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## GLOSSARY

## LIST OF ACRONYMS

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## **APPENDICES**

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- Appendix 2 Forms and Certifications
- Appendix 3 Handbook (HB) Letters
- Appendix 4 7 CFR Part 11, National Appeals Division Rules of Procedures
- Appendix 5 Appraisal Guidelines
- Appendix 6 NP Interest Rates
- Appendix 7 State Supplements

<b>ACRONYMS USED IN THIS HANDBOOK</b>
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ACE	Active Corps of Executives
ADR	Alternative Dispute Resolution
AFDC	Aid to Families with Dependent Children
CFR	Code of Federal Regulations
COLA	Cost of Living Adjustment
CFPB	Consumer Financial Protection Bureau
CFR	Code of Federal Regulations
COR	Contracting Officer Representative
DLOS	Dedicated Loan Origination and Servicing System
DOJ	Department of Justice
EA	Environmental Assessment
EIS	Environmental Impact Statement
EPA	Environmental Protection Agency
ECOA	Equal Credit Opportunity Act
EIR	Equivalent Interest Rate
FEMA	Federal Emergency Management Agency
FHA	Federal Housing Administration
FCP	Farm Credit Program
FP	Farmer Program

FSA	Farm Service Agency
HB	Handbook
HUD	Department of Housing and Urban Development
IRA	Individual Retirement Account
IRS	Internal Revenue Service
NAD	National Appeals Division
NEPA	National Environmental Policy Act
NFIP	National Flood Insurance Program
OGC	Office of General Counsel
OIG	Office of Inspector General
PI	Principal and Interest
PITI	Principal, Interest, Taxes, and Insurance
PRAS	Principal Reduction Attributable to Subsidy
RD	Rural Development
REO	Real Estate Owned
RESPA	Real Estate and Settlement Procedures Act
RHS	Rural Housing Service
SCORE	Service Corps of Retired Executives
SCRA	Servicemembers Civil Relief Act of 2003
Servicing Office	Servicing and Asset Management Office

SF	Standard Form
SFHA	Special Flood Hazard Area
SFH	Single Family Housing
TDD	Telecommunication Device for the Deaf
TSQ	Transaction Screen Questionnaire
U.S.C.	United States Code
USDA	The United States Department of Agriculture
VA	Department of Veterans Affairs
VISTA	Volunteers in Service to America



## APPENDIX 2

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**FORMS REFERENCED IN THIS HANDBOOK**

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**Forms**

Form RD 443-16, Assignment of Income from Real Estate Security  
Form RD 465-1, Application for Partial Release, Subordination, or Consent  
Form RD 1910-5, Request for Verification of Employment  
Form RD 1924-10, Release by Claimants  
Form RD 1924-12, Inspection Report  
Form RD 1927-8, Agreement with Prior Lienholder  
Form RD 1940-16, Promissory Note  
Form RD 1944-4, Certification of Disability or Handicap  
Form RD 1944-6, Interest Credit Agreement  
Form RD 1944-14, Payment Assistance/Deferred Mortgage Assistance Agreement  
Form RD 1944-62, Request for Verification of Deposit  
Form RD 1955-1, Offer to Convey Security  
Form RD 1965-14, Proof of Claim of the United States of America (Individual)  
Form RD 3550-1, Authorization to Release Information  
Form RD 3550-2, Request for Verification of Gift/Gift Letter  
Form RD 3550-4, Employment and Asset Certification  
Form RD 3550-6, Notice of Special Flood Hazards, Flood Insurance Purchase Requirements, and Availability of Federal Disaster Relief Assistance  
Form RD 3550-9, Initial Escrow Account Disclosure Statement  
Form RD 3550-12, Subsidy Repayment Agreement  
Form RD 3550-15, Tax Information  
Form RD 3550-16, Release from Personal Liability  
Form RD 3550-17, Funds Transmittal Report  
Form RD 3550-18, Reamortization Agreement  
Form RD 3550-19, Transmittal-Closing Documents  
Form RD 3550-20, Application for Settlement of Indebtedness  
Form RD 3550-21, Payment Subsidy Renewal Certification  
Form RD 3550-22, Assumption Agreement, Single Family Housing  
Form RD 3550-27, Substitute Payment Coupon  
Form 3550-28A, Authorization Agreement for Preauthorized Payments (This Form is only applicable to the Servicing Office).  
FEMA Form 81-93, Standard Flood Hazard Determination  
IRS Form 1099-C, Cancellation of Debt  
IRS Form 4506-T, Request for Transcript of Tax Return

**CERTIFICATIONS**

Verification of Pensions and Annuities  
Verification of Student Income and Expenses  
Verification of Medical Expenses  
Verification of Social Security Benefits  
Verification of Public Assistance  
Verification of Child/Dependent Care  
Verification of Unemployment Benefits  
Verification of Business Expenses  
Verification of Support Payments  
Certification of Disposition of Assets  
Record of Oral Verification

## VERIFICATION OF PENSIONS AND ANNUITIES

**This form is for internal use, only, by the Rural Development Servicing Office**

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

#### A. INCOME FROM ANNUITIES

1. \$ \_\_\_\_\_ Current monthly gross amount received. Will the applicant continue to receive this monthly amount for the next twelve months? \_\_\_\_ Yes \_\_\_\_ No If, no please explain.
2. Describe any deductions from the gross amount that are taken.

#### B. VERIFICATION OF ASSETS

1. \$ \_\_\_\_\_ Current market value of assets held in the retirement or pension plan.
2. Can the applicant withdraw amounts from the retirement account without retiring or terminating employment? \_\_\_\_ Yes \_\_\_\_ No. If yes, explain the terms of the withdrawal, including any penalties.
3. Can the applicant borrow against amounts in the retirement account? \_\_\_\_ Yes \_\_\_\_ No If yes, explain the terms (maximum amount, interest rate, repayment term, purposes, etc.)

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF STUDENT INCOME AND EXPENSES

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

1. Describe any financial assistance the above-reference student receives.

<u>Amount</u>	<u>Source</u>	<u>Purpose for Which Funds May Be Used</u>
---------------	---------------	--

2. Describe any expenses the above-referenced student has for:

\$ _____	Tuition
\$ _____	Housing
\$ _____	Books
\$ _____	Supplies and Equipment
\$ _____	Transportation
\$ _____	Misc. Personal Expenses
\$ _____	Total

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF MEDICAL EXPENSES

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

1. Please list the purpose of any accumulated medical bills, identify to whom the amount is owed, and provide the amount to be paid during the coming 12 months.

**Amount**

**Owed To**

**Medical Expenses for**

2. Medical Insurance Premiums

\$ \_\_\_\_\_ Amount Paid      Payment Period: \_\_\_\_ per month, \_\_\_\_ per year

Medical Insurance Premiums

\$ \_\_\_\_\_ Amount Paid      Payment period: \_\_\_\_ per month, \_\_\_\_ per year

3. List other anticipated medical expenses

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature)      Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF SOCIAL SECURITY BENEFITS

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

#### Social Security Data

\_\_\_\_\_ Date of Birth

\_\_\_\_\_ Gross Monthly Social Security Benefit Amount, Type of Benefit

\_\_\_\_\_ Gross Monthly Supplemental Security Income Payment Amount (including State Supplement) Type of Benefit

\_\_\_\_\_ Amount of Monthly Deductions for Medicare Paid by the Applicant

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_ Telephone Number: \_\_\_\_\_

(Signature)

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF PUBLIC ASSISTANCE

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

Number in Family: _____	<u>Rate Per Month</u>
Aid to Families with Dependent Children	\$ _____
General Assistance	\$ _____
Does this amount include Court Awarded Support Payments	<input type="checkbox"/> Yes <input type="checkbox"/> No
Amount Specifically Designated for Shelter and Utilities	\$ _____
Other Assistance - Type: _____	\$ _____
Total Monthly Grant	\$ _____
Other Income - Source: _____	\$ _____
*Maximum Allowance for Rent and Utilities	\$ _____
Amount of Public Assistance given during the past 12 months	\$ _____

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF CHILD/DEPENDENT CARE

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

Name of Person or Agency Providing Care: \_\_\_\_\_

Address: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Name(s) of person or Persons Cared for: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Specify Hours \_\_\_\_\_ and Days \_\_\_\_\_ of Care.

Average Amount Paid for Care: \$ \_\_\_\_\_ ☐ Week ☐ Month

Estimated Amount to be Paid in coming 12 months (including full-time summer care of school children, if applicable): \$ \_\_\_\_\_

Will any amount of this expense be reimbursed by an outside source: ☐ Yes ☐ No

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)



## VERIFICATION OF UNEMPLOYMENT BENEFITS

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

1. Are benefits being paid now? ☐ Yes ☐ No
2. If yes, what is Gross Weekly payment? \$ \_\_\_\_\_
3. Date of Initial Payment \_\_\_\_\_
4. Duration of Benefits \_\_\_\_\_ weeks  
Is claimant eligible for future benefits? ☐ Yes ☐ No
5. If yes, How many weeks? \_\_\_\_\_
6. If no, what is termination date of benefits? \_\_\_\_\_

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF BUSINESS EXPENSES

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

Based on business transacted during \_\_\_\_\_ 19 \_\_\_\_, to \_\_\_\_\_ 19 \_\_\_\_

- |                                |          |
|--------------------------------|----------|
| 1. Gross Income                | \$ _____ |
| 2. Expenses:                   |          |
| (a) Interest on Loans          | \$ _____ |
| (b) Cost of Goods/Materials    | \$ _____ |
| (c) Rent                       | \$ _____ |
| (d) Utilities                  | \$ _____ |
| (e) Wages/Salaries             | \$ _____ |
| (f) Employee Contributions     | \$ _____ |
| (g) Federal Withholding Tax    | \$ _____ |
| (h) State Withholding Tax      | \$ _____ |
| (i) FICA                       | \$ _____ |
| (j) Sales Tax                  | \$ _____ |
| (k) Other                      | \$ _____ |
| (l) Straight Line Depreciation | \$ _____ |
| Total Expenses                 | \$ _____ |
| 3. Net Income                  | \$ _____ |

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
Telephone Number: \_\_\_\_\_

(Signature)

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

## VERIFICATION OF SUPPORT PAYMENTS

### REQUEST FOR INFORMATION

Federal regulations require us to verify financial information provided by applicants for housing assistance. We ask your cooperation in supplying the information requested. The attached Form 3550-1, Borrower's Certification and Authorization provides the applicant's authorization.

Your prompt return of the requested information will be appreciated. A self-addressed return envelope is enclosed for your convenience. If you have questions, please call \_\_\_\_\_ at \_\_\_\_\_.

### APPLICANT IDENTIFICATION

Name \_\_\_\_\_ Social Security Number \_\_\_\_\_

### REQUESTED INFORMATION

Name of Person Paying Support: \_\_\_\_\_

Address: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

For ( ) Former Spouse

( ) Children

Children Names are:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Amount of Support  
\$ \_\_\_\_\_ ☐ Week, ☐ Month, ☐ Year

**VERIFIER INFORMATION:** Please sign this verification form and print the name, address and telephone number of the verifier.

Name: \_\_\_\_\_ Title: \_\_\_\_\_

\_\_\_\_\_  
(Signature) Telephone Number: \_\_\_\_\_

**WARNING:** Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)

CERTIFICATION OF DISPOSITION OF ASSETS	
I/we certify that during the two years (24 months) period preceding the effective date of my certification or recertification of eligibility for program participation, I/we _____ have _____ have not disposed of more than \$1,000 in asset(s) for less than fair market value.	
If asset(s) were disposed of for less than fair market value, describe:	
Asset	Date of Disposition
1.	
2.	
3.	
The amount received for the asset(s) disposed:	
1.	
2.	
3.	
<div> <div>Signature of Applicant</div> <div>Date</div> </div> <div> <div>Signature of Spouse</div> <div>Date</div> </div>	
<b>WARNING:</b> Knowingly and willingly making a false or fraudulent statement to any department of the United States Government is a felony punishable by fine and imprisonment (Title 18, Section 1001, U.S. Code)	

[illegible]

## APPENDIX 3

### LETTERS REFERENCED IN THIS HANDBOOK

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Handbook Letter 101(3550), Standardized Adverse Decision Letter  
Handbook Letter 102(3550), Continuation with Unreaffirmed Debt After Discharge in  
Bankruptcy  
Handbook Letter 103(3550), Agreement to Increase Salary Offset  
Handbook Letter 104(3550), Notification of Salary Offset  
Handbook Letter 105(3550), Notification of Administrative Offset  
Handbook Letter 106(3550), Request for Administrative Offset  
Handbook Letter 107(3550), Request for Salary Offset  
Handbook Letter 108(3550), Notification of IRS Offset  
Handbook Letter 109(3550), Confirmation of IRS Offset  
Handbook Letter 110(3550), Notification That the Agency Will Continue With Loan  
Handbook Letter 111(3550), Request for Borrower to Refinance With Private Credit  
Handbook Letter 112(3550), Reminder Letter  
Handbook Letter 113(3550), Follow up Request for Borrower to Refinance With Private  
Credit  
Handbook Letter 114(3550), Unresponsive  
Handbook Letter 115(3550), Response to Request to Sale for Less Than the Debt

REFERENCE: Servicing and Asset Management Office Handbook Chapter 1

SUBJECT: Standardized Adverse Decision Letter

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Date: [ *insert today's date* ]

[ *insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]  
[ *insert borrower(s) street/post office address* ]  
[ *insert city, state, and zip code* ]

Re: [ *Type/Amount of Assistance Requested* ]

Dear [ *insert borrower last name(s) (Mr., Mrs., Ms.)* ]:

Thank you for the opportunity to consider your request for Rural Development assistance. In reviewing your request, we considered all information submitted to the Agency and the regulations that govern the assistance for which you applied. After careful review, we regret to inform you that we were unable to take favorable action on your request. The specific reasons for our decision are as follows:

(The following items should be included in each adverse decision letter and can be presented in different formats depending upon the type of assistance requested and reasons for denial:

- Specific reasons for the decision;
- Regulatory basis (CFR citation) for the decision;
- If applicable, a statement of any evidence considered in making the decision such as credit reports, financial statements, etc.;
- If applicable, a statement of any issues presented by the customer such as those discussed during any meetings or phone conversations; and

If you believe our decision is incorrect, or the facts used in this case are in error, you may pursue your rights to challenge our decision. Please see the attached document.

