the security property is involved, title clearance will be obtained before release of the existing security.

(6) Proceeds from the sale of a portion of the security property, granting an easement or right-of-way, damage compensation, and all similar transactions requiring the lender's

consent, will be used in the following order:

(i) To pay customary and reasonable costs related to the transaction that must be paid by the borrower.

(ii) To be applied on a prior lien debt, if any.

(iii) To be applied to the guaranteed indebtedness or used for improvements to the security property consistent with the purposes and limitations applicable for use of guaranteed loan funds. Proposed development will be planned and performed in accordance with Agency standards and supervised by the lender to ensure that the proceeds are used as planned.

(7) The Agency determines that the environmental requirements of part 1940, subpart G of this title are met.

#### **§ 3555.256 Transfer and assumptions.**

This section addresses requirements imposed upon the lender for notifying the Agency of a borrower's intent to transfer title to a security property, and if title is transferred, under what conditions the Agency will continue to honor the guarantee.

(a) *Transfer without assumption.* (1) The lender must notify the Agency if the borrower transfers the security property and the transferee does not assume the debt.

(2) Except as described in paragraph (d) of this section, the Agency will withdraw the guarantee if a security property is transferred with the lender's knowledge without assumption of the debt.

(b) *Transfer with assumption.* (1) The lender must obtain Agency approval before consenting to a transfer with an assumption of the outstanding debt.

(2) The Agency may approve a transfer with an assumption of the outstanding debt if the following conditions are met.

(i) The transferee must assume the entire outstanding debt and acquire all property securing the guaranteed loan balance; however, the transferor must remain personally liable.

(ii) The transferee must meet the eligibility requirements described in subpart D of this part.

(iii) The property generally must meet the site and dwelling requirements described in subpart E of this part, or be brought to those standards. Guaranteed loans secured by properties located in areas that have ceased to be rural may be assumed, however, notwithstanding the fact that the property is located in a nonrural area.

(iv) The priority of the existing lien securing the guaranteed loan must be maintained or improved.

(v) Any new rates and terms must not exceed the rates and terms allowed for

new loans under this part, and the interest rate must not exceed the interest rate on the initial loan.

(vi) The transferee must pay any recapture owed at the time of the transfer and assumption.

(vii) A new guarantee fee, calculated based on the remaining principal balance, must be paid to the Agency in accordance with § 3555.107(e).

(viii) If additional financing is required to complete the transfer and assumption or to make needed repairs, the Agency may approve a supplemental guaranteed loan provided adequate security exists.

(c) *Transfer without approval.* If a lender becomes aware that a borrower has transferred a property without the lender's knowledge, the lender must take one of the following actions:

(1) Notify the Agency and continue the loan without the guarantee;

(2) Obtain Agency approval for the transfer with assumption; or

(3) Liquidate the guaranteed loan and submit a claim for any loss.

(d) *Transfer without triggering the due-on-sale clause.* (1) Due-on-sale clauses in security instruments are not triggered by the following types of transfers:

(i) A transfer from the borrower to a spouse or children not resulting from the death of the borrower;

(ii) A transfer to a relative, joint tenant, or tenant by the entirety resulting from the death of the borrower;

(iii) A transfer to a spouse or ex-spouse resulting from a divorce decree, legal separation agreement, or property settlement agreement;

(iv) A transfer to a person other than a deceased borrower's spouse who wishes to assume the loan for the benefit of persons who were dependent on the deceased borrower at the time of death, if the dwelling will be occupied by one or more persons who were dependent on the borrower at the time of death, and there is a reasonable prospect of repayment; or

(v) A transfer into an inter vivos trust in which the borrower does not transfer rights of occupancy in the property.

