Loan Note Guarantee and Indemnification

Single Family Housing Guaranteed Loan Program

Training Objectives

- Where is the topic located?
  - 7 CFR Part 3555 and HB-1-3555
- Learning Checks
- Resources
Things change!

- Every effort has been made to ensure training references are accurate at the time of publication.

- Always reference the most recent USDA publications available online.

Guaranteed Loan Program Regulation

7 CFR Part 3555

- The regulation is the rule!
- 8 Subparts: A – H
- Appendix 1
7 CFR Part 3555

3555.108 Full faith and credit.
(a) General.
(b) Interest.
(c) Violations.
(d) Indemnification.

7 CFR Part 3555: 3555.108
Sec. 3555.108 Full faith and credit.

(a) General. The Loan Note Guarantee constitutes an obligation supported by the full faith and credit of the United States and is incontestable except for fraud or misrepresentation of which the lender has actual knowledge at the time it becomes such lender or which the lender participates in or condones. Misrepresentation includes negligent misrepresentation.

(b) Interest. A note that provides for the payment of interest on interest, however, shall not be guaranteed. If the note to which the Loan Note Guarantee is attached or relates provides for the payment of interest on interest, then the Loan Note Guarantee is void. Notwithstanding the prohibition of interest on interest, interest may be capitalized in connection with re-amortization under subpart G of this part.
7 CFR Part 3555: 3555.108

(c) Violations. The Loan Note Guarantee will be unenforceable by the lender to the extent any loss is occasioned by violation of usury laws, civil rights laws, negligent servicing, failure to obtain the required security or use of loan funds for unauthorized purposes, regardless of the time at which Rural Development acquires knowledge of the foregoing. Negligent servicing is defined as servicing that is inconsistent with this subpart and includes the failure to perform those services which a reasonably prudent Lender would perform in servicing its own loan portfolio of loans that are not guaranteed. The term includes not only the concept of a failure to act, but also not acting in a timely manner or acting contrary to the manner in which a reasonably prudent Lender would act up to the time of loan maturity or until a final loss is paid.

(d) Indemnification. The loan note guarantee will remain in effect for any holder of the loan who acquired it from an originating lender. If the Agency determines that a lender did not originate a loan in accordance with the requirements in this part, and the Agency pays a claim under the loan guarantee, the Agency may revoke the originating lender’s eligibility status in accordance with subpart B of this part and may also require the originating lender:

(1) To indemnify the Agency for the loss, if the default leading to the payment of loss claim occurred within five (5) years of loan closing, when one or more of the following conditions is satisfied:

(i) The originating lender utilized unsupported data or omitted material information when submitting the request for a conditional commitment to the Agency;

(ii) The originating lender failed to properly verify and analyze the applicant’s income and employment history in accordance with Agency guidelines;
7 CFR Part 3555: 3555.108(d)(1)

(iii) The originating lender failed to address property deficiencies identified in the appraisal or inspection report that affect the health and safety of the occupants or the structural integrity of the property;

(iv) The originating lender used an appraiser that was not properly licensed or certified, as appropriate, to make residential real estate appraisal in accordance with § 3555.103(a); or,

7 CFR Part 3555: 3555.108(d)

(2) To indemnify the Agency for the loss regardless of how long ago the loan closed or the default occurred, if the Agency determines that fraud or misrepresentation was involved with the origination of the loan.

(3) In addition, the Agency may use any other legal remedies it has against the originating lender.
Guaranteed Loan Program Technical Handbook

HB-1-3555

• Provides guidance to support the regulation
• HB is not the rule
• 20 Chapters
16.6 AGENCY REVIEW OF CLOSING DOCUMENTS AND ISSUANCE OF THE LOAN NOTE GUARANTEE
A. Incomplete Closing Documents
   • 30 days to correct
B. Acceptable Closing Documents
   • LNG is issued
C. Unacceptable Closing Documents
   • Correction may be eligible, otherwise LNG denied
HB-1-3555: 16.7 Closing date

