

CHAPTER 10: CLAIMS

10.1 PURPOSE AND OVERVIEW


This chapter addresses the property liquidation and claim processes. When all reasonable efforts to resolve deficiencies in loan performance have failed, the lender must liquidate the loan and dispose of the property in order to submit a final loss claim. An overview of the GRRHP liquidation and claim payment process is shown in Exhibit 10-1.

KEY TOPICS IN THIS CHAPTER

- Pre-Liquidation Requirements
- Decision to Liquidate
- Property Liquidation
- Agency Election of Assignment or Conveyance
- Determination of the Claim Amount
- Payment of the Final Claim

EXHIBIT 10-1
THE LIQUIDATION PROCESS FOR GRRHP

The lender submits a liquidation plan and supporting documentation to the Agency within 30 calendar days of the decision to liquidate.



The Agency notifies the lender of its decision to approve or reject the plan within 20 calendar days of receipt of the plan. If the Agency fails to respond to the lender within 20 calendar days, the liquidation plan will be considered approved by default, and the 90-day period for interest accrual will commence.

If the liquidation is expected to exceed 90 calendar days, the lender must submit with the liquidation plan *Form RD 449-30*, “*Loan Note Guarantee Report of Loss*”, for an estimated loss payment.

Payment on the estimated loss claim is normally made within 30 calendar days after the Agency’s approval of *Form RD 449-30*.

The lender acquires and disposes of the property in accordance with the liquidation plan.

The lender submits a final report of loss on *Form RD 449-30* to the Agency.
The final loss claim is normally paid within 60 calendar days of receipt of the final report of loss.

SECTION 1: PRE-LIQUIDATION REQUIREMENTS

10.2 OVERVIEW

Before a decision to liquidate can be considered, the lender must make all reasonable attempts to resolve the deficiencies with the property. Chapter 7 provides a variety of Agency-recommended special servicing actions to help lenders restore a property's physical and financial health. Implementation of a workout plan can often delay or eliminate the need to liquidate the account. As a part of the notification to the Agency of a decision to liquidate, the lender must certify that they have made all reasonable attempts to resolve the issues using special servicing methods.

SECTION 2: DECISION TO LIQUIDATE

10.3 OVERVIEW

A decision to liquidate must be made by the lender when it determines that the default cannot be cured through special servicing, and it is in the best interest of the Agency and the lender to liquidate.

In the event of a default involving a loan to an Indian tribe or tribal corporation, which is secured by an interest in land within such tribe's reservation (as determined by the Secretary of the Interior), including a community in Alaska incorporated by the Secretary of the Interior pursuant to the Indian Reorganization Act (25 U.S.C. 461 et seq.), the lender shall only pursue liquidation after offering to transfer the account to an eligible tribal member, the tribe, or the Indian housing authority serving the tribe. If the lender subsequently proceeds to liquidate the account, the lender shall not sell, transfer, or otherwise dispose of or alienate the property except to one of the entities described in the preceding sentence.

Liquidation should be considered when any of the following circumstances exist:

- A loan has been delinquent for 90 calendar days, and the lender and borrower have not been able to agree on the terms to cure the delinquency;
- The borrower has failed to comply with the approved workout plan; or
- Delaying liquidation will impair the recovery value of the collateral or jeopardize full recovery on the loan.

If not already paid off under the guarantee, the holder may initiate by written demand to the lender and/or the Agency requesting commencement of foreclosure or repurchase of the unpaid guaranteed portion of the loan when the borrower is not less than 60 days in default or the

lender has failed to remit to the holder its pro rata share of any payment made by the borrower within 30 days of the lender's receipt thereof [*§3565.405(a) and (b)*]. During the liquidation process, the lender must follow the procedures for repurchasing the loan from the holder regardless of when the holder formally requests that it be reimbursed under the guarantee [*§3565.405(a) and (b)*].

Once a decision is made to liquidate a loan, the lender must meet the following deadlines in order to be eligible for payment under the guarantee:



- Notify the borrower and the Agency within 7 calendar days from the date of the decision to liquidate (see Paragraph 10.4);
- Submit a liquidation action plan for Agency approval within 30 calendar days of the notice to the Agency (see Paragraph 10.5); and
- Submit *Form RD 449-30* for an estimated loss payment if the liquidation is expected to exceed 90 calendar days (see Paragraph 10.7).