(2) When a transferee obtains a property with a guaranteed loan through a transfer that does not trigger the due-on-sale clause:

(i) The lender will notify the Agency of the transfer;

(ii) The Agency will continue with the guarantee, whether or not the transferee assumes the guaranteed loan;

(iii) The transferee may assume the guaranteed loan on the rates and terms contained in the promissory note. If the account is past due at the time an assumption agreement is executed, the

loan may be reamortized to bring the account current;

(iv) The transferee may assume the guaranteed loan under new rates and terms if the transferee applies and is eligible; and

(v) The transferee may receive interest assistance if eligible in accordance with § 3555.105.

(3) Any subsequent transfer of title, except upon death of the inheritor or between inheritors to consolidate title, will trigger the due-on-sale clause.

#### § 3555.257 Unauthorized assistance.

(a) *Unauthorized assistance due to false information.*

(1) If the borrower receives a guaranteed loan based on false information provided by the borrower, the Agency may require the lender to accelerate the guaranteed loan. If the lender fails to accelerate the loan upon request, the Agency may withdraw the guarantee.

(2) If the borrower receives a guaranteed loan based on false information provided by the lender, the Agency may withdraw the guarantee, and may withdraw the lender's approval to participate in the program.

(3) If, based on false information provided by either the lender or the borrower, the borrower receives interest assistance above the amount to which the borrower was entitled, the lender must require the borrower to repay the unauthorized amount within 30 calendar days. If the borrower repays the excess interest assistance, the guaranteed loan may be continued. If the false information was not provided by the borrower, and if the borrower cannot repay the excess amount within 30 calendar days, the account can be reamortized to include the excess interest assistance.

(4) If the borrower or lender provides false information, the Agency may, in addition to criminal and civil false claim actions, pursue suspension or debarment.

(b) *Unauthorized assistance due to inaccurate information.* (1) Inaccurate information is incorrect information inadvertently provided, used, or omitted without the intent to obtain benefits for which the recipient was not eligible.

(2) The Agency will continue to honor a guarantee for a loan made to an applicant who receives a guaranteed loan based on inaccurate information if the applicant was eligible to receive the guaranteed loan at the time it was made, and if the loan funds were used only for eligible loan purposes.

(3) If, based on inaccurate information, the borrower receives interest assistance above the amount to

which the borrower was entitled, the lender must require the borrower to repay it within 30 calendar days. If the borrower cannot repay the excess amount within 30 calendar days, the lender may enter into a forbearance agreement with the borrower, or reamortize the guaranteed loan. If the borrower arranges to repay the interest assistance, the Agency will continue to honor the guarantee.

#### §§ 3555.258–3555.300 [Reserved]

### Subpart G—Servicing Accounts With Repayment Problems

#### § 3555.301 General policy.

Lenders must make reasonable efforts to resolve any repayment problems and provide borrowers with the maximum opportunity to become successful homeowners. The lender may use the servicing options described in this subpart if a borrower is having difficulty keeping an account current.

#### § 3555.302 Forbearance.

Lenders may offer borrowers the opportunity to avoid liquidation by entering into a forbearance agreement that specifies a reasonable plan for bringing the account current.

#### § 3555.303 Protective advances.

Lenders may pay for the following expenses necessary to protect the security property and charge the cost against the borrower's account.

(a) *Advances for taxes and insurance.* Lenders may advance funds to pay past due real estate taxes, hazard and flood insurance premiums, and other related costs.

(b) *Advances for costs other than taxes and insurance.* Protective advances for costs other than taxes and insurance, such as emergency repairs, can be made only if the borrower cannot obtain an additional loan or reimbursement from an insurer, or the borrower has abandoned the property.

#### § 3555.304 Reamortization.

(a) *Situations with false information provided by the borrower.* If a borrower has received unauthorized assistance only due to false information provided by the borrower, reamortization is not permitted.