Sincerely,

[ *insert name of RHS Official* ]  
[ *insert title of RHS Official* ]

Attachment [ *insert Attachment 1-B or 1-C, as appropriate from Chapter 1* ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 5

SUBJECT: Continuation With Unreaffirmed Debt After Discharge in Bankruptcy

Name of Borrower  
Address of Borrower  
Address of Borrower

Subject: Continuation with Unreaffirmed Debt After  
Discharge in Bankruptcy  
Account No. \_\_\_\_\_

Dear Homeowner:

USDA Rural Housing Service (RHS) formerly known as Farmers Home Administration (FmHA) has received notice that you have been discharged in a Chapter 7 bankruptcy. RHS records indicate that you did not surrender the property that is security for the above referenced RHS loan but have elected to retain the property without reaffirmation of your debt with RHS.

If your loan is in arrears all delinquent payments must be paid immediately if you plan to continue with the loan. You will be expected to make scheduled payments on or before the due date and to comply with all covenants of the Promissory Note and mortgage documents securing your loan. These requirements include maintaining adequate property insurance and paying taxes when they are due. Noncompliance with these stipulations may result in foreclosure.

RHS will continue to service your loan in accordance with governing policies and regulations even though you did not reaffirm the debt. This will include sending monthly billing statements and delinquency notices when applicable. You are entitled to all RHS program benefits for which you may be eligible such as payment assistance, moratorium, and applicable appeal rights. Because your debt was not reaffirmed, you are not legally obligated to repay the loan; however, if you intend to remain in the property, required payments must be made every month. In the event of default, RHS will not seek to collect from you personally but will look only to the security property for recovery of the debt.

For questions regarding your account, please call our Customer Service Department toll free at 1-800-414-1226 or TDD 1-800-438-1832, 7 A.M. to 5 P.M. Central Time, Monday through Friday. With a touch tone telephone, the Voice Response Unit (VRU) can provide automated confidential account information 7 days a week, outside of normal business hours. Please refer to your RHS loan number when you call or write us.

Sincerely,

Bankruptcy Section Head

USDA Rural Housing Service is an Equal Opportunity Lender, Provider, and Employer. Complaints of discrimination should be sent to: USDA, Director, Office of Civil Rights, Washington, DC 20250-9410

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(12-23-96) SPECIAL PN

Revised (03-31-21) SPECIAL PN



REFERENCE: Servicing and Asset Management Office Handbook Chapter 7 SUBJECT:

Agreement to Increase Salary Offset

---

Date: [ *insert today's date* ]

[ *insert Agency name* ]  
[ *insert Agency street/post office/ address* ]  
[ *insert city, state, and zip code* ]

Dear [ *insert Agency Representative* ]:

I, [ *Name of employee* ], agree to have \$ [ *amount employee wants withheld* ] withheld from my salary per pay period. This amount exceeds 15 percent of my disposable pay per pay period which is \$ [ *15 percent of disposable pay per pay period* ]. If the amount is less than 15 percent, it is based on the following reasons:

[ *list reasons* ]

\_\_\_\_\_  
[ *Employee's Signature* ]

\_\_\_\_\_  
[ *Date* ]

\_\_\_\_\_ Accepted

\_\_\_\_\_ Rejected

\_\_\_\_\_  
[ *Certifying Official* ]

\_\_\_\_\_  
[ *Date* ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 7

SUBJECT: Notification of Salary Offset

Date: [ *insert today's date* ]

[ *insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]

[ *insert borrower(s) street/post office address* ]

[ *insert city, state, and zip code* ]

Dear [ *insert borrower last name(s) (Mr., Mrs., Ms.)* ]:

The Rural Housing Service (RHS) has reviewed the record relating to your [ *delinquency* ] [ *debt* ], and determined that you owe the U.S. Government \$ [ *variable* ]. In accordance with 7 CFR 3550 a review has been made of the circumstances giving rise to the [ *delinquency* ] [ *debt* ]. Based on that review, it is my judgment that the cost of collecting the debt through salary offset will not exceed the amount of the debt. In addition, to my knowledge, there are not any legal restrictions that would bar collecting that debt.

We intend to collect this amount by offsetting your salary until the [ *delinquency* ] [ *debt* ] and all accumulated interest and other costs are paid in full. Deductions of 15 percent of your disposable income will begin with the first pay period occurring 30 days from the date you receive this letter and will continue until the delinquency or other debt is paid. You may voluntarily agree to a higher percentage. If you agree to RHS collecting more than 15 percent of your disposable pay, please let us know immediately in writing.

Interest and other costs may be assessed in accordance with Department Regulation 2520-1, Interest on Delinquent Debt, and 4 CFR 102.13.

As a Federal employee, you have the following rights:

1. The right to copy the records relating to the [ *delinquency* ] [ *debt* ]. Charges will be assessed for copying;
2. The right to enter into a written agreement for a repayment schedule different from that proposed so long as your terms of repayment are agreeable to RHS;
3. The right to a hearing conducted by a USDA Administrative Law Judge or a hearing official from outside USDA. The hearing will consider the existence of the [ *delinquency* ] [ *debt* ], the amount of the [ *delinquency* ] [ *debt* ], and/or percentage of disposable pay to be deducted each pay period. The timely filing of a petition or a hearing will stop collection proceedings;

1. The right to a final decision on a hearing at the earliest practical date, but not later than 60 calendar days after you file your hearing petition;
2. The right to request a waiver of salary overpayment. You may also question the amount or validity of a salary overpayment or general delinquency or other debt by submitting a claim to the Comptroller General in accordance with General Accounting Office procedures;
3. The right to have any monies paid on or deducted for the [ *delinquency* ] [ *debt* ] which are later waived or found not owed to the United States to be promptly refunded to you unless there are applicable contractual or statutory provisions to the contrary.

*(Use this paragraph only for collection-only accounts or other delinquent accounts for which there is no security)*

RHS has a debt settlement procedure which might allow your debt to be canceled or charged off. If you would like to know more about this, contact the Customer Service Department.

Submitting false or frivolous statement, representations, or evidence may subject you to disciplinary proceedings or civil or criminal penalties.

If you wish to file a petition for a hearing, we must receive the petition within 30 days from the date you receive this letter. The petition should be mailed to:

[ *Insert address* ]

You must sign the petition and must indicate your knowledge of whether you are [ *delinquent* ] [ *liable for the debt* ], or any part of the [ *delinquency* ] [ *debt* ]. You should fully identify and explain all the information and evidence that supports your position. If you would like reconsideration of the percentage of disposable income to be deducted, you should state your reasons.

Sincerely.

[ *insert name of RHS Official* ]  
[ *insert title of RHS Official* ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 7

SUBJECT: Notification of Administrative Offset

---

Date: [ *insert today's date* ]

[ *insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]  
[ *insert borrower(s) street/post office address* ]  
[ *insert city, state, and zip code* ]

Dear [ *insert borrower last name(s) (Mr., Mrs., Ms.)* ]:

The Rural Housing Service (RHS) intends to use administrative offset to collect the debt or debts you owe them. This notice advises of your rights concerning administrative offset as given by the Debt Collection Act, 31 U.S.C. 3716; the Federal Claims Collection Standards, 4 CFR 101-105; and the Rural Housing Service's Administrative Offset Regulations, 7 CFR 3550.

The RHS intends to begin taking, by administrative offset, money you are owed by (*Insert the name of the Federal Agency where RHS will send the offset request*) up to the full amount of the debt or debts you owe RHS.

RHS records show that you owe a total amount of \$ [ *amount past due* ], as of [ *date* ], and that interest is accumulating, after this date, at \$        per        .

The RHS will start offsetting this money in not less than 30 days after you receive this notice. RHS will not start offsetting this money, however, if you pay your debt in full within 30 days after you receive this notice.

### **Your Right To A Meeting Before Administrative Offset Begins**

You also have the right to a conference with an RHS official before RHS begins using administrative offset. At this conference you can:

- present any information on whether you really owe the debt or debts mentioned in the notice you received with this one, and whether the amounts RHS claims that you owe are correct or not, and/or
- give reasons why it would create an extreme hardship for you, or would be unfair for some other reason, if RHS uses administrative offset to collect the debt or debts you owe.

Is in the discretion of RHS to decide whether special circumstances do or do not justify a decision not to use administrative offset to collect the debt or debts you owe RHS.

You can also, either at the conference, or without asking for a conference, present any written submission to RHS on why you think the debt is not really owed, why the amount is not correct, or why you think administrative offset would create an extreme hardship or otherwise be unfair. If you want to present a written submission, you must present it within 30 calendar days after you receive this notice.

### **Your Right To Copy Records On Your Loan Or Loans**

You also have the right to inspect and copy any records concerning your account with RHS prior to your conference with RHS.

### **How To Request Your Conference And A Copy Your Records**

If you want a conference, or if you want to have a copy any of RHS records concerning your account, you must make a request. You can do this by contacting the office that sent you these notices as soon as you can, by telephone or in writing. You must make your request to copy your records within 15 calendar days after you receive this notice, and you must make your request for a conference within 30 calendar days after you receive this notice. If you ask to copy records and also ask for a conference, the RHS will schedule the conference not less than 10 working days after the date you inspect the records. You will be advised of the time and date of the meeting.

### **How to Make a Written Submission**

If you want to make a written submission, but do not want a conference, you must have your written submission to RHS within 30 days after you receive this notice.

### **Your Appeal Rights**

If, at the conference with RHS, you ask that offset not be used in your case, but the RHS decision is to use it, you then have the right to an administrative appeal on the issue of whether this decision was made in accordance with the laws and regulations applicable to RHS. The RHS will advise you on how to ask for this appeal in a letter that will be sent after the conference.

If you make a written submission, but do not have a meeting, you will have administrative appeal rights after the RHS responds to your written submission. The RHS will advise you on how to ask for this appeal in a letter that will be sent to you after considering your submission.

---

You can decide not to ask for a conference or make a written submission, and instead ask for an administrative appeal now. If you want an administrative appeal now, and do not also want a meeting or to make a written submission, you must request your administrative appeal now. See the attachment for your appeal rights (*Attach borrower appeal rights*) A request for appeal must be sent to the Area Supervisor, National Appeal Staff, (*Insert address*), postmarked no later than (*Insert date 30 days from date of letter*).

If, after your conference or after your written submission, the RHS decides to go ahead with administrative offset, RHS will begin using administrative offset to collect amounts you owe even though your administrative appeal process is about to start or is still pending.

If you ask for an administrative appeal now, instead of requesting a conference or making written submission, RHS will go ahead with administrative offset during the appeal. But, if you should win your appeal, any money collected by administrative offset will be returned to you with interest.

### **Last Notice**

This is the last notice on administrative offset that RHS will send out before it starts using administrative offset. If you want to use any of the rights set out in this notice, you must take action now.

Sincerely,

[ *insert name of RHS Official* ]  
[ *insert title of RHS Official* ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 7

SUBJECT: Request for Administrative Offset

---

Date: [ *insert today's date* ]

[ *insert Agency name* ]  
[ *insert Agency street/post office address* ]  
[ *insert city, state, and zip code* ]

Dear [ *insert Agency Representative* ]:

The Rural Housing Service (RHS) requests administrative offset from [ *Agency* ] program payments due or to become due to the below named delinquent debtor. This debt results from default on an RHS loan. RHS has exhausted all other resources available to it in an attempt to collect this debt.

[ *insert debtor(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]  
[ *insert debtor(s) street/post office address* ]  
[ *insert city, state, and zip code* ]  
[ *insert County* ]

RHS account number (variable)

Total amount delinquent (\$)

Principal delinquent (\$)

Interest delinquent (\$)

Delinquency as of (date)

Interest rate/year (%)

Daily accrual (\$)

Date due process letter was sent to debtor: [ Insert date Handbook Letter 105(3550) was sent to debtor. Must be at least 30 days before the date of this letter. ]

RHS certifies that the person named in this request owes this debt and that all of the due process and other applicable requirements of 31 U.S.C. 3716, 4 CFR Part 102, and its own regulations regarding administrative offset have been met. RHS has not been notified of any bankruptcy proceedings filed by the debtor.

Make checks payable to the Rural Housing Service and mail offset funds to [ *Insert address and closing* ].

Sincerely,

Servicing and Asset Management Office Servicing Representative

---

(12-23-96) SPECIAL PN

Revised (03-31-21) SPECIAL PN

REFERENCE: Servicing and Asset Management Office Handbook Chapter 7 SUBJECT:

Request for Salary Offset

---

Date: [ *insert today's date* ]

[ *insert Agency name* ]  
[ *insert Agency street/post office address* ]  
[ *insert city, state, and zip code* ]

Dear [ *insert Agency Representative* ]:

The Rural Housing Service requests salary offset from [ *Agency Name* ]. The employee named below has asked us to withhold [ *15 percent of their disposable pay or stated amount* ] each pay period to offset their [ *delinquency, indebtedness* ] with the Department of Agriculture.