When the lender decides to liquidate, they must report to the Agency on a monthly basis using *Form RD 1980-41* until the account is satisfied or the guarantee is terminated.

At the same time the lender has decided to pursue liquidation, the lender must notify the holder of the intent to liquidate, unless the holder has already been paid under the guarantee.

10.4 NOTICE OF LIQUIDATION AND POTENTIAL CLAIM

Once the lender has made a decision to liquidate the account, they must notify the Agency and the borrower within 7 calendar days of the decision. This notification will inform the borrower that liquidation proceedings will commence and alert the Agency to expect a submission of the liquidation plan. The holder may request of the lender that it (the holder) be paid off prior to liquidation. If, under the guarantee, the lender does not repurchase the loan from the holder, the Agency will repurchase the loan from the holder in accordance with [*§3565.405 (b)*].



10.5 SUBMISSION OF A LIQUIDATION PLAN

Within 30 calendar days after notifying the Agency of the decision to liquidate, the lender must submit to the Agency, in writing, the proposed liquidation plan. Upon approval by the Agency, the lender will commence liquidation. If, within 20 calendar days of the Agency's receipt of the liquidation plan, the Agency fails to respond to the lender's proposal, the liquidation plan will be approved by default.

A liquidation plan must include, but is not limited to the following:

- Documentation to establish the lender's and/or holder's ownership of the guaranteed loan, promissory note, and related security instruments and a copy of the payment ledger or equivalent which reflects the current loan balance, accrued interest to date, and the method of computing the interest.
- A full and complete list of all collateral, including any personal and corporate guarantors.
- The recommended liquidation methods for making the maximum collection possible on the indebtedness and the justification for such methods, including recommended actions for:
 - ◊ Acquiring and disposing of all collateral; and
 - ◊ Collecting from guarantors.
- An appraisal of the collateral and the due diligence report. In order to formulate a liquidation plan that maximizes recovery, collateral must be evaluated in accordance with the requirements contained in Chapter 11 for the release of hazardous substances, petroleum products, or other environmental hazards that may adversely impact the market value of the collateral. The appraiser must consider this information in developing an appraised value.
- The proposed date of foreclosure.
- The proposed date of liquidation.
- Steps to be taken to preserve the collateral and protect the tenants.
- Copies of the borrower's latest available financial statements.
- Copies of the personal or corporate guarantor's latest available financial statements.
- An itemized list of estimated liquidation expenses expected to be incurred along with justification for each expense.
- A schedule to periodically report to the Agency on the progress of liquidation.
- An estimate and justification of protective advances.
- Proposed protective bid amounts on collateral to be sold at auction and a breakdown to show how the amounts were determined.
- A determination of whether a deed-in-lieu of foreclosure will be considered.

- If a voluntary conveyance is considered, the proposed amount to be credited to the guaranteed debt.
- Any relevant legal opinions, including, for example, opinions on environmental issues, title searches, and bankruptcy.

10.6 APPROVAL OF LIQUIDATION PLAN

The Agency will accept or reject the lender's liquidation plan within 20 calendar days after receipt of the plan or request that the lender make revisions to the plan. If the Agency fails to meet this deadline, the plan will be approved by default. When the State Office receives the lender's liquidation plan, the State Office immediately must notify the Director of the Multi-Family Housing Guarantee Loan Division.

The State Office will review and assess the lender's liquidation plan. The State Office will recommend acceptance or rejection of a liquidation plan and send it to the National Office for concurrence in a timely manner. The Director of the Multi-Family Housing Guarantee Loan Division will review the State Office recommendation and the liquidation plan. The National Office must concur with the State Office recommendation on all lender submitted liquidation plans.

When a liquidation plan is approved by the Agency, the lender must proceed expeditiously with liquidation, in accordance with the terms of the plan. Agency approval of the lender's liquidation plan is normally classified as a categorical exclusion under the Agency's environmental review process, unless the proposed method of liquidation will result in an alteration of the purpose, operation, location, or design of the project as originally approved. The liquidation plan may be modified when conditions warrant. All modifications must be approved, in writing, by the Agency prior to implementation.