(b) *All other situations.* If the borrower has not provided false information, the lender may bring a borrower's account current by reamortizing the guaranteed loan at the promissory note interest rate if:

(1) The lender can demonstrate that there is a reasonable possibility that the borrower will be able to repay the loan after reamortization;

(2) Reamortization is required to enable the borrower to meet scheduled obligations;

(3) The lender's lien priority will not be adversely affected; and

(4) The loan term after reamortization does not exceed the remaining term of the loan before reamortization.

(c) *Loan guarantee amount.* The amount of the loan guarantee is not changed by reamortization.

#### **§ 3555.305 Liquidation.**

(a) *Policy.* When a lender determines that a borrower is unable or unwilling to meet loan obligations, the lender may accelerate the guaranteed loan and, if necessary, foreclose. The lender must accelerate the guaranteed loan when the account is three scheduled payments past due unless there is a reasonable prospect of resolving the delinquency through another method. The borrower is responsible for all expenses associated with liquidation and acquisition.

(b) *Acceleration and foreclosure.* The lender must initiate foreclosure within 90 calendar days of the decision to liquidate unless Federal, State, or local law requires that foreclosure action be delayed. In such a case, foreclosure must be initiated within 60 calendar days after acceleration becomes possible.

(c) *Reinstatement of accounts.* Unless State law imposes other requirements, the lender may reinstate an accelerated account only if the borrower:

(1) Pays in a lump sum all past-due amounts, any protective advances, and any foreclosure-related costs incurred by the lender; and

(2) Has the ability to continue making scheduled payments on the guaranteed loan.

(d) *Bankruptcy.* (1) When a petition in bankruptcy is filed by a borrower after acceleration, the lender must suspend collection and foreclosure actions in accordance with title 11 of the United States Code (title 11).

(2) The lender may accept conveyance of security property by the trustee in the bankruptcy, or the borrower, if the bankruptcy court has approved the transaction, and the lender will acquire title free of all liens and encumbrances except the lender's liens.

(3) Whenever possible after the borrower has filed for protection under Chapter 7 of title 11, a reaffirmation agreement will be signed by the borrower and approved by the bankruptcy court prior to discharge, if the lender and the borrower decide to continue.

(e) *Voluntary liquidation.* A borrower may voluntarily liquidate the security

property using any of the following methods.

(1) *Refinancing or sale.* The borrower may refinance or sell the security property for a price that reflects at least the property's estimated market value. The sale proceeds, less any reasonable and customary sale or closing costs incurred by the borrower, must be applied to the borrower's account.

(2) *Deed in lieu of foreclosure.* The lender may accept a deed in lieu of foreclosure unless the lender's anticipated costs for selling the property, including any costs required to make the property marketable, exceed the property's estimated market value.

(3) *Offer by junior lienholder.* If a junior lienholder makes an offer in the amount of at least the anticipated net recovery value, as calculated in accordance with § 3555.353, the lender may assign the note and mortgage to the junior lienholder.

(f) *Maintain condition of security property.* The lender must make reasonable and prudent efforts to ensure that the condition of the security property is maintained during any liquidation, acquisition, and sale of the property.

(g) *Interest assistance.* If the borrower is receiving interest assistance, the interest assistance agreement will be canceled when the borrower transfers title or ceases to occupy the property.

(h) *Debt settlement reporting.* The lender must report to the IRS and credit reporting agencies any debt settled through liquidation.

#### **§§ 3555.306–3555.350 [Reserved]**

### **Subpart H—Collecting on the Guarantee**

#### **§ 3555.351 Loan guarantee limits.**

(a) The maximum loss payment under the guaranteed loan program is the lesser of:

(1) Any loss sustained by the lender of an amount equal to 90 percent of the principal amount actually advanced to the borrower; or

(2) For the first portion of the loss, up to 35 percent of the principal actually advanced, the Agency will pay 100 percent of the loss. For any remaining loss, up to 65 percent of the principal actually advanced, the Agency will pay 85 percent of the loss.

(b) For purposes of this section, the "principal amount actually advanced" means the total amount of the loan as indicated by the promissory note, less any loan funds not actually disbursed to the borrower or on behalf of the borrower.