[ *insert debtor(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]  
[ *insert debtor(s) street/post office address* ]  
[ *insert city, state, and zip code* ]  
[ *insert County* ]

This salary offset has been taken in accordance with the Debt Collection Act of 1982 and the Department of Agriculture's Salary Offset Regulations. If you have any questions or concerns regarding this action, you should contact the Customer Service Department at

\_\_\_\_\_.

Sincerely,

[ *insert name of RHS Official* ]  
[ *insert title of RHS Official* ]



REFERENCE: Servicing and Asset Management Office Handbook Chapter 7 SUBJECT:

Notification of IRS Offset

---

Date: [ *insert today's date* ]

[ *insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]

[ *insert borrower(s) street/post office address* ]

[ *insert city, state, and zip code* ]

Dear [ *insert borrower last name(s) (Mr., Mrs., Ms.)* ]:

**Refund for Offset**

Our records indicate that you are more than 2 months delinquent on a debt to the Rural Housing Service (RHS). The Internal Revenue Service (IRS) collects many delinquent payments by deducting the amount of the debt from income tax refunds to which delinquent borrowers were entitled. RHS plans to collect delinquent amounts through offset, and will refer information concerning your account to IRS. All amounts collected will be applied to your loan less processing fees.

**Legal Notice**

Any Federal agency that is owed a past-due, legally enforceable debt will notify the IRS of the amount of the debt. A Federal agency, before notifying the IRS, must notify the taxpayer that the Agency plans to refer the debt to IRS for offset, determine that the debt is past-due and legally enforceable after providing the taxpayer at least 60 days in which to present evidence to the contrary, and make reasonable efforts to collect the debt. This letter is to comply with these requirements.

**Joint Filings with IRS**

If you are married, filing a joint tax return, and you incurred this debt separately from your spouse who has no legal responsibility for the debt and who has income and withholding and/or estimated tax payments, he or she may be entitled to receive his or her portion of the joint refund. Such taxpayers filing joint returns should contact the IRS before filing their return regarding the steps to take to protect the share of the refund which may be payable to the non-obligated spouse.

### **60 Days to Provide Information**

If you feel you should not be reported for offset, you have 60 days from the date of receipt of this letter to provide written information to the Customer Service Department to show that offset should not be exercised. For example, you will not be reported if you have brought the account current to less than 2 months past due, or if you have agreed to bring the account current and RHS has officially agreed to that plan. Also, you will be exempted if the debt has been discharged in bankruptcy, you are under the jurisdiction of a bankruptcy court, or it is determined that RHS is not legally entitled to collect the debt at this time. The Customer Service Department will review the information you provide and notify you of the final decision regarding the offsetting of your IRS refund.

We strongly urge you to bring your account current.

### **Credit Bureau Reporting**

If you are reported for IRS offset, your account may be reported to credit bureau agencies. You have the same 60 day period from receipt of this letter to file a written request with the Servicing Office for a review of the status of your account and any information that is proposed to be reported to credit agencies. Once reporting begins it will be continued and updated monthly for 7 years. The amounts listed on the reverse side of this notice reflect the status of your RHS loan(s) based on payments received by RHS Customer Service Department.

ALL CONTACTS WITH RHS ARE TO BE DIRECTED TO THE CUSTOMER SERVICE DEPARTMENT WHICH IS SERVICING YOUR LOAN.

Sincerely,

[ *insert name of RHS Official* ]

[ *insert title of RHS Official* ]

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REFERENCE: Servicing and Asset Management Office Handbook Chapter 7 SUBJECT:

Confirmation of IRS Offset

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Date: [ *insert today's date* ]

[ *insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.)* ]

[ *insert borrower(s) street/post office address* ]

[ *insert city, state, and zip code* ]

Dear [ *insert borrower last name(s) (Mr., Mrs., Ms.)* ]:

[ *Insert the appropriate response* ]

We have reviewed the information you submitted concerning Internal Revenue Service (IRS) offset and have requested that your name be removed from IRS offset records. No offset will be exercised against your refund.

*OR*

We have reviewed the information you submitted concerning IRS offset and do not agree with you. We believe that your RHS debt is legally enforceable and that you are at least 2 months past due in your payments. Your name will remain on IRS records, and offset will be exercised against your refunds. In addition, information concerning your account may be reported to a credit bureau.

Sincerely,

[ *insert name of RHS Official* ]

[ *insert title of RHS Official* ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 2 SUBJECT:  
Notification That the Agency Will Continue With Loan

---

Date: [insert today's date]

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]  
[ insert borrower(s) street/post office address ]  
[ insert city, state, and zip code ]

Dear [ insert borrower(s) last name(s) (Mr., Mrs., Ms.) ]:

Based on Rural Housing Service's (RHS) evaluation of your present financial position and a comparison of lender requirements, it has been determined that you may experience difficulty obtaining suitable credit from other sources to refinance your RHS loan. For this reason, RHS will continue with your loan and you will not be asked to pursue refinancing at this time.

However, your loan will remain subject to the refinancing requirement and you may be asked to refinance the balance of your RHS indebtedness at a later date.

Sincerely,

[ insert name of Approval Official ]  
[ insert title of Approval Official ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 2 SUBJECT:  
Request for Borrower to Refinance With Private Credit

---

Date: [ insert today's date ]

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]  
[ insert borrower(s) street/post office address ]  
[ insert city, state, and zip code ]

Dear [ insert borrower(s) last name(s) (Mr., Mrs., Ms.) ]:

Your Security Instrument with Rural Housing Service (RHS) states that you will refinance the unpaid balance of your RHS loan when you have progressed to the point you can obtain credit from a private lending institution at reasonable rates and terms. After reviewing lender mortgage requirements, it appears that you would qualify for refinancing at this time. Within **90 days** from the date of this letter, we request that you refinance your housing loan in full with a private lender.

Currently, mortgage interest rates are at historic lows. You may be able to reduce the interest rate on your RHS loan and get a 25 percent discount on your subsidy recapture by refinancing your RHS loan with a private lender. By refinancing your RHS loan you may be able to save thousands of dollars in interest costs and also reduce your monthly mortgage payment.

As mentioned, we are offering a 25 percent discount on the recapture if the following conditions are met:

- Recapture is paid along with the final loan payment,
- You remain in the home, and
- You retain title to the property.

When the property's market value is determined, the Servicing and Asset Management Office (Servicing Office) will calculate your payoff and include the amount of discounted subsidy recapture owed. You will be given the opportunity to pay off the subsidy recapture in a lump sum or defer repayment. If you choose to defer repayment, you ***will not*** be eligible for the 25 percent discount.

In order to proceed with obtaining credit with another lender in your area, payoff information specific to your account may be obtained by calling the Servicing Office at 1-800-414-1226, 7:00 a.m. to 5:00 p.m., Monday through Friday, Central Standard Time.

If you are unable to refinance, you will need to provide the Servicing Office (within **90 days**) a letter from another lender documenting that you made an earnest effort to seek other credit but were unable to be approved for refinancing. This letter should include:

- Name of the lender contacted,
- Amount of loan requested and the amount, if any, offered by the lender,
- Rates and terms offered by the lender and specific reasons why credit is not available,
- Information provided to the lender regarding the purpose of the loan requested.

If you need assistance or have questions you may contact the Servicing Office by calling 1-800-414-1226 and entering code 1777 when prompted.

Sincerely,

[ insert name of Approval Official ]

[ insert title of Approval Official ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 2 SUBJECT:

Reminder Letter

---

Date: [ insert today's date ]

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]

[ insert borrower(s) street/post office address ]

[ insert city, state, and zip code ]

Dear [ insert borrower(s) last name(s) (Mr., Mrs., Ms.) ]:

This is a reminder to our *previous* letter requesting that you refinance your Rural Housing Service (RHS) Loan within **90 days** from (insert date Request to Refinance letter was sent). You need to take positive steps toward refinancing your RHS Loan. Failure to cooperate with this review is a violation of your security instruments. If we do not receive the information requested in our previous letter, RHS may recommend legal proceedings without further notice.

If you have not yet applied to refinance your home loan with a mortgage lender, you may call the Servicing and Asset Management Office (Servicing Office) at 1-800-414-1226 to provide financial information. When you call, please be prepared to provide the amount of your monthly gross income and installment debt payments. RHS will review your financial information and advise you regarding your ability to refinance. Another opportunity to refinance is through a guaranteed lender. Your local Field Office can provide a list of guaranteed lenders.

Payoff information may be obtained by calling the Servicing Office at 1-800-414-1226 and entering option 2 when prompted, or TDD 1-800-438-1832, 7:00 a.m. to 5:00 p.m., Monday through Friday, Central Standard Time. With a touch tone telephone, the Voice Response Unit (VRU) can provide automated confidential account information, seven days per week, outside of normal business hours. The Servicing Office can also provide information on deferring recapture of payment subsidies, possible discounts for paying subsidy recapture, and final payments.

Sincerely,

[ insert name of Approval Official ]

[ insert title of Approval Official ]

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(05-27-98) SPECIAL PN

Revised (03-31-21) SPECIAL PN

REFERENCE: Servicing and Asset Management Office Handbook Chapter 2 SUBJECT:  
Follow up Request for Borrower to Refinance With Private Credit

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Date: [insert today's date]

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]  
[ insert borrower(s) street/post office address ]  
[ insert city, state, and zip code ]

Dear [ insert borrower(s) last name(s) (Mr., Mrs., Ms.) ]:

This is a follow up to our letter requesting you to refinance your Rural Housing Service (RHS) loan.

We have reexamined the financial progress you have made since obtaining your loan based upon the financial information you recently provided. A determination was made that other credit appears to be available to you at rates and terms you can reasonably be expected to afford.

You need to take positive steps to refinance your loan within 90 days from (insert date of Handbook Letter 7).

Sincerely,

[ insert name of Approval Official ]  
[ insert title of Approval Official ]



REFERENCE: Servicing and Asset Management Office Handbook Chapter 2 SUBJECT:  
Unresponsive

---

Date: [insert today's date]

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]  
[ insert borrower(s) street/post office address ]  
[ insert city, state, and zip code ]

Dear [ insert borrower(s) last name(s) (Mr., Mrs., Ms.) ]:

Since the Servicing Office has not heard from you regarding our refinancing request, it appears that you are not taking advantage of historic low mortgage interest rates to refinance your home loan and reduce your interest rate.

We continue to encourage you to take advantage of refinancing opportunities. You may refinance your RHS loan at any time without penalty. Your loan remains subject to the refinancing requirement.

Sincerely,

[ insert name of Approval Official ]  
[ insert title of Approval Official ]

REFERENCE: Servicing and Asset Management Office Handbook Chapter 6

SUBJECT: RESPONSE TO REQUEST TO SALE FOR LESS THAN THE DEBT

*Date: [insert today's date]*

[ insert borrower(s) first/mi/last name(s) (Mr., Mrs., Ms.) ]  
[ insert borrower(s) street/post office address ]  
[ insert city, state, and zip code ]

RE: [ Type of Assistance Requested ]  
[ insert account # ]  
[ Residential Real Estate Located at (Popular Street Address of Property) ]

Dear [ insert borrower last name(s) (Mr., Mrs., Ms.) ]:

USDA Rural Development has reviewed your request for consent to allow you to sell the subject property for the sale price that you have proposed. USDA Rural Development consents to this sale and agrees to release its first mortgage lien upon receipt of net proceeds from the sale in an amount not less than \$\_\_\_\_\_. By approving this sale, the Agency is agreeing only to release its lien; however, you will remain obligated for repayment of any remaining debt. The remaining debt can be settled through the debt settlement process. For your convenience a Debt Settlement Application is enclosed for you to complete and return to the Servicing and Asset Management Office as instructed in the application.

- or -

USDA Rural Development has reviewed your request for consent to allow you to sell the subject property for the sale price that you have proposed and does not consent to this sale for the following reasons: [ insert specific reasons ]. Please contact the local field office at the above location for additional information.

Sincerely,

[ insert name of Rural Development Official ]  
[ insert title of Rural Development Official ]

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(05-27-98) SPECIAL PN

Revised (03-31-21) SPECIAL PN

APPENDIX 4  
7 CFR PART 11--NATIONAL APPEALS DIVISION RULES OF PROCEDURE

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#### 11.14 Filing of appeals and computation of time.

Authority: 5 U.S.C. 301; Title II, Subtitle H, Pub. L. 103-354, 108 Stat. 3228 (7 U.S.C. 6991 et seq.); Reorganization Plan No. 2 of 1953 (5 U.S.C. App.).

#### § 11.1 Definitions.

For purposes of this part:

Adverse decision means an administrative decision made by an officer, employee, or committee of an agency that is adverse to a participant. The term includes a denial of equitable relief by an agency or the failure of an agency to issue a decision or otherwise act on the request or right of the participant within timeframes specified by agency program statutes or regulations or within a reasonable time if timeframes are not specified in such statutes or regulations. The term does not include a decision over which the Board of Contract Appeals has jurisdiction.

Agency means:

- (1) The Agricultural Stabilization and Conservation Service (ASCS);
- (2) The Commodity Credit Corporation (CCC);
- (3) The Farm Service Agency (FSA);
- (4) The Farmers Home Administration (FmHA);
- (5) The Federal Crop Insurance Corporation (FCIC);
- (6) The Natural Resources Conservation Service (NRCS);
- (7) The Rural Business-Cooperative Service (RBS);
- (8) The Rural Development Administration (RDA);
- (9) The Rural Housing Service (RHS);
- (10) The Rural Utilities Service (RUS) (but not for programs authorized by the Rural Electrification Act of 1936 and the Rural Telephone Bank Act, 7 U.S.C. 901 et seq.);

(11) The Soil Conservation Service (SCS);

(12) A State, county, or area committee established under section 8(b)(5) of the Soil Conservation and Domestic Allotment Act (16 U.S.C. 590h(b)(5)); and

(13) Any successor agency to the above-named agencies, and any other agency or office of the Department which the Secretary may designate.