• Date on closing disclosure
• Interest credit may be eligible

HB-1-3555

CHAPTER 20: LOSS CLAIMS – COLLECTING ON THE GUARANTEE

20.1 OVERVIEW

20.2 LOSS CLAIM COVERAGE
   A. Loan Guarantee Limits
   B. Losses Covered by the Guarantee
   C. Reasonable and Customary

20.3 FILING A LOSS CLAIM
   A. Property That is Sold
   B. Unsold Real Estate Owned (REO) Property
   C. Definition of Value Types in the Appraisal Process and General Procedures
   D. Loss Administration – Record the Loss Claim in GLS
HB-1-3555: 20.2 Loss Claim Coverage

A. Loan Guarantee Limits

Maximum payment is lesser of:

- 90% of original principal amount or
- 100% of loss equal to 35% of original principal amount plus 85% of remaining loss up to 65% of original principal amount

Example: Original principal amount: $165,000

1. $165,000 x 90% = $148,500
2. $165,000 x 35% = $57,750
   - 65% of $165,000 = $107,250
   - 85% of $107,250 = $91,162.50
   - $57,750 + $91,162.50 = $148,912.50

Maximum loss claim payout: $148,500
HB-1-3555

4.7 REPORT SIGNIFICANT CHANGES
4.8 ADHERE TO SFHGLP GUIDELINES
4.9 INDEMNIFICATION
4.10 PREVENT MORTGAGE FRAUD

HB-1-3555

HB-1-3555

HB-1-3555
HB-1-3555: 4.9 Indemnification

- Originating lender
- Defaults within 60 months of loan closing
- Unsupported data or omitted material information
- Failure to verify/analyze income or employment
- Identified property deficiencies
- Ineligible appraiser

HB-1-3555: 4.9 Indemnification

- Originating lender
- No timeframe from loan closing
- Loss due to fraud and misrepresentation
Form RD 3555-17/17E

This Loan Note Guarantee is issued under the Agreement for Guaranteed Single Family Housing Loans of

The United States Department of Agriculture, acting through the Rural Housing Service of the Rural Development Service (hereinafter referred to as "RHS"), pursuant to Title V of the Housing Act of 1949 (42 U.S.C. 1471 et. seq.) agrees that, subject to the terms and conditions hereof, it will pay to the Lender the lesser of:

1. Any loss of an amount equal to 10 percent of the principal amount actually advanced to the Borrower, or
2. Any loss sustained by the Lender of an amount up to 50 percent of the principal amount actually advanced to the Lender, plus
3. Any additional loss sustained by the Lender of an amount up to the remaining 50 percent of the principal amount actually advanced to the Borrower.

Loan includes only (a) principal and interest evidences by the Note, (b) any loan subsidy, and (c) any principal and interest indebtedness approved by RHS for protection and preservation of collateral. Interest (including any subsidy) shall be covered by the Loan Note Guarantee up to 90 days from the Loan Note Guarantee's initial date of issuance of the application date of the initial loss settlement, whichever is earlier. Net proceeds received from liquidation of the collateral will be used in calculating the amount of loss sustained by the Lender. If the Lender acquires the collateral, net proceeds from collateral for calculating loss shall be determined by RHS as follows: (i) the collateral will be appraised as of the date of acquisition; (ii) the Lender shall deduct from such appraisal value an estimate of liquidation cost which will include an allowance for 90 days, the estimated time the property will be held by the Lender.

RHS conducts the liquidation of the loan, loss accumulated to a Lender by accruing interest after the date RHS accepts responsibility for the liquidation will not be covered by the Loan Note Guarantee. Lessor may sell the guaranteed loan only to a Lender which meets the qualifications of in the manner as provided in 2 CFR part 3555.