10.7 FILING AN ESTIMATED LOSS CLAIM

Upon approval of the liquidation plan, all interest credit payments, if applicable, from the Agency will cease. If the liquidation plan is expected to exceed 90 calendar days the lender will submit an estimated loss payment with the liquidation plan. Any estimated loss payment must be applied to the outstanding principal and interest of the guaranteed debt. Estimates must be prepared and submitted by the lender on *Form RD 449-30* using the basic loss formula as provided on the report. The estimated loss claim will be promptly processed. Payment of the estimated loss amount will normally be made to the lender within 30 calendar days after the loss estimate has been approved by the Agency.

10.8 WITHDRAWAL OF A CLAIM


At the request of the lender, if the borrower cures the default prior to the earliest payment of the estimated loss claim or foreclosure, the guarantee will continue as if the default had not occurred. The lender must notify the State Office, the Agency Finance Office and the holder that the default has been cured.

SECTION 3: PROPERTY LIQUIDATION

10.9 PROPERTY ACQUISITION

The first step in the liquidation process is to acquire the property. The liquidation plan must inform the Agency of the proposed method of acquisition, including:

- Judicial foreclosure;
- Non-judicial foreclosure; or
- Deed-in-lieu of foreclosure.

The lender must estimate the time frame when the acquisition should occur.  In most cases, acquisition should be completed within 120 calendar days from approval of the liquidation plan. If the lender foresees a longer acquisition period, the reasons for the delay must be explained in the liquidation plan. Examples of appropriate reasons for a delay include:

- A State law declaration of bankruptcy by the borrower;
- Time to provide written notice to tenants or similar tenant protection measures;
- Constraints imposed by other liens or financing on the property; and
- Court backlog.

Unless otherwise approved by the Agency, the amount bid by the lender at foreclosure sale must equal the lesser of the sum of the outstanding principal and interest, liquidation expense, and approved protective advances or the appraised value of the property.

Once the collateral has been purchased by a third party through foreclosure, the borrower has conveyed title to the lender, or an estimated loss payment is made by the Agency to the lender, no further transfer of physical assets can be made. Once the lender has title to the property, interested purchasers of the real estate owned (REO) property may negotiate with the lender, at the lender's discretion.

10.10 LENDER LIQUIDATION

If a property is acquired by the lender through foreclosure or other method of conveyance, the lender must dispose of the property in accordance with the liquidation plan. If complications in the liquidation process lead to unforeseen delays, the lender must immediately notify the Agency of the reason for the delay and submit a revised date for expected liquidation. Failure to inform the Agency of the unforeseen circumstance could result in the denial of payments to the lender under the guarantee.



While the Agency expects the lender to dispose of the property in a manner that will yield the highest possible market value, marketing and liquidation actions must ensure that protections afforded to tenants in [7 CFR part 3560, subpart D] are provided.



10.11 FAILURE TO COMPLY WITH THE LIQUIDATION PLAN

The purpose of the liquidation plan is to ensure timely liquidation of property at the lowest cost to the Agency. If the lender fails to comply with the liquidation plan that has been approved by the Agency, it may result in the denial of benefits to the lender under the guarantee.

If the lender becomes aware of any situation that would change any part of the liquidation plan, it must immediately inform the Agency of the reasons for such change and submit an amendment to the liquidation plan for approval by the Agency.

SECTION 4: AGENCY ELECTION OF ASSIGNMENT OR CONVEYANCE

10.12 OVERVIEW

While liquidation by the lender will occur in almost every case, the Agency reserves the right to require the lender to assign the loan or convey the property to the government prior to liquidation if it determines that assignment or conveyance of title is in the best interest of the government. In these cases, the lender may submit a claim in accordance with the provisions of Section 5 of this chapter. If a holder remains in possession of a certificate of guarantee of the loan during this process, it must also be notified of such action by the lender.

Examples of reasons the Agency may require loan assignment or conveyance of title include:

- It would be less costly to the government for the Agency to dispose of the property;

- Tenant protection issues are of such a complicated nature that disposal or retention of the property by the Agency is necessary; and
- The lender has been grossly negligent in servicing the loan.

After a review of the proposed liquidation plan, the Agency will inform the lender if it will require an assignment or conveyance of title.