Agency record means all the materials maintained by an agency related to an adverse decision which are submitted to the Division by an agency for consideration in connection with an appeal under this part, including all materials prepared or reviewed by the agency during its consideration and decision-making process, but shall not include records or information not related to the adverse decision at issue. All materials contained in the agency record submitted to the Division shall be deemed admitted as evidence for purposes of a hearing or a record review under Sec. 11.8.

Agency representative means any person, whether or not an attorney, who is authorized to represent the agency in an administrative appeal under this part.

Appeal means a written request by a participant asking for review by the National Appeals Division of an adverse decision under this part.

Appellant means any participant who appeals an adverse decision in accordance with this part. Unless separately set forth in this part, the term "appellant" includes an authorized representative.

Authorized representative means any person, whether or not an attorney, who is authorized in writing by a participant, consistent with Sec. 11.6(c), to act for the participant in an administrative appeal under this part. The authorized representative may act on behalf of the participant except when the provisions of this part require action by the participant or appellant personally.

Case record means all the materials maintained by the Secretary related to an adverse decision. The case record includes both the agency record and the hearing record.

Days means calendar days unless otherwise specified.

Department means the United States Department of Agriculture (USDA).

Director means the Director of the Division or a designee of the Director.

Division means the National Appeals Division established by this part.

Equitable relief means relief which is authorized under section 326 of the Food and Agriculture Act of 1962 (7 U.S.C. 1339a) and other laws administered by the agency.

Ex parte communication means an oral or written communication to any officer or employee of the Division with respect to which reasonable prior notice to all parties is not given, but it shall not include requests for status reports, or inquiries on Division procedure, in reference to any matter or proceeding connected with the appeal involved.

Hearing, except with respect to Sec. 11.5, means a proceeding before the Division to afford a participant the opportunity to present testimony or documentary evidence or both in order to have a previous determination reversed and to show why an adverse determination was in error.

Hearing Officer means an individual employed by the Division who conducts the hearing and determines appeals of adverse decisions by any agency.

Hearing record means all documents, evidence, and other materials generated in relation to a hearing under Sec. 11.8.

Implement means the taking of action by an agency of the Department in order fully and promptly to effectuate a final determination of the Division.

Participant means any individual or entity who has applied for, or whose right to participate in or receive, a payment, loan, loan guarantee, or other benefit in accordance with any program of an agency to which the regulations in this part apply is affected by a decision of such agency. With respect to guaranteed loans made by FSA, both the borrower and the lender jointly must appeal an adverse decision except that the denial or reduction of a final loss payment to a lender shall be appealed by the lender only. The term does not include persons whose claim(s) arise under:

- (1) Programs subject to various proceedings provided for in 7 CFR part 1;
- (2) Programs governed by Federal contracting laws and regulations (appealable under other rules and to other forums, including to the Department's Board of Contract Appeals under 7 CFR part 24);
- (3) The Freedom of Information Act (appealable under 7 CFR part 1, subpart A);

- (4) Suspension and debarment disputes, including, but not limited to, those falling within the scope of 7 CFR parts 1407 and 3017;
- (5) Export programs administered by the Commodity Credit Corporation;
- (6) Disputes between reinsured companies and the Federal Crop Insurance Corporation;
- (7) Tenant grievances or appeals prosecutable under the provisions of 7 CFR part 1944, subpart L, under the multi-family housing program carried out by RHS;
- (8) Personnel, equal employment opportunity, and other similar disputes with any agency or office of the Department which arise out of the employment relationship;
- (9) The Federal Tort Claims Act, 28 U.S.C. 2671 et seq., or the Military Personnel and Civilian Employees Claims Act of 1964, 31 U.S.C. 3721; or
- (10) Discrimination complaints prosecutable under the nondiscrimination regulations at 7 CFR parts 15, 15a, 15b, and 15e.

Record review means an appeal considered by the Hearing Officer in which the Hearing Officer's determination is based on the agency record and other information submitted by the appellant and the agency, including information submitted by affidavit or declaration.

Secretary means the Secretary of Agriculture.

#### § 11.2 General statement.

(a) This part sets forth procedures for proceedings before the National Appeals Division within the Department. The Division is an organization within the Department, subject to the general supervision of and policy direction by the Secretary, which is independent from all other agencies and offices of the Department, including Department officials at the state and local level. The Director of the Division reports directly to the Secretary of

Agriculture. The authority of the Hearing Officers and the Director of the Division, and the administrative appeal procedures which must be followed by program participants who desire to appeal an adverse decision and by the agency which issued the adverse decision, are included in this part.

(b) Pursuant to section 212(e) of the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act of 1994, Public Law 103-354 (the Act), 7 U.S.C. 6912(e), program participants shall seek review of an adverse decision before a Hearing Officer of the Division, and may seek further review by the Director, under the provisions of this part prior to seeking judicial review.

### § 11.3 Applicability.

(a) Subject matter. The regulations contained in this part are applicable to adverse decisions made by an agency, including, for example, those with respect to:

- (1) Denial of participation in, or receipt of benefits under, any program of an agency;
- (2) Compliance with program requirements;
- (3) The making or amount of payments or other program benefits to a participant in any program of an agency; and
- (4) A determination that a parcel of land is a wetland or highly erodible land.

(b) Limitation. The procedures contained in this part may not be used to seek review of statutes or USDA regulations issued under Federal law.

### § 11.4 Inapplicability of other laws and regulations.

The provisions of the Administrative Procedure Act generally applicable to agency adjudications (5 U.S.C. 554, 555, 556, 557, & 3105) are not applicable to proceedings under this part. The Equal Access to Justice Act, as amended, 5 U.S.C. 504, does not apply to these proceedings. The Federal Rules of Evidence, 28 U.S.C. App., shall not apply to these proceedings.



§ 11.5 Informal review of adverse decisions.

(a) Required informal review of FSA adverse decisions. A participant must seek an informal review of an adverse decision issued at the field service office level by an officer or employee of FSA, or by any employee of a county or area committee established under section 8(b)(5) of the Soil Conservation and Domestic Allotment Act, 16 U.S.C. 590h(b)(5), before NAD will accept an appeal of an FSA adverse decision. Such informal review shall be done by the county or area committee with responsibility for the adverse decision at issue. The procedures for requesting such an informal review before FSA are found in 7 CFR part 780. After receiving a decision upon review by a county or area committee, a participant may seek further informal review by the State FSA committee or may appeal directly to NAD under Sec. 11.6(b).

(b) Optional informal review. With respect to adverse decisions issued at the State office level of FSA and adverse decisions of all other agencies, a participant may request an agency informal review of an adverse decision of that agency prior to appealing to NAD. Procedures for requesting such an informal review are found at 7 CFR part 780 (FSA), 7 CFR part 614 (NRCS), 7 CFR part 1900, subpart B (RUS), 7 CFR part 1900, subpart B (RBS), and 7 CFR part 1900, subpart B (RHS).

(c) Mediation. A participant also shall have the right to utilize any available alternative dispute resolution (ADR) or mediation program, including any mediation program available under title V of the Agriculture Credit Act of 1987, 7 U.S.C. 5101 et seq., in order to attempt to seek resolution of an adverse decision of an agency prior to a NAD hearing. If a participant:

(1) Requests mediation or ADR prior to filing an appeal with NAD, the participant stops the running of the 30-day period during which a participant may appeal to NAD under Sec. 11.6(b)(1), and will have the balance of days remaining in that period to appeal to NAD once mediation or ADR has concluded.

(2) Requests mediation or ADR after having filed an appeal to NAD under Sec. 11.6(b), but before the hearing, the participant will be deemed to have waived his right to have a hearing within 45 days under Sec. 11.8(c)(1) but shall have the right to have a hearing within 45 days after conclusion of mediation or ADR.

§ 11.6 Director review of agency determination of appealability and right of participants to Division hearing.

(a) Director review of agency determination of appealability.

(1) Not later than 30 days after the date on which a participant receives a determination from an agency that an agency decision is not appealable, the participant must submit a written request to the Director to review the determination in order to obtain such review by the Director.

(2) The Director shall determine whether the decision is adverse to the individual participant and thus appealable or is a matter of general applicability and thus not subject to appeal, and will issue a final determination notice that upholds or reverses the determination of the agency. This final determination is not appealable. If the Director reverses the determination of the agency, the Director will notify the participant and the agency of that decision and inform the participant of his or her right to proceed with an appeal.

(3) The Director may delegate his or her authority to conduct a review under this subsection to any subordinate official of the Division other than a Hearing Officer. In any case in which such review is conducted by such a subordinate official, the subordinate official's determination shall be considered to be the determination of the Director and shall be final and not appealable.

(b) Appeals of adverse decisions.

(1) To obtain a hearing under Sec. 11.8, a participant personally must request such hearing not later than 30 days after the date on which the participant first received notice of the adverse decision or after the date on which the participant receives notice of the Director's determination that a decision is appealable. In the case of the failure of an agency to act on the request or right of a recipient, a participant personally must request such hearing not later than 30 days after the participant knew or reasonably should have known that the agency had not acted within the timeframes specified by agency program regulations, or, where such regulations specify no timeframes, not later than 30 days after the participant reasonably should have known of the agency's failure to act.

(2) A request for a hearing shall be in writing and personally signed by the participant, and shall include a copy of the adverse decision to be reviewed, if available, along with a brief statement of the participant's reasons for believing that the decision, or the agency's failure to act, was wrong. The participant also shall send a copy of the request for a hearing to the agency, and may send a copy of the adverse decision to be reviewed to the agency, but failure to do either will not constitute grounds for dismissal of the appeal. Instead of a hearing, the participant may request a record review.

(c) If a participant is represented by an authorized representative, the authorized representative must file a declaration with NAD, executed in accordance with 28 U.S.C. 1746, stating that the participant has duly authorized the declarant in writing to represent the participant for purposes of a specified adverse decision or decisions, and attach a copy of the written authorization to the declaration.

#### § 11.7 Ex parte communications.

(a) Ex parte communications.

(1) At no time between the filing of an appeal and the issuance of a final determination under this part shall any officer or employee of the Division engage in ex parte communications regarding the merits of the appeal with any person having any interest in the appeal pending before the Division, including any person in an advocacy or investigative capacity. This prohibition does not apply to:

(i) Discussions of procedural matters related to an appeal; or

(ii) Discussions of the merits of the appeal where all parties to the appeal have been given notice and an opportunity to participate.

(2) In the case of a communication described in paragraph (a)(1)(ii) of this section, a memorandum of any such discussion shall be included in the hearing record.

(b) No interested person shall make or knowingly cause to be made to any officer or employee of the Division an ex parte communication relevant to the merits of the appeal.

(c) If any officer or employee of the Division receives an ex parte communication in violation of this section, the one who receives the communication shall place in the hearing record:

(1) All such written communications;

(2) Memoranda stating the substance of all such oral communications; and

(3) All written responses to such communications, and memoranda stating the substance of any oral responses thereto.

(d) Upon receipt of a communication knowingly made or knowingly caused to be made by a party in violation of this section the Hearing Officer or Director may, to the extent consistent with the interests of justice and the policy of the underlying program, require the party to show cause why such party's claim or interest in the appeal should not be dismissed, denied, disregarded, or otherwise adversely affected on account of such violation.

#### § 11.8 Division hearings.

##### (a) General rules.

(1) The Director, the Hearing Officer, and the appellant shall have access to the agency record of any adverse decision appealed to the Division for a hearing. Upon request by the appellant, the agency shall provide the appellant a copy of the agency record.

(2) The Director and Hearing Officer shall have the authority to administer oaths and affirmations, and to require, by subpoena, the attendance of witnesses and the production of evidence. A Hearing Officer shall obtain the concurrence of the Director prior to issuing a subpoena.

(i) A subpoena requiring the production of evidence may be requested and issued at any time while the case is pending before the Division.

(ii) An appellant or an agency, acting through any appropriate official, may request the issuance of a subpoena requiring the attendance of a witness by submitting such a request in writing at least 14 days before the scheduled date of a hearing. The Director or Hearing Officer shall issue a subpoena at least 7 days prior to the scheduled date of a hearing.

(iii) A subpoena shall be issued only if the Director or a Hearing Officer determines that:

(A) For a subpoena of documents, the appellant or the agency has established that production of documentary evidence is necessary and is reasonably calculated to lead to information which would affect the final determination or is necessary to fully present the case before the Division; or

(B) For a subpoena of a witness, the appellant or the agency has established that either a representative of the Department or a private individual possesses information that is pertinent and necessary for disclosure of all relevant facts which could impact the final determination, that the information cannot be obtained except through testimony of the person, and that the testimony cannot be obtained absent issuance of a subpoena.

(iv) The party requesting issuance of a subpoena shall arrange for service. Service of a subpoena upon a person named therein may be made by registered or certified mail, or in person. Personal service shall be made by personal delivery of a copy of the subpoena to the person named therein by any person who is not a party and who is not less than 18 years of age. Proof of service shall be made by filing with the Hearing Officer or Director who issued the subpoena a statement of the date and manner of service and of the names of the persons served, certified by the person who made the service in person or by return receipts for certified or registered mail.

(v) A party who requests that a subpoena be issued shall be responsible for the payment of any reasonable travel and subsistence costs incurred by the witness in connection with his or her appearance and any fees of a person who serves the subpoena in person. The Department shall pay the costs associated with the appearance of a Department employee whose role as a witness arises out of his or her performance of official duties, regardless of which party requested the subpoena. The failure to make payment of such charges on demand may be deemed by the Hearing Officer or Director as sufficient ground for striking the testimony of the witness and the evidence the witness has produced.