Lender may obtain participation in its loan under its procedures. Participation means a sale of an interest in the loan whereas the Lender remains the sole collateral securing the note and all responsibility for all loans occurring and liquidated. A participant has no rights under this instrument.
Form RD 3555-17/17E

CONDITIONS OF THE GUARANTEE

1. Loan Servicing
   Lender will be responsible for servicing the entire loan and Lender will remain mortgagee and/or second party of record. The Lender may sell loan servicing rights to an RHS eligible Lender whom the purchaser Lender agrees to be bound by all of the same terms as the selling Lender and the agreement and the RHS Loan Agreement for Guaranteed Single Family Housing Loans.

2. Full Faith and Credit
   The Loan Note Guarantee constitutes an obligation supported by full faith and credit of the United States and is incontestable except for fraud or misrepresentation of which the lender has actual knowledge at the time it becomes such lender or which the lender participates in.

According to the Privacy Act of 1974, no person is required to respond to a collection of information unless it displays a valid OMB control number. The valid OMB control number for this information collection is 0571-0099. The time required to complete this information collection is estimated to average 5 minutes per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.
Form RD 3555-17/17E

Form RD 3555-17
(Rev. 06-16)
Page 2 of 2 - Borrower Name: ____________________________
RHS Borrower ID: ____________________________

or conditions. A note which provides for the payment of interest on interest shall not be guaranteed. If the rate to which this instrument is attached or relates provides for the payment of interest on interest then this Loan Note Guarantee is void. In addition, the Loan Note Guarantee will be unenforceable by the Lender to the extent any loss is occasioned by violation of any laws, negligent servicing, or failure to obtain the required security regardless of the issue at which RHS acquires knowledge of the existing. Any losses occasioned will be unenforceable by the Lender to the extent the loan funds are used for purposes other than those approved by RHS in its Form RD 3555-17. "Conditional Commitment for Single Family Housing Loan Guarantees" signifies servicing is defined as the failure to perform those services which a reasonably prudent lender would perform in servicing its own loan portfolio of loans that are not guaranteed. The term includes not only the concept of a failure to act but also not acting in a timely manner or acting contrary to this amount at which a reasonably prudent lender would act up to the time of loan origination or until a final loss is paid. If RHS determines that a Lender did not originate a loan in accordance with the requirements in 7 CFR part 3555 and RHS pays a claim under the loan guarantee, RHS may revoke the Lender's eligibility status in accordance with Section 3555.52 and may also require the Lender: (1) To indemnify RHS for the loss, if the payment under the guarantee was made within 60 months of loan closing, or (2) To indemnify RHS for the loss regardless of how long ago the loan closed, if RHS determines that fraud or misrepresentation was involved in connection with the origination of the loan in accordance with Section 3555.100.

Form RD 3555-17/17E

1. Lender will receive all payments of principal and interest, annual fee, and any loan subsidy on the account of the entire loan.
2. The Loan Note Guarantee is subject to an annual fee billed to the Lender and collected by the Agency on an annual basis for the life of the loan, based upon an annual fee percentage of: ______%. The annual fee will be based on the average annual scheduled unpaid principal balance of the loan and may be passed on to the guaranteed loan borrower. A late charge will be charged if the fee is not paid by the date set by RHS.
3. Prepayment Subventions made by the Lender pursuant to RHS regulations will be reduced against the amount of the loan in the Loan Note Guarantee.
4. The Loan Note Guarantee will terminate automatically (a) upon full payment of the guaranteed loan; or (b) upon full payment of any loss obligations hereunder; or (c) upon written notice from the Lender to RHS that the guarantee will terminate provided this Loan Note Guarantee is retained to be canceled by RHS.
5. Any amount due under this instrument will be determined and paid, as provided in 7 CFR part 3555 in effect on the date of this instrument.
6. All notices and actions may be initiated through Rural Development National Financial and Accounting Operations Center at the following email address: RD_DPTO.GIF@rural.usda.gov.
TIPS

• Underwriter = USDA Approved Lender
• USDA = not an underwriter
• Research Rule & HB questions: Table of Contents
• Research Rule & HB questions: Control + F
7 CFR PART 3555 / HB-1-3555
LEARNING CHECKS

Question Slide

“Topic”

• Question will be bulleted with scenario, or
• Include a statement/question

TRUE/FALSE or other answer options will be displayed
ANSWER SLIDE

“Topic”
ANSWER: 7 CFR Part 3555 and HB-1-3555 references provided

X. Correct Response

• Additional guidance for clarification may be provided

LET’S GET STARTED.
LNG and Indemnification

Loan Note Guarantees may only be issued to USDA approved lenders.