10.13 ASSIGNMENT OF THE LOAN

An assignment of the guaranteed loan to the Agency must be in written and recordable form and must be completed within 90 calendar days of the Agency notice to the lender. The assignment documents will be forwarded to the OGC's Regional Attorney for review. The assignment will be considered complete once the following transactions are completed to the Agency's satisfaction.



- Conveyance to the Agency of all rights and interests arising under the loan.
- Assignment to the Agency of all claims against the borrower or others arising out of the loan transaction, including:
 - ◇ All collateral agreements affecting financing, construction, use, or operation of the property; and
 - ◇ All claims under policies of title, or other insurance, surety bonds, or other guarantees.
- A due diligence report which evaluates the effect of potential contamination from hazardous wastes and from the release of hazardous substances and petroleum products on the security value of real property and an appraisal which takes the findings of the due diligence report into consideration.

If the Agency requires an assignment, the lender must stop any liquidation actions that are in process.

10.14 CONVEYANCE OF TITLE TO THE AGENCY

When the Agency requires a conveyance of title to the property, the lender must inform the Agency of the method and time frame for obtaining title to the property. The lender must obtain a deed in lieu of foreclosure from the borrower or implement the approved liquidation

plan. Once the foreclosure action is completed and the lender has obtained title to the property, the lender must transfer the title to the Agency. The Agency will accept the conveyance of title upon acceptance of the documents listed below and receipt of a satisfactory warranty deed.

- A release of all claims of the lender or other holder of the guarantee against the property.
- A due diligence report which evaluates the effect of potential contamination from hazardous wastes and from the release of hazardous substances and petroleum products on the security value of real property and an appraisal which takes the findings of the due diligence report into consideration.
- An assignment of the lender's rights to any operating funds and any reserves or escrow account established for such purposes as:
 - ◇ The maintenance of the property, including any replacement reserve or capital improvement reserves; or
 - ◇ The payment of property taxes and insurance.

Prior to acceptance of conveyance of property, the Agency will conduct an inspection to determine the physical condition, security, and need for rehabilitation and repair. This inspection will encompass site conditions, building exteriors, common elements, and interiors of all units.

SECTION 5: DETERMINATION OF THE CLAIM AMOUNT

10.15 INTRODUCTION

The determination of the claim amount actually begins during the development of the liquidation plan. Factors such as the date of the decision to liquidate, estimated liquidation value of the security property, estimated date of foreclosure and estimated date of liquidation will all affect the amount the Agency will be required to pay to the lender. The Agency will review the liquidation plan to be sure that the costs and time frames of acquisition and liquidation minimize losses to the government. Calculating the amount payable under the guarantee is a multi-step process detailed below.

If there is a loss claim due to contamination from a release of hazardous substances, hazardous wastes, or petroleum products, the Agency shall not finalize loss claims until the guaranteed lender has sold the property or the Agency has accepted assignment or conveyance of title to the property.

10.16 DETERMINATION OF THE DATE OF LOSS

A. Lender Liquidation

The date of loss is the date the loan is terminated due to foreclosure or other means of conveyance. This date will be the earliest of:

- The date on which the property is acquired; or
- The proposed date of acquisition in the liquidation plan or any approved modifications to the liquidation plan.

If the date of acquisition is later than the date approved by the Agency, the date of loss for the purpose of calculation of the claim will be the Agency's approved date.

B. Assignment or Conveyance of Title to the Agency

Where the Agency requires an assignment of the loan or conveyance of title, the date of loss will be the date on which the Agency accepts assignment of the loan or conveyance of title.

In submitting the liquidation plan to the Agency, the lender must specify the estimated date of assignment or conveyance of title. Unless the delay in assignment or conveyance is due to Agency action or inaction, the date of loss may be no later than the date approved in the liquidation plan or any amendment.

10.17 CALCULATION OF LOSS

In order to receive payment under the guarantee, the lender must calculate and submit for Agency approval *Form RD 449-30*. The information contained in the report will be used to estimate the loss to the Agency on an individual loan. The aggregate amounts reported by all lenders will be used to forecast the amount the Agency will need to disburse in claim payments in a fiscal year. When completing the report of loss, the lender should use the following as a guide.