(vi) If a person refuses to obey a subpoena, the Director, acting through the Office of the General Counsel of the Department and the Department of Justice, may apply to the United States District Court in the jurisdiction where that person resides to have the subpoena enforced as provided in the Federal Rules of Civil Procedure (28 U.S.C. App.).

(3) Testimony required by subpoena pursuant to paragraph (a)(2) of this section may, at the discretion of the Director or a Hearing Officer, be presented at the hearing either in person or telephonically.

(b) Hearing procedures applicable to both record review and hearings.

(1) Upon the filing of an appeal under this part of an adverse decision by any agency, the agency promptly shall provide the Division with a copy of the agency record. If requested by the appellant prior to the hearing, a copy of such agency record shall be provided to the appellant by the agency within 10 days of receipt of the request by the agency.

(2) The Director shall assign the appeal to a Hearing Officer and shall notify the appellant and agency of such assignment. The notice also shall advise the appellant and the agency of the documents required to be submitted under paragraph (c)(2) of this section, and notify the appellant of the option of having a hearing by telephone.

(3) The Hearing Officer will receive evidence into the hearing record without regard to whether the evidence was known to the agency officer, employee, or committee making the adverse decision at the time the adverse decision was made.

(c) Procedures applicable only to hearings.

(1) Upon a timely request for a hearing under Sec. 11.6(b), an appellant has the right to have a hearing by the Division on any adverse decision within 45 days after the date of receipt of the request for the hearing by the Division.

(2) The Hearing Officer shall set a reasonable deadline for submission of the following documents:

(i) By the appellant:

(A) A short statement of why the decision is wrong;

(B) A copy of any document not in the agency record that the appellant anticipates introducing at the hearing; and

(C) A list of anticipated witnesses and brief descriptions of the evidence such witnesses will offer.

(ii) By the agency:

(A) A copy of the adverse decision challenged by the appellant;

(B) A written explanation of the agency's position, including the regulatory or statutory basis therefor;

(C) A copy of any document not in the agency record that the agency anticipates introducing at the hearing; and

(D) A list of anticipated witnesses and brief descriptions of the evidence such witnesses will offer.

(3) Not less than 14 days prior to the hearing, the Division must provide the appellant, the authorized representative, and the agency a notice of hearing specifying the date, time, and place of the hearing. The hearing will be held in the State of residence of the appellant, as determined by the Hearing Officer, or at a location that is otherwise convenient to the appellant, the agency, and the Division. The notice also shall notify all parties of the right to obtain an official record of the hearing.

(4) Pre-hearing conference. Whenever appropriate, the Hearing Officer shall hold a pre-hearing conference in order to attempt to resolve the dispute or to narrow the issues involved. Such pre-hearing conference shall be held by telephone unless the Hearing Officer and all parties agree to hold such conference in person.

(5) Conduct of the hearing.

(i) A hearing before a Hearing Officer will be in person unless the appellant agrees to a hearing by telephone.

(ii) The hearing will be conducted by the Hearing Officer in the manner determined by the Division most likely to obtain the facts relevant to the matter or matters at issue. The Hearing Officer will allow the presentation of evidence at the hearing by any party without regard to whether the evidence was known to the officer, employee, or committee of the agency making the adverse decision at the time the adverse decision was made. The Hearing Officer may confine the presentation of facts and evidence to pertinent matters and exclude irrelevant, immaterial, or unduly repetitious evidence, information, or questions. Any party shall have the opportunity to present oral and documentary evidence, oral testimony of witnesses, and arguments in support of the party's position; controvert evidence relied on by any other party; and question all witnesses. When appropriate, agency witnesses requested by the appellant will be made available at the hearing. Any evidence may be received by the Hearing Officer without regard to whether that evidence could be admitted in judicial proceedings.

(iii) An official record shall be made of the proceedings of every hearing. This record will be made by an official tape recording by the Division. In addition, either party may request that a verbatim transcript be made of the hearing proceedings and that such transcript shall be made the official record of the hearing. The party requesting a verbatim transcript shall pay for the transcription service, shall provide a certified copy of the transcript to the Hearing Officer free of charge, and shall allow any other party desiring to purchase a copy of the transcript to order it from the transcription service.

(6) Absence of parties.

(i) If at the time scheduled for the hearing either the appellant or the agency representative is absent, and no appearance is made on behalf of such absent party, or no arrangements have been made for rescheduling the hearing, the Hearing Officer has the option to cancel the hearing unless the absent party has good cause for the failure to appear. If the Hearing Officer elects to cancel the hearing, the Hearing Officer may:



(A) Treat the appeal as a record review and issue a determination based on the agency record as submitted by the agency and the hearing record developed prior to the hearing date;

(B) Accept evidence into the hearing record submitted by any party present at the hearing, and then issue a determination; or

(C) Dismiss the appeal.

(ii) When a hearing is cancelled due to the absence of a party, the Hearing Officer will add to the hearing record any additional evidence submitted by any party present, provide a copy of such evidence to the absent party or parties, and allow the absent party or parties 10 days to provide a response to such additional evidence for inclusion in the hearing record.

(iii) Where an absent party has demonstrated good cause for the failure to appear, the Hearing Officer shall reschedule the hearing unless all parties agree to proceed without a hearing.

(7) Post-hearing procedure. The Hearing Officer will leave the hearing record open after the hearing for 10 days, or for such other period of time as the Hearing Officer shall establish, to allow the submission of information by the appellant or the agency, to the extent necessary to respond to new facts, information, arguments, or evidence presented or raised at the hearing. Any such new information will be added by the Hearing Officer to the hearing record and sent to the other party or parties by the submitter of the information. The Hearing Officer, in his or her discretion, may permit the other party or parties to respond to this post-hearing submission.

(d) Interlocutory review. Interlocutory review by the Director of rulings of a Hearing Officer are not permitted under the procedures of this part.

(e) Burden of proof. The appellant has the burden of proving that the adverse decision of the agency was erroneous by a preponderance of the evidence.

(f) Timing of issuance of determination. The Hearing Officer will issue a notice of the determination on the appeal to the named appellant, the authorized representative, and the agency not later than 30 days after a hearing or the closing

date of the hearing record in cases in which the Hearing Officer receives additional evidence from the agency or appellant after a hearing. In the case of a record review, the Hearing Officer will issue a notice of determination within 45 days of receipt of the appellant's request for a record review. Upon the Hearing Officer's request, the Director may establish an earlier or later deadline. A notice of determination shall be accompanied by a copy of the procedures for filing a request for Director review under Sec. 11.9. If the determination is not appealed to the Director for review under Sec. 11.9, the notice provided by the Hearing Officer shall be considered to be a notice of a final determination under this part.

§ 11.9 Director review of determinations of Hearing Officers.

(a) Requests for Director review.

(1) Not later than 30 days after the date on which an appellant receives the determination of a Hearing Officer under Sec. 11.8, the appellant must submit a written request, signed personally by the named appellant, to the Director to review the determination in order to be entitled to such review by the Director. Such request shall include specific reasons why the appellant believes the determination is wrong.

(2) Not later than 15 business days after the date on which an agency receives the determination of a Hearing Officer under Sec. 11.8, the head of the agency may make a written request that the Director review the determination. Such request shall include specific reasons why the agency believes the determination is wrong, including citations of statutes or regulations that the agency believes the determination violates. Any such request may be made by the head of an agency only, or by a person acting in such capacity, but not by any subordinate officer of such agency.

(3) A copy of a request for Director review submitted under this paragraph (a) shall be provided simultaneously by the submitter to each party to the appeal.

(b) Notification of parties. The Director promptly shall notify all parties of receipt of a request for review.

(c) Responses to request for Director review. Other parties to an appeal may submit written responses to a request for Director review within 5 business days from the date of receipt of a copy of the request for review.

(d) Determination of Director.

(1) The Director will conduct a review of the determination of the Hearing Officer using the agency record, the hearing record, the request for review, any responses submitted under paragraph (c) of this section, and such other arguments or information as may be accepted by the Director, in order to determine whether the decision of the Hearing Officer is supported by substantial evidence. Based on such review, the Director will issue a final determination notice that upholds, reverses, or modifies the determination of the Hearing Officer. The Director's determination upon review of a Hearing Officer's decision shall be considered to be the final determination under this part and shall not be appealable. However, if the Director determines that the hearing record is inadequate or that new evidence has been submitted, the Director may remand all or a portion of the determination to the Hearing Officer for further proceedings to complete the hearing record or, at the option of the Director, to hold a new hearing.

(2) The Director will complete the review and either issue a final determination or remand the determination not later than--

(i) 10 business days after receipt of the request for review, in the case of a request by the head of an agency; or

(ii) 30 business days after receipt of the request for review, in the case of a request by an appellant.

(3) In any case or any category of cases, the Director may delegate his or her authority to conduct a review under this section to any Deputy or Associate Directors of the Division. In any case in which such review is conducted by a Deputy or Associate Director under authority delegated by the Director, the Deputy or Associate Director's determination shall be considered to be the determination of the Director under this part and shall be final and not appealable.

(e) Equitable relief. In reaching a decision on an appeal, the Director shall have the authority to grant equitable relief under this part in the same manner and to the same extent as such authority is provided an agency under applicable laws and regulations.

§ 11.10 Basis for determinations.

- (a) In making a determination, the Hearing Officers and the Director are not bound by previous findings of facts on which the agency's adverse decision was based.
- (b) In making a determination on the appeal, Hearing Officers and the Director shall ensure that the decision is consistent with the laws and regulations of the agency, and with the generally applicable interpretations of such laws and regulations.
- (c) All determinations of the Hearing Officers and the Director must be based on information from the case record, laws applicable to the matter at issue, and applicable regulations published in the Federal Register and in effect on the date of the adverse decision or the date on which the acts that gave rise to the adverse decision occurred, whichever date is appropriate under the applicable agency program laws and regulations.

§ 11.11 Reconsideration of Director determinations.

- (a) Reconsideration of a determination of the Director may be requested by the appellant or the agency within 10 days of receipt of the determination. The Director will not consider any request for reconsideration that does not contain a detailed statement of a material error of fact made in the determination, or a detailed explanation of how the determination is contrary to statute or regulation, which would justify reversal or modification of the determination.
- (b) The Director shall issue a notice to all parties as to whether a request for reconsideration meets the criteria in paragraph (a) of this section. If the request for reconsideration meets such criteria, the Director shall include a copy of the request for reconsideration in the notice to the non-requesting parties to the appeal. The non-requesting parties shall have 5 days from receipt of such notice from the Director to file a response to the request for reconsideration with the Director.
- (c) The Director shall issue a decision on the request for reconsideration within 5 days of receipt of responses from the non-requesting parties. If the Director's decision upon reconsideration reverses or modifies the final determination of the Director rendered under Sec. 11.9(d), the Director's decision on reconsideration will become the final determination of the Director under Sec. 11.9(d) for purposes of this part.

§ 11.12 Effective date and implementation of final determinations of the Division.

- (a) On the return of a case to an agency pursuant to the final determination of the Division, the head of the agency shall implement the final determination not later than 30 days after the effective date of the notice of the final determination.
- (b) A final determination will be effective as of the date of filing of an application, the date of the transaction or event in question, or the date of the original adverse decision, whichever is applicable under the applicable agency program statutes or regulations.

§ 11.13 Judicial review.

- (a) A final determination of the Division shall be reviewable and enforceable by any United States District Court of competent jurisdiction in accordance with chapter 7 of title 5, United States Code.
- (b) An appellant may not seek judicial review of any agency adverse decision appealable under this part without receiving a final determination from the Division pursuant to the procedures of this part.

§ 11.14 Filing of appeals and computation of time.

- (a) An appeal, a request for Director review, or any other document will be considered "filed" when delivered in writing to the Division, when postmarked, or when a complete facsimile copy is received by the Division.
- (b) Whenever the final date for any requirement of this part falls on a Saturday, Sunday, Federal holiday, or other day on which the Division is not open for the transaction of business during normal working hours, the time for filing will be extended to the close of business on the next working day.
- (c) The time for filing an appeal, a request for Director review, or any other document expires at 5:00 p.m. local time at the office of the Division to which the filing is submitted on the last day on which such filing may be made.

## APPENDIX 5

### APPRAISAL GUIDELINES *[7 CFR 3550.62]*

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#### A. SERVICING ACTIONS REQUIRING APPRAISALS

The Servicing Office may need to establish a property's market value in order to take several special servicing actions. In most cases the value of the property is determined through an appraisal.

When an appraisal is required, the Servicing Office will request assistance from the Field Staff. The Servicing Office may need to have an appraisal conducted when:

- The property's value is needed to determine the amount of subsidy subject to recapture.
- The borrower requests that a portion of the security property be released and the Agency needs to determine if the remainder has adequate value to secure the Agency's debt.
- The borrower offers a deed-in-lieu of foreclosure and the Agency must know the property's value to determine whether to accept the deed or pursue judicial foreclosure.
- The Agency needs to determine whether its lien has value.
- The Agency pursues foreclosure and it must know the property's value in order to establish the bid price.
- The Agency is considering making a protective advance and the Agency needs to determine if the property's value will support the advance.

#### B. APPRAISAL BASICS

Real estate appraisers make their judgments about a property's value based on many factors. These factors include: location, market conditions, construction quality, and amenities. Appraisers use two appraisal methods to arrive at a final estimate of value: the sales comparison approach and the cost approach. A third method of estimating value, a broker's price opinion (BPO), may be used under certain servicing action.

- **Sales comparison approach.** Using the recent sales price of properties that are very close in location and characteristics to the property to be appraised, the appraiser estimates a market value for the property, after correcting for differences such as location, physical characteristics, and market conditions.