#### **§ 3555.352 Loss covered by the guarantee.**

When a loan is liquidated, the Agency will reimburse the lender for the difference between the guaranteed loss incurred by the lender and the net recovery value of the property up to the guarantee limit. Guaranteed losses may include the following:

(a) Principal and interest, as evidenced by the guaranteed loan note;

(b) Additional interest accrued from the start of liquidation to the date of final loss settlement; and

(c) Any principal and interest indebtedness on protective advances, as described in § 3555.303.

#### **§ 3555.353 Net recovery value.**

The net recovery value of the property is determined differently for properties that have been sold than for properties that are in the lender's inventory at the time the loss claim is filed.

(a) *Actual net recovery value.* For a property that the lender has sold when a loss claim is filed, net recovery value is calculated as the difference between:

(1) The proceeds from the sale and any other amounts recovered; and

(2) Liquidation and disposition costs that are reasonable and customary for the area. Costs incurred by in-house staff are not allowable.

(b) *Anticipated net recovery value.* For a property that the lender has not sold when a loss claim is filed, net recovery value is calculated as the difference between:

(1) The value of the property as determined by an appraisal that is calculated to provide reasonable assurance that the property will sell within 90 days of being placed on the market; and

(2) Liquidation and estimated disposition costs that are reasonable and customary for the area. Costs incurred by in-house staff are not allowable.

#### **§ 3555.354 Loss claim procedures.**

(a) *Sold property.* For property that has been sold, the lender must submit a loss claim within 30 calendar days of the sale.

(b) *REO property.* If the property has not been sold and remains an REO property, the lender must take the following steps.

(1) Notify the Agency that the property has not been sold.

(i) If the property is not located on American Indian restricted land, the lender must notify the Agency if the property has not been sold within 90 calendar days of foreclosure, or from the end of any applicable redemption period, whichever is later.

(ii) If the property is located on an American Indian restricted land, the

lender must notify the Agency if the property has not been sold within 12 months of foreclosure, or from the end of any redemption period, whichever is later.

(2) Upon notification that the property has not been sold, the Agency will conduct an appraisal and provide the results to the lender. The lender must submit a loss claim within 30 calendar days of receiving the results of the appraisal.

(c) *Deficiency judgments.* The lender must enforce any judgment for which there are current prospects of collection before filing a loss claim, and amounts collected must be applied against the outstanding debt. The Agency will make a loss payment if there are not current prospects for collection.

**§ 3555.355 Reducing or denying the claim.**

(a) *Determination of loss payment.* If the lender has failed to fulfill any of its

obligations under this part, the Agency may cancel the guarantee or reduce any loss claim by the portion of the loss that the Agency determines was caused by the lender's failure to comply with the full faith and credit provision of the guarantee agreement. The circumstances under which loss claims may be denied or reduced include, but are not limited to, the following lender actions:

- (1) Failure to adhere to required servicing and liquidation procedures;
- (2) Failure to ensure that the security property is adequately maintained;
- (3) Delay in filing a loss claim;
- (4) Claiming unauthorized expenses;
- (5) Providing unauthorized assistance;
- (6) Failure to obtain the required security or maintain the security position;
- (7) Violating usury laws; or
- (8) Committing, or failing to report knowledge of, fraud.

(b) *Disputes.* If the lender disputes the loss claim amount determined by the Agency, the Agency will pay the undisputed portion of the loss claim, and the lender may appeal the decision.

**§ 3555.356 Future recovery.**

If the lender recovers additional funds after the loss claim has been paid, the proceeds will be distributed so that the total loss to the Government is equivalent to the loss that would have been incurred had the recovered amount been included in the initial loss calculation.

**§§ 3555.357–3555.400 [Reserved]**

Dated: November 30, 1999.

**Jill Long Thompson,**

*Under Secretary, Rural Development.*

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