A. Request for Estimated Loss Claim

Form RD 449-30 must be completed following the guidance in Paragraph 10.7. Unpaid principal and interest figures inserted in lines 11 and 12 must be calculated as of the date of submission of the form.

B. Final Report of Loss (when an estimated loss claim payment has not been made)

The unpaid principal and interest figure on *Form RD 449-30* must be calculated based on the date of loss as explained in Paragraph 10.16 A. For interest calculation purposes, the Agency will pay interest that accrues no more than 90 calendar days from the date the liquidation plan is approved by the Agency.

10.18 PROTECTIVE ADVANCES

The calculation of the loss amount may include any amounts approved by the Agency for protective advances not paid from the project's cash flow. In general, protective advances are funds necessary to protect the value of the asset and ensure the security, health, and safety of the tenants. The lender must obtain the Agency's written approval for any protective advance above \$5,000. Such amounts may include:

- Property taxes;
- Water and sewer charges and other special assessments that are liens prior to the guaranteed loan; and
- Property insurance.

The lender may include an estimated amount of protective advances as part of the liquidation plan (see Paragraph 10.5). Once the plan is approved by the Agency, this amount must be included by the lender in the calculation for the report of final loss on *Form RD 449-30*, unless a different amount is approved by the Agency.

10.19 LIQUIDATION EXPENSES

The calculation of the loss amount will include any amounts approved by the Agency for liquidation expenses. In general, liquidation expenses are defined as those expenses necessary to market and dispose of the property. Such amounts may include:

- Loan guarantee fees paid after the borrower default;
- Reasonable third-party expenses to maintain and liquidate the property; and
- Independent appraiser's fees, including the cost of the due diligence report.

10.20 LEGAL EXPENSES DURING BANKRUPTCY PROCEEDINGS

The lender is responsible for protecting the guaranteed loan and all collateral securing the loan in bankruptcy proceedings. The State Office will immediately notify the National Office of all bankruptcy and pending bankruptcy proceedings and shall submit status reports to the National Office on a monthly basis.

When a bankruptcy proceeding results in the liquidation of the borrower entity legal expenses will be handled as directed by the court. All reasonable and customary legal expenses to protect the collateral may be shared based on the guaranteed percentage, usually a 90/10 split between the Agency and the lender. Chapter 11 of the Bankruptcy Code pertains to a reorganization of a business, where legal protection is afforded to the business. Expenses incurred by the lender in a Chapter 11 reorganization can never be liquidation expenses unless the proceeding becomes a Chapter 11 liquidation.

10.21 MAXIMUM GUARANTEE PAYMENT

The maximum guarantee payment will not exceed the product of 90 percent, or such lesser guarantee percentage as set forth in the Loan Note Guarantee Agreement, times the allowable loss amount, as determined in *Form RD 449-30*. The maximum guarantee payment must be approved by the Agency in accordance with Section 6 of this chapter.

SECTION 6: PAYMENT OF THE FINAL CLAIM

10.22 OVERVIEW

Within 60 calendar days of liquidation of the property, the lender must submit a report of final loss to the Agency using *Form RD 449-30*.

The lender must certify that all possibilities of collection have been exhausted as a condition for payment of the final claim. Upon payment, in whole or in part, the note or judgement evidencing the debt shall be assigned to the United States, and the lender shall have no further claim against the borrower or the United States.

10.23 SUBMISSION OF A REPORT OF FINAL LOSS

If the final loss is less than the estimated loss payment, the lender will reimburse the Agency for the overpayment, using *Form RD 1980-43*, "*Lender's Guaranteed Loan Payment to USDA*".

In those instances where the lender has made authorized protective advances not included in the estimated loss payment, it may claim recovery for the guaranteed portion of approved amounts advanced, and interest resulting from such advances, not to exceed 90 calendar days from the Agency's approval of the liquidation plan. Such payment will be made by the Agency when the final report of loss is approved.

10.24 THE APPROVED CLAIM AMOUNT

If the State Office reviewing the lender's claim is satisfied with the lender's calculation of the final claim amount, then the State Office will forward the claim payment request to the USDA Finance Office for processing. The Finance Office will process the claim normally within 60 calendar days of receipt of the claim request from the State Office.