- **Cost approach.** Under this method the appraiser uses standard estimates of the cost to construct the subject dwelling and an estimate of the site value to derive an estimate of value.
- **BPO.** A BPO is a statement by a licensed real estate broker as to the market value of a piece of property. A BPO may be authorized for use in limited circumstances.

The procedures appraisers must follow are found at the end of this Appendix. Depending on the purpose of the proposed loan, an appraiser will either give the estimated value of the property in its current condition (called the “as is” value ), or, based on construction plans and specifications, give the estimated value of the property after development (called the “as developed/ improved” value). The “as is” value will be used for most Servicing Office actions.

### C. APPRAISAL ORDERS

The Servicing Office may use one of the following methods to order an appraisal: (1) it may request one from Field Staff; or (2) it may use local appraisers located throughout the country who are under contract with the Servicing Office.

Field Staff should order appraisals within 7 days of receiving the work queue from the Servicing Office. In-house appraisals are to be completed within 30 days of the appraisal order. Contract appraisals are to be completed within the time specified on the contract; this should generally not exceed 30 days.

### D. DUE DILIGENCE

The appropriate level of due diligence must be performed in conjunction with the appraisal for all servicing activities that require a determination of market value. Due diligence is the process of inquiring into the environmental condition of real estate in the context of a real estate

#### Appraisals in Remote Rural Areas or Tribal Lands

In remote rural areas and on Tribal lands, a lack of comparables can make it difficult to appraise a new construction property. In these areas, the sales comparison approach is not required. Instead, *Form 1007, Marshall and Swift Square Foot Appraisal* must be used. These appraisals must be conducted by Agency staff with appraisal authority; they cannot be done by contract appraisers.

Remote rural areas are defined as areas with all of the following characteristics:

- Scattered population;
- Low density of residences;
- Lack of basic shopping facilities;
- Lack of community and public services and facilities; and
- Lack of comparable sales data.

transaction to determine the presence of contamination from hazardous substances, hazardous wastes, or petroleum products. Due diligence also requires the determination of what impact such contamination may have on the market value of the property. Due diligence must be initiated by completing the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)*, the initial level of inquiry in the due diligence process. If the completed TSQ raises any concerns, it must be sent to the appropriate Environmental Coordinator for further evaluation and guidance.

## **E. REVIEWING APPRAISALS**

The Servicing Office should review each contract appraisal after it is received to determine the property's value. (Field Staff will conduct these reviews before sending the appraisals to the Servicing Office; therefore these reviews are unnecessary for Field-generated appraisals.) Appraisals will be reviewed for accuracy through a combination of administrative reviews and random spot-checks. If an appraisal is found to be unacceptable by any review, a new appraisal should be ordered and acceptably completed before the servicing action can continue.

### **1. Administrative Review**

Administrative reviews are the least detailed of the reviews. They are to be performed on all contract or fee appraisals. This review determines whether the appraisal is complete, the mathematics are correct, there is a proper number of current comparables, and that both the cost and the comparable sales approaches were used to establish market value. The review should be completed as soon as possible, but must be completed within 7 days of the receipt of the appraisal.

A completed administrative review is necessary to authorize payment of a contract appraiser. The invoice cannot be paid until the appraisal review is complete.

### **2. Technical Review**

A technical review is performed to determine whether the appraisal made by the appraiser was complete, with clear reasoning and adequate support for the conclusion of value. Technical reviews will be completed for the first appraisal conducted by any contract or fee appraiser. Additional technical reviews may be ordered if there were problems encountered on the first technical review. In addition to the initial review, technical reviews will be done in a random, spot-check method for both contract and in-house appraisals.

A technical review may also be conducted when problems are detected by the administrative review. These problems must be significant and result in an appraisal that does not support the concluded value. The Servicing Office will determine whether a technical review is merited prior to recommending payment of the appraiser and approval of the loan.



### **3. Entering the Appraisal Results**

After the review, if the appraisal is found to be acceptable, the Servicing Office should enter the property's appraised value into MortgageServ. If the appraisal is acceptable, the Servicing Office should use the property's appraised value to make its decision regarding the servicing action being contemplated.

### ***F. PAYING FOR APPRAISALS [7 CFR 3550.62(b)]***

The Agency will charge borrowers a fee for each servicing action that requires an appraisal. The charge to the applicant will be \$280, and the fee will be charged to the borrower's account.

## CHAPTER 1: OVERVIEW

### SECTION 1: INTRODUCTION TO THE SERVICING AND ASSET MANAGEMENT OFFICE HANDBOOK

#### 1.1 WELCOME TO THE SERVICING AND ASSET MANAGEMENT OFFICE HANDBOOK

This handbook provides Agency staff with the tools needed to service loans efficiently and effectively. Its goal is to help staff at the Servicing and Asset Management Office (Servicing Office), assist borrowers, while making sure that basic legal and administrative requirements are met. The handbook provides loan servicing policies for Section 502 direct loans and Section 504 loans and grants. Specific procedures to implement these policies are described in a separate handbook.

The guidance provided by this handbook is intended to be consistent with all applicable laws, Executive Orders, and Departmental regulations, including other Agency regulations. Nothing contained in this handbook should be construed to supersede, rescind, or otherwise amend such laws, Executive Orders, and regulations.




#### 1.2 USING THIS HANDBOOK

The handbook is organized to allow the reader to look up information on specific topics easily. New staff may want to read the handbook in its entirety, while more experienced staff may use it as a reference book. Several graphic tools and conventions have been used to make information easier to find and understand.


##### A. Handbook Symbols

- **References.** The book symbol directs the reader to additional information sources, such as laws, regulations, or instructions.



- **State Supplements.** State and local laws and the laws of Federally-recognized tribes may affect how Agency requirements are implemented. Topics commonly affected by such laws include the treatment of liens, the liquidation process, and environmental policies. The United States symbol denotes subjects for which further instructions may be issued through State Supplements which will be filed in Appendix 7 of this Handbook or for which individual State laws are likely to be particularly relevant. 
- **Civil rights.** The fair housing symbol highlights processing procedures with significant fair housing or civil rights implications. 
- **Deadlines.** Time frames for completing required actions are underlined to make them easier to locate, for example: “within 7 days.” Unless the text specifies business days, all references to days are in terms of calendar days.
- **Documentation.** The notepad symbol highlights key activities or information that must be carefully documented. 

## B. Citations and Text Boxes

- **Regulatory citations.** The regulation for the direct single family housing program is provided in 7 CFR Part 3550. The text of that regulation is provided in Appendix 1. To help readers locate the regulatory authority for procedures described here, references to this regulation appear in italicized brackets, for example: [*7 CFR 3550.55*]. Other regulations or RD instructions are simply referenced.
- **Form and letter references.** Agency forms and Agency handbook (HB) letters are shown in *italics*. All forms referenced in this Handbook can be found in Appendix 2 and all handbook letters can be found in Appendix 3.
- **Helpful hints.** Helpful hints, cautions, or important facts are included in boxes throughout the text and shown with the string around the finger symbol. 
- **Examples and exhibits.** Text boxes labeled as examples or exhibits provide a specific illustration of a concept described in the text or provide additional detailed information. Examples are used when the text box is inserted adjacent to the relevant text and is not referenced. Exhibits are used when the text refers to the text box. Exhibits are numbered in sequence, using the chapter number; for example, Exhibit 3-1 is the first exhibit in Chapter 3.

### C. Attachments and Appendices

- **Glossary and acronyms lists.** Key words and terms are defined in the glossary. A list of acronyms used in the handbook is also provided. Both the glossary and list of acronyms can be found at the end of the handbook.
- **Attachments.** Attachments at the end of each chapter contain technical information that is specific to the topics covered in the chapter. Attachments are referenced in sequence, using the chapter number and a letter, for example, Attachment 4-A is the first attachment in Chapter 4.
- **Appendices.** Appendices at the end of the handbook include forms and other reference materials that relate to multiple chapters.

### D. Terminology

Because terminology may vary from State to State and change over time, this handbook uses certain standard terminology to provide consistency.

- **Agency.** The term “Agency” is used throughout this handbook to refer to the organizational unit within the United States Department of Agriculture (USDA) that is responsible for administration of the direct single family housing program.
- **Borrower.** The term “borrower” refers to one or more individuals who are receiving Agency assistance.
- **Servicing Office.** These terms are used to refer to individuals in the Servicing and Asset Management Office, previously known as, the National and Financial Operations Center, Customer Service Center, or Centralized Servicing Center. This term is used throughout this handbook to refer to the office that services loans and grants.
- **Field Office.** Because the number of offices and the nature of the work conducted in each office may vary from State to State, the term “Field Office” is used throughout this handbook to refer to the office that is originating the loan.
- **Field Staff and Approval Official.** These terms refer to a person who is completing tasks for purposes other than originating a loan and is located in the field.

## **E. How This Handbook Is Organized**

- **Chapter 1. Overview** provides a summary of Section 502 and Section 504 requirements, and also contains general program and administrative requirements that are referenced throughout the remaining chapters (for example, appeals and civil rights policies).
  - **Chapter 2. Regular Servicing** covers the transfer of responsibility for a loan from the Field Office to the Servicing Office and discusses routine transactions with the borrower, including payments, reviewing requests from the borrower that require Agency approval, final payments, and recapture. Guidance for two of the regular servicing activities -- processing payment subsidies and requirements related to taxes and insurance -- are large enough to require separate chapters, which follow.
  - **Chapter 3. Escrow, Taxes, and Insurance** covers the Agency's role in administering escrow accounts for taxes and insurance, borrower responsibilities regarding taxes and insurance, and remedies that may be applied if the borrower fails to pay taxes or insurance.
  - **Chapter 4. Payment Subsidies and Income Determinations** includes instructions for initiating and renewing payment subsidies, including guidance on making income determinations.
  - **Chapter 5. Special Servicing** covers servicing actions that may be required to assist borrowers who become delinquent on their accounts including delinquency workout agreements, moratoriums on payments, protective advances, and reamortization.
  - **Chapter 6. Liquidation and Acquisition** provides guidance for circumstances in which special servicing actions have failed and the borrower's account must be liquidated by foreclosure.
- Chapter 7. Special Collections** describes policies for dealing with unauthorized assistance, offsets, and debt settlement.

## SECTION 2: OVERVIEW OF THE DIRECT SINGLE FAMILY HOUSING PROGRAM

### 1.3 GOALS OF THE DIRECT SINGLE FAMILY HOUSING PROGRAM

The purpose of the direct single family housing program is to provide low- and very low-income people the opportunity to own adequate, modest, decent, safe, and sanitary homes in rural areas. In providing this service, the Agency strives to meet several goals.

- **Customer service.** The Agency is committed to providing customer-friendly, streamlined service.
- **Effective use of resources.** As a publicly-funded program, the direct single family housing program must use tax dollars efficiently. The Agency aims to minimize administrative costs and service loans responsibly.
- **Efficient processing.** The Agency has streamlined its servicing processes and adopted private sector practices to the extent feasible. This not only saves staff time, but also allows borrowers to receive the maximum benefit from Agency funds.

### 1.4 SECTION 502 -- AN OVERVIEW

#### A. Program Loans

The Section 502 direct loan program is intended to provide very low- and low-income people with the opportunity to acquire, build, rehabilitate, improve, or relocate dwellings in rural areas. The standard term for a Section 502 loan is 33 years. However, loans may be made for a shorter term, and in certain cases for 38 years. Each loan is made at a note rate established by the Agency as prescribed in RD Instruction 440.1. Payment subsidies are available to some borrowers to reduce monthly loan payments. In summary, to be eligible for a Section 502 loan, applicants must:



- Have an adjusted income that is at or below the applicable low-income limit at loan approval (except for assumed loans or loans to purchase Real Estate Owned (REO) property);
- Have an adjusted income that is at or below the applicable moderate-income limit for assumed loans or loans to purchase an REO property;

- Be unable to obtain sufficient credit from another source;
- Agree to personally occupy the dwelling;
- Meet citizenship or eligible non-citizen requirements;
- Have the legal capacity to incur a loan obligation and not be suspended or debarred from participation in Federal programs; and
- Demonstrate both the willingness and ability to repay the loan.

### **B. Nonprogram Loans**

The Agency may provide credit on non-program terms to expedite the assumption of an existing program loan or purchase of a REO property by a borrower who is not eligible for the Section 502 program. Other uses include conversion of a program loan that has received unauthorized assistance, or continuation of a loan after a partial release of security. Nonprogram loans are made only when it is in the best interest of the Government, and non-program borrowers are not eligible for certain special servicing actions.

## **1.5 SECTION 504 -- AN OVERVIEW**

The Section 504 direct loan and grant program is intended to provide funds to homeowners who cannot obtain other credit to repair and rehabilitate their properties or correct health and safety hazards. To be eligible, the applicant must have adjusted income that is at or below the applicable very low-income limit and meet other eligibility requirements similar to those for Section 502 loans. The Section 504 program offers grants to correct health and safety hazards for homeowners 62 years of age and older who cannot obtain a loan for this purpose.

### **A. Section 504 Grants**

Grant funds may be used only to make repairs and improvements that will remove identified health and safety hazards or to repair or remodel dwellings to make them accessible and useable for household members with disabilities. Grants are available only to eligible applicants who are 62 years of age or older. Recipients may receive multiple grants, up to a lifetime maximum of \$7,500.

## Paragraph 1.5 Section 504 -- An Overview

**B. Section 504 Loans**

Loan funds may be used to make general repairs and improvements to properties and to remove health and safety hazards. Borrowers may obtain multiple Section 504 loans, but the sum of the outstanding balance on all Section 504 loans cannot exceed \$20,000. The loans have a maximum term of 20 years and an interest rate of 1 percent.