A. TRUE    B. FALSE

LNG and Indemnification

ANSWER: 3555.108 and HB 16.6 A

A. TRUE

• A Third Party Originator (TPO) and non-USDA approved lenders may not receive Conditional Commitments or Loan Note Guarantees (LNG)
LNG and Indemnification

Form RD 3555-17 must be printed, signed, and mailed to the approved lender.

A. TRUE   B. FALSE

LNG and Indemnification

ANSWER: 3555.108 and HB 16.6 B

B. FALSE

• The Loan Note Guarantee is issued electronically
• Form RD 3555-17E denotes the form was issued electronically
LNG and Indemnification

• Bixby Bank receives LNG
• Loan is sold to Orange Lending
• Loss is paid three years post closing
• Review determines negligence in origination
• Who is responsible to indemnify USDA

A. Bixby Bank     B. Orange Lending

ANSWER: 3555.108(d) and HB 4.9
A. Bixby Bank

• Indemnification applies to originating lender
• Servicers/Holder will be reimbursed under the terms of the LNG
• USDA will pursue indemnification
LNG and Indemnification

USDA may pursue indemnification from an originating lender up to ___ months post loan closing due to misrepresentation of material loan data.

A. 30   B. 60

ANSWER: 3555.108(d) and HB 4.9

60 months from loan closing applies for errors regarding:
- Misrepresentation/omissions
- Improper analysis of income/employment
- Failure to correct property deficiencies
- Ineligible appraiser
LNG and Indemnification

USDA may pursue indemnification from an originating lender _________ post loan closing due to fraud and negligence.

A. up to 60 months  B. with no time limit

ANSWER: 3555.108(d) and HB 4.9

- Fraud and negligence to the U.S. Government are always eligible for indemnification
LNG and Indemnification

- Loan closing received
- Conditional Commitment interest rate: 4.5%
- Lender closed the loan at 5.00%
- USDA must deny the LNG request

A. TRUE    B. FALSE

LNG and Indemnification

ANSWER: 3555.108 and HB 16.6 A

B. FALSE

- Lender may have 30 days to correct interest rate
- USDA may offer additional remedy options
- If no resolution is achieved, LNG must be denied
LNG and Indemnification

- Loan closing received
- USDA notifies lender of items that require correction
- Lender does not respond within 30 day timeframe
- USDA must deny the LNG request

A. TRUE  B. FALSE

ANSWER: 3555.108 and HB 16.6 A

A. TRUE

- USDA provided 30 days to correct
- Lender has not responded
- Lender notification requesting additional time to correct will be honored
LNG and Indemnification

- Loan closing received
- Borrower received $500 back at loan closing
- Borrower had $250 of eligible funds in the transaction
- The loan closed at or below the amount authorized on the Conditional Commitment
- USDA must deny the LNG request

A. TRUE  B. FALSE

LNG and Indemnification

ANSWER: 3555.108 and HB 16.6 A

B. FALSE

- Lender can apply $250 to the principal loan balance
- The closed loan did not exceed the authorized amount on the commitment
LNG and Indemnification

• Sunny Lending was issued a LNG
• They are selling the loan to Grey Bank but cannot find the LNG
• Sunny Lending may request a copy of the LNG from USDA

A. TRUE  B. FALSE

ANSWER: 3555.108 and HB 16.8

A. TRUE

• The approved lender may request a duplicate copy of the LNG
• A TPO and non-approved lenders may not access or request copies of the LNG
WAY TO GO!

Regulations
GovDelivery Sign up

Thank you for supporting the USDA Single Family Housing Guaranteed Loan Program!
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