**1.6 THE ROLE OF FIELD OFFICES**

Loans are originated and closed in Field Offices. Once loans are closed and the final disbursement has been made, they are serviced by the Servicing Office. The Servicing Office may ask for assistance from Field Staff when a local presence is needed to facilitate a servicing action.

In addition, Field Staff have an obligation to report information that comes to their attention indicating risks to the security property or changes in borrower circumstances. Such items might include knowledge of hazardous dwelling conditions, environmental hazards, non-occupancy, abandonment, or changes in income. Field Staff who learn of borrower difficulties also may recommend that the borrower contact the Servicing Office for assistance.



HB-2-3550

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## SECTION 3: AUTOMATION

### 1.7 THE DEDICATED LOAN ORIGATION AND SERVICING (DLOS) SYSTEM

The Agency's Dedicated Loan Origination and Servicing (DLOS) system is designed to expedite loan-making, standardize information collection and recordkeeping, and facilitate communication between Field Offices and the Servicing Office. DLOS tracks loans from application through servicing using two interconnected systems: UniFi and LoanServ.

#### A. UniFi

UniFi is a web-based application used for loan origination. It retains applicant information, makes complex calculations, and maintains a central record of all activities associated with an individual application from the time of pre-qualification through loan closing. Information from UniFi is uploaded into LoanServ each night.

#### B. LoanServ

LoanServ is a mainframe-based application that is used to service Agency loans and monitor loan performance. LoanServ should be used to record every action taken by the Servicing Office regarding an individual borrower's account.



#### LoanServ Advantages

Using LoanServ consistently will allow different operators at Servicing Office to work with a borrower's account at different times.

Since Field Offices have access to some portions of LoanServ, it can help the Servicing Office and Field Staff keep abreast of each other's activities. If the Servicing Office needs assistance in the field for some servicing action, LoanServ can be used to send a work queue to the Field Staff. For example, a Servicer involved in working out an insurance claim with a borrower might ask Field Staff to visit the property to assess the repair work that has been done to date. Similarly, if Field Staff obtain information about a change in a borrower's employment status that has not been reported to the Servicing Office, the LoanServ work queue can be used to pass that information on to the Servicing Office.

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## SECTION 4: GENERAL PROGRAM REQUIREMENTS

### 1.8 CIVIL RIGHTS [7 CFR 3550.3]



The Agency will administer its programs fairly and in accordance with both the letter and the spirit of all equal opportunity and fair housing legislation and applicable Executive Orders. The civil rights compliance requirements for the Agency are contained in RD Instruction 1901-E. Exhibit 1-1 lists the applicable Federal laws and Executive Orders and highlights key aspects of these requirements.



#### Exhibit 1-1


#### Major Civil Rights Laws Affecting the Direct Single Family Loan Program

- **Equal Credit Opportunity Act (ECOA).** Prohibits discrimination in the extension of credit on the basis of race, color, religion, national origin, sex, marital status, age, income from public assistance and exercise of rights under the Consumer Protection Act.
- **Title VI of the Civil Rights Act of 1964.** Prohibits discrimination in a Federally-assisted program on the basis of race, color, and national origin.
- **Title VIII of the Civil Rights Act of 1968** (also known as the Fair Housing Act of 1988, as amended). Prohibits discrimination in the sale, rental or financing of housing on the basis of race, color, religion, sex, national origin, familial status, or disability.
- **Section 504 of the Rehabilitation Act of 1973.** Prohibits discrimination in a Federally-conducted program on the basis of disability.
- **Age Discrimination Act of 1975.** Prohibits discrimination in a Federally-assisted program on the basis of age.
- **Executive Order 11063 as Amended by 12259.** Prohibits discrimination in housing or residential property financing to any Federal-assisted activity against individuals on the basis of race, color, religion, sex, or national origin.
- **Executive Order 11246.** Nondiscrimination in employment by construction contractors (and subcontractors) receiving Federally-assisted construction contracts in excess of \$10,000. It provides for equal employment opportunity without regard to race, color, religion, sex, and national origin.
- **Executive Order 13166.** Prohibits discrimination on the basis of national origin, and ensures programs normally provided in English are accessible to persons with Limited English Proficiency (LEP).

## A. Nondiscrimination

The various civil rights laws prohibit the denial of loans, grants, services, and benefits provided under the Section 502 and 504 programs to any person based upon race, color, national origin, sex, religion, marital status, familial status, age, physical or mental disability, source of income, or because the applicant has, in good faith, exercised any right under the Consumer Credit Protection Act (15 U.S.C. 1601). Discrimination in employment practices also is prohibited.

Effective management and consistent procedures are good business practices that help ensure that all borrowers are treated fairly. Poor program implementation, whether or not discrimination is intended, has possible civil rights consequences.

	<b>Key Civil Rights Issues for Loan Servicers</b>
<ul style="list-style-type: none"><li>• Access</li><li>• Consistency and fairness of treatment</li><li>• Disparate impacts -- intended or unintended</li><li>• Record keeping</li></ul>	

In the servicing process, attention to consistent procedures is especially important in several key areas, which are listed below.

- **Outreach.** Information about the availability of servicing relief and how to apply must be broadly disseminated. In addition, the extent of the information, assistance, and courtesy extended to those who make inquiries must be consistent.
- **Determining eligibility.** Servicers must use equal rigor for all borrowers when verifying income, considering eligibility for program benefits and assistance, and allowing borrowers to clarify information.
- **Making exceptions.** Standards for offering exceptions must be applied consistently.

## Paragraph 1.8 Civil Rights [7 CFR 3550.3]

- **Subsidies and other assistance.** Opportunities for subsidies and favorable servicing remedies must be made available consistently.
- **Hearings and appeals.** Avenues for remedies when problems arise must be made available consistently.

**B. Reasonable Accommodations for Persons with Disabilities [7 CFR 15e.130]**

No individual with a disability shall, on the basis of their disability, be excluded from participation in, be denied the benefits of, or otherwise be subjected to discrimination under any program or activity conducted by the agency. The Agency must make reasonable accommodations to permit persons with disabilities equal access to apply for and benefit from Agency programs. Reasonable accommodations may include providing facilities that are physically accessible so that all people can come to Agency offices, effective communication and outreach tools so that all applicants can get good program information (for example, a Telecommunications Device for the Deaf (TDD)), or making a modification to an Agency process or procedure to enable access.

When a customer with a disability cannot access a program or finds it difficult to meet a specific requirement of a program, the Agency must consider if the same result can be reached through different means. The Agency does not distinguish between reasonable accommodations and reasonable modifications. Instead, both are captured by the term “reasonable accommodations.” Under the regulations, the Agency must follow the requirement to make reasonable accommodations through changes that may be necessary to provide equal opportunity to participate in the federally conducted program or activity.

**1.9 REVIEW AND APPEALS [7 CFR 3550.4]****A. ADVERSE DECISIONS**

Decisions that are not made in favor of a program participant (applicant or borrower) are known as adverse decisions. Adverse decisions must be based upon regulations which are published in the Code of Federal Regulations (CFR). For the direct SFH programs, any adverse decisions must be based upon 7 CFR Part 3550 (Appendix 1) and not the administrative guidance contained in this Handbook. Adverse decisions include: (1) administrative actions taken by Agency officials; and (2) the Agency’s failure to take required actions within time frames specified in statutes or regulations, or within a reasonable time if no deadline is specified. [7 CFR Part 11](#) is the National Appeals Division (NAD) regulation and provides procedures that both Agency officials and program participants must follow when an adverse decision is appealed. If the Servicing Office is taking an adverse action on a case that is also under the jurisdiction of a Field Office, the Servicing Office should first consult with the Field Office. *Handbook Letter 101(3550), Standardized Adverse Decision Letter*, will be used for all adverse decisions unless another format is prescribed in this Handbook. Exhibit 1-2 provides a sample of an adverse decision letter.



**Exhibit 1-2**

**Sample Adverse Decision Letter**

Mr. and Mrs. John Doe  
1 Main Street  
Anytown, Anywhere 01234

Re: Application for \$154,000 Direct  
Single Family Housing Loan

Dear Mr. & Mrs. Doe,

Thank you for the opportunity to consider your request for Rural Development assistance. In reviewing your request, we considered all information submitted to the Agency and the regulations that govern the assistance for which you applied. After careful review, we regret to inform you that we were unable to take favorable action on your request. The specific reasons for our decision are as follows:

1. Your income exceeds the maximum income to qualify for our direct single family housing program. 7 CFR 3550.53(a) requires that an applicant's income must not exceed the applicable low-income limit for the area. In Any County, the maximum income limit is \$39,500. According to income reported on your application and verified using paystubs and tax returns., your income was calculated at \$42,250. Unfortunately, this income exceeds the applicable limits. At the time of your loan interview, Mr. Doe indicated that he worked substantial overtime last year, and did not anticipate overtime income for this year. According to a verification of employment, overtime income has recently been earned this year, and your employer anticipates that you will earn at least the same amount of overtime this year as you have earned in the past. Overtime income must be considered if it is reasonable to anticipate it will continue. We reverified with your employer that, because of recent workforce changes, overtime will continue this year in an amount at least equal to last year. This was further confirmed by copies of paystubs which you recently submitted to this office for review.

2. Your credit history was not acceptable. 7 CFR 3550.53(h) requires that an applicant must have an acceptable credit history to obtain program assistance. The regulation provides, in part, that a delinquency on any debt owed to the Federal Government is an indicator of unacceptable credit. Your credit report reflected that you are in default on your student loan which is guaranteed by the Federal Government.

If one of the above reasons included an unacceptable credit history, please note that a tri-merge credit report on you was obtained from Equifax Mortgage Solutions, 815 East Gate, Suite 102, Mount Laurel, NJ 08054; telephone (800) 333-0037. You may obtain a free copy of your credit report from Equifax and dispute the accuracy or completeness of the report directly to Equifax. While the report was provided by Equifax, the decision to deny your request for assistance was made by this Agency and not Equifax.

If you believe our decision is incorrect, or the facts used in this case are in error, you may pursue your rights to challenge our decision. Please see the attached for your rights.

Sincerely,

## Paragraph 1.9 Reviews and Appeals [7 CFR 3550.4]

Letters notifying participants of adverse decisions must contain the necessary information regarding an informal administrative meeting, mediation/Alternative Dispute Resolution (ADR), appeal rights to NAD, and civil rights. Attachments 1-A through 1-G contain, as necessary, the civil rights language and include information on requesting an informal administrative review, mediation and rights to NAD. The Attachments are all titled to assist the Servicing Office in selecting the correct Attachment for the decision being made. The Attachments do not need to be used when an RD Form, Handbook Letter, or other document already includes the appropriate participant rights.

### B. State Director Responsibilities

State Directors should issue a State Supplement providing guidance for processing appeal and mediation requests. The guidance should include an attachment outlining the mediation provider(s) specific to their State and identifying an Alternative Dispute Resolution (ADR) Coordinator.

### C. ADR Coordinator Responsibilities

The ADR Coordinator is responsible for: Establishing a source/vendor list of Community-Based Mediation Centers (CBMCs) and/or Alternative Mediation Service Providers, per RD Instruction 1940-E, 1940.206 (c)(1), if the State does not have a USDA-funded mediation program. The list will be maintained annually in alphabetical order and the providers are selected in sequential order. States will need to maintain documentation to ensure that mediation providers receive an equal number of referrals. The list should include the name, contact information, and cost of each mediator; the list cannot include arbitrators. The Farm Service Agency (FSA) should be able to provide the ADR Coordinator with a list of acceptable mediation sources in the State. Other contacts include the National Association of Conflict Resolution or State bar association. When making contacts with these sources, make sure the Agency requests the services of a mediator and not an arbitrator. A mediator resolves disputes by negotiating a resolution through mutual agreement. An arbitrator resolves disputes through hearing both parties and then rendering a binding decision and may not be used.

- Verifying that the request for mediation was submitted within 30 days of receipt of the adverse action. If so, issuing Attachment 1-D to the program participant. If the State does not have a USDA-funded mediation program, the program participant will have 10 days to select a mediation service provider. If a selection is not made within the allotted time, issuing Attachment 1-F to notify the program participant of the expiration to select a mediation service provider.



- Issuing Attachment 1-E to initiate mediation services to the selected provider.
- Ensuring the mediation is conducted within 45 days of receipt of the request.
- Issuing Attachment 1-G to the program participant if the mediation did not resolve the dispute.
- Communicating with all parties involved and ensuring they have a copy of the mediation documentation.

The ADR Coordinator is not responsible for attending mediations and hearings; that responsibility belongs to the Agency representative.

#### D. Agency Representative (Appeal Coordinator) Responsibilities

When the Servicing Office is taking an adverse action that is not under the jurisdiction of the Field Office, the Appeal Coordinator will represent the Agency; however, occasionally, another appropriate staff member may represent the Agency. The Appeal Coordinator is responsible for:

- Furnishing documentation that supports the adverse decision. Since the documentation is based on the adverse decision letter, the Appeal Coordinator needs to ensure that adverse decision letters list all the reasons for the denial and contains a brief narrative, the applicable program provisions, and pertinent facts.
- Representing the Agency in mediations and hearings. This may include a Servicing Office face-to-face hearing involving a servicing matter where the Servicing Office Appeals Coordinator requested the State Director to appoint Field Staff to attend the hearing and represent the Servicing Office. The Servicing Office Appeals Coordinator will provide sufficient documentation and phone resources to the person selected by the State Director to adequately represent the Agency in the case.
- Implementing the mediation/NAD decision within 30 days after the effective date of notice of the final determination.

### 1.10 AGENCY DECISIONS

#### A. Informal Administrative Review

When an Agency official makes a decision that will adversely affect a program participant, the participant is entitled to an opportunity for a separate informal administrative review by the decision maker or next level supervisor. The Agency official must give the program participant notice of their right to this review no later than 10 days after the date of adverse decision. If the

## Paragraph 1.10 Agency Decisions [7 CFR 3550.4]

Informal review does not result in a resolution of the matter, Attachment 1-A, Informal Administrative Review, will be sent within 7 days.

### B. Appealable Decisions

Attachment 1-B will be provided to the participant no later than 10 days after the adverse decision, which includes rights to seek a mediation/ADR with the Alternative Dispute Resolution (ADR) and/or request a hearing with National Appeals Division (NAD).

In cases where denial of assistance is based upon both appealable and non-appealable actions, the denial of assistance is not appealable. Attachment 1-C will be used in these cases and will include all reasons for the adverse decision.

### C. Non-Appealable Decisions

Certain decisions made by the Agency cannot be appealed. In these cases, the participant is still offered an opportunity for an informal administrative review; however, appeal rights to NAD and mediation are not offered. The participant will be informed no later than 10 days after the adverse decision using Attachment 1-C, Non-Appealable Decision, which provides an opportunity to request an informal administrative review and/or NAD request to review the accuracy of the Agency's decision.

## 1.11 Participant Rights

The program participant can request applicable appeal options below within 30 days of receipt of the adverse action. The requests for an appeal can be submitted simultaneously; however, the options below should be performed in order. If an applicant chooses to skip any of the options below, doing so will waive their right to the previous option.



The program participant has the right to a face-to-face hearing in the participant's State of residence. The program participant also has the right to request that the hearing be handled by teleconference or a may choose a Record Review.

### A. Informal Administrative Review

The program participant must make a request for an informal review in writing, and the request will be retained in the participant's case file. The borrower must submit a written request within 30 calendar days from when they receive an adverse decision letter. If unable to determine when the letter was received, count 7 calendar days after the date of the adverse decision letter (letter date + 7 days = receipt date of letter + 30 days = 37 days when request must be made). The informal administrative review can be conducted by the decision maker or representative

of the Agency through a telephone or face-to-face meeting at the Agency's discretion. The purpose of the informal administrative review is to further explain the Agency's reasons for the adverse decision, listen to why the participant feels the decision may be incorrect, and obtain any further information from the participant to support their request. The review must be completed within 45 days of the request. The participant will be notified of the outcome in writing using Attachment 1-A. The State Director may require that the decision be reviewed by the next-level supervisor or other designated Rural Development official prior to notifying the participant of the decision.

## B. Mediation

Adverse decisions which are appealable to NAD also require that the participant be given the opportunity to seek mediation prior to conducting a hearing with NAD. The purpose of mediation is to resolve disputes through the use of a neutral mediator. Mediation must be completed within 45 days after the case is referred to the mediation source, unless the complexity of the case warrants a longer time frame and all parties agree to a specific time frame. A mediator will generally conduct a teleconference between the parties prior to accepting a case to determine if the case can be mediated.

There is generally a cost associated with participation in mediation. The cost is contingent upon the service provider. When there are costs, they will be shared equally between the Agency and the program participant, if Agency funds are available. Where Agency program funds are not available, the Agency will participate in mediation if requested by the program participant; however, the program participant will be notified in advance of the portion of the cost the Agency will pay (if any) and their estimated cost for this service. The State Director will ensure that all participants requesting mediation in their State are treated consistently and pay the same percentage of the cost toward this service. The State Director may also consent to pay a larger percentage (up to 100 percent) of the cost of mediation for participants with incomes below the federal poverty level. The Agency will issue Attachments 1-E and 1-F, notifying the participant a mediation source selected and cost of such service. If State funds are unavailable, the State Office PLCE Initiator will request Program Loan Cost Expense (PLCE) "A" funds from the National Office Budget Execution Branch. The State will provide a list of acceptable mediators to the participant and request the participant to select or provide an additional acceptable provider within 10 days.

If the program participant does not provide the name of a mediation provider within 10 days, Attachment 1-F is used to notify the program participant of expiration and their request for mediation will be considered withdrawn. Withdrawal or cancellation of a mediation does not extinguish the participant's right to request an appeal with NAD. There are three types of mediation services as follows:

## Paragraph 1.11 Participant Rights [7 CFR 3550.4]

- **USDA-funded mediation program**

Many States have a mediation program that is annually certified by USDA. These programs are funded, in part, by USDA, and were established primarily to mediate cases originating from the Farm Service Agency (FSA). In States with a USDA-funded mediation program, program participants who are provided appeal rights will be generally referred to the USDA-funded mediation program. In States where alternative mediation sources are readily available at a lower cost than the USDA-funded mediation program, the State will follow the guidance for States with a CBMC or States without a USDA-funded mediation program, and include the USDA mediation program on the list of acceptable providers.

- **Community-Based Mediation Center**

A CBMC is a nonprofit, public entity operating under the guidance of a governing board. Its goal is to provide an alternative to the judicial system by the use of trained mediators located in the geographical area served. The CBMC provides mediation services to clients regardless of their ability to pay. In States without a USDA-funded State mediation program, the CBMC is an option. Customers with appeal rights who request mediation can be referred to the CBMC.

- **Alternative mediation service providers**

In States without a USDA-funded mediation program or access to a CBMC, Agency officials will provide a list of alternative mediation service providers. If there is a significant variation in cost between service providers, this option will not be used.

## **C. Appeal**

Participants who wish to appeal an adverse decision must submit a written request to NAD within 30 days of receiving notice of an adverse decision. If unable to determine when the letter was received, count 7 calendar days after the date on the adverse decision letter [date on letter + 7 days = date of receipt of letter + 30 days = 37 days when request must be made]. The request must be signed by the participant and include: (1) a copy of the adverse decision to be appealed; and (2) a brief statement describing why the participant believes the decision is wrong.

*Upon receiving a notice from NAD that an appeal has been filed, the Appeal Coordinator will promptly provide NAD with a copy of the Agency record, specific references in 7 CFR Part 3550 to support the adverse decision, and any other pertinent information. A copy will also be provided to the program participant.*

NAD will notify the participant and the Agency once it has made a final determination. If NAD reverses the Agency's decision, the next loan processing action must take place within 30 days after the effective date of the notice; unless the Agency requests a review of the case by the Director of NAD. For more guidance on the Director review and other information regarding appeals, refer to [7 CFR Part 11](#).

## 1.12 NAD HEARING PREPARATION

Providing an Agency record means all the materials maintained by an Agency related to an adverse decision, including all materials prepared or reviewed by the Agency during its consideration and decision-making process related to the adverse decision. The Administrative Judge shall set a reasonable deadline for submission of the following documents:

(A.) By the appellant;

1. A short statement of why the decision is wrong;
2. A copy of any document not in the Agency record that the appellant anticipates introducing at the hearing; and
- ( 3) A list of anticipated witnesses and brief descriptions of the evidence such witnesses will offer.

(B.) By the Agency:

1. A copy of the adverse decision challenged by the appellant;
2. A written explanation of the Agency's position, including the regulatory or statutory basis therefor;
3. A copy of any document not in the Agency record that the Agency anticipates introducing at the hearing; and
4. A list of anticipated witnesses and brief descriptions of the evidence such witnesses will offer.

Not less than 14 days prior to the hearing, the National Appeals Division must provide the appellant, the authorized representative, and the Agency a notice of hearing specifying the date, time, and place of the hearing. The hearing will be held in the State of

residence of the appellant, as determined by the Administrative Judge, or at a location that is otherwise convenient to the appellant, the Agency, and NAD. The notice also shall notify all parties of the right to obtain an official record of the hearing.

#### A. Pre-Hearing Conference

Whenever appropriate, the Administrative Judge shall hold a pre-hearing conference in order to attempt to resolve the dispute or to narrow the issues involved. A pre-hearing conference shall be held by telephone unless the Administrative Judge and all parties agree to hold such conference in person.

#### B. Post-Hearing Procedure

The Administrative Judge may leave the hearing record open after the hearing, to allow the submission of information by the appellant or the Agency. The Agency representative is responsible to respond to new facts, information, arguments, or evidence presented or raised at the hearing. Any new information will be added to the hearing record and sent to the other party or parties by the submitter of the information.

#### C. Timing of Issuance of Determination

The Administrative Judge will issue a notice of the determination on the appeal to the named appellant, the authorized representative, and the Agency not later than 30 days after a hearing or the closing date of the hearing record in cases in which the Administrative Judge receives additional evidence from the Agency or appellant after a hearing. In the case of a record review, the Administrative Judge will issue a notice of determination within 45 days of receipt of the appellant's request for a record review.

#### D. Requests for a Director Review

The Appeal Coordinator is responsible for filing a request for a Directors review on reversed Agency decisions that have merit and are not favorable to the Agency. The SFH Administrator or a person acting in such capacity can submit a written request for a Directors review within 15 business days after receipt of Administrative Judge's decision. The request should include specific reasons why the Agency believes the determination is wrong, including citations of statutes or regulations that the Agency believes the determination violates. In consideration of the limited timeframe, the Appeal Coordinator should send a request immediately to the Servicing Office.

Director, which will be forward to the Single Family Housing Direct Loan Division in the National Office for review.

1. The program participant can submit a written request for a Director review within 30 days after receipt of the Administrative Judge's decision. The Director will review the Administrative Judge's decision to determine if it was correct. The request should include specific reasons why the appellant believes the determination is wrong.

2. A copy of a request for a Director review will be provided simultaneously by the submitter to each party to the appeal. The Director will determine whether the decision of the Administrative Judge is supported by substantial evidence. Based on such review, the Director will issue a final determination notice that upholds, reverses, or modifies the determination of the Administrative Judge. The Agency shall implement the final determination no later than 30 days after the effective date of the notice of the final determination.

3. Reconsideration of a determination of the Director may be requested by the appellant or the Agency within 10 days of receipt of the determination.

### **1.13 CONFLICT OF INTEREST [7 CFR 3550.9]**

All employees must strive to maintain the highest levels of honesty, integrity, and impartiality in conducting their activities on behalf of the Agency. The Agency's requirements for handling assistance to employees, relatives, and associates are described in RD Instruction 1900-D. State Office, Servicing Office, and National Office employee relationships are reviewed by the State Director who will obtain the Administrator's written concurrence for application processing. To reduce the potential for conflicts of interest, all processing, approval, servicing, or review activity must be conducted by Agency employees who:



- Are not the recipient (applicant or borrower), a recipient's family member, or a close known relative and/or associate of the recipient;
- Do not have an immediate working relationship with the recipient, the Agency employee related to the recipient, or the Agency employee who would normally conduct the activity; and

## Paragraph 1.13 Conflict of Interest [7 CFR 3550.9]

- Do not have a business or close personal association with the recipient.

**A. Borrower Disclosure**

Borrowers must disclose any known relationship or association with Agency employees when they apply for assistance through the Agency.

**B. Agency Employee Disclosure**

Agency employees must disclose any known relationship or association with a borrower, regardless of whether the relationship is known to others.

**C. Disposition of REO Properties**

Agency employees and members of their families are precluded from purchasing REO property, assumptions from Agency borrowers, or security property sold at a foreclosure sale. Closing agents and members of their families are precluded from purchasing properties in which they have been professionally involved.

**1.14 OTHER FEDERAL REQUIREMENTS****Environmental Requirements [7 CFR 3550.5]**

The Agency considers environmental quality equally with economic, social and other factors in its program development and decision-making processes. Both the Loan Originator and the Loan Approval Official are responsible for effectively integrating Agency environmental policies and procedures with loan and grant origination and servicing activities. Agency environmental policies and procedures and historic preservation requirements can be found in RD Instruction 1970. Agency-assisted properties also must meet the lead-based paint requirements contained in Exhibit H of RD Instruction 1924-A. Resolution of conflicts or significant differences between Agency environmental regulations and State or local environmental laws requires prior consultation with the appropriate State Environmental Coordinator and, if necessary, National Office environmental staff.





### **Construction Standards**

Sites and dwellings developed or rehabilitated with Section 502 funds must meet the construction standards outlined in RD Instructions 1924-A and 1924-C. Existing dwellings must be decent, safe, and sanitary and meet all applicable State and local codes.



### **Administrative Requirements**

Agency employees must comply with Agency and Departmental administrative requirements.

#### **1. Procurement**

Goods and services procured to support Agency activities such as appraisals, inspections, broker services, and property management services must conform with the policies and procedures of RD Instruction 2024-A.

#### **2. File Management**

Files and other Agency records must be maintained in accordance with RD Instruction 2033-A.

#### **3. Handling Funds**

Funds received in the Field Office that are not part of a borrower's regular installment, for example, credit report fees or appraisal fees are forwarded to the Servicing Office using *Form RD 3550-17, Funds Transmittal Report*. If a borrower did not receive a billing statement, Field Staff can submit the payment using *Form RD 3550-27, Substitute Payment Coupon*.

### **1.15 EXCEPTION AUTHORITY [7 CFR 3550.8]**



Exceptions to any requirement of this handbook or 7 CFR Part 3550 can be approved in individual cases by the Administrator or designee if application of the requirement or failure to take action would adversely affect the Government's interest. Any exception must be consistent with the authorizing statute and other applicable laws.

Requests for exceptions are submitted to the Administrator or designee through the Deputy Administrator, Single Family Housing and may be initiated by the State Director; the Deputy Administrator, Single Family Housing; the Deputy Administrator, Servicing Office; or the Director, Single Family Housing Direct Loan Division.

Paragraph 1.12 Exception Authority [7 CFR 3550.8]

The exception request must provide clear and convincing evidence of the need for the exception. At a minimum the request must include:

- A full explanation of the circumstances, including an explanation of the adverse effect on the Government's interest;
- A discussion of proposed alternatives considered; and
- A discussion of how the adverse effect will be eliminated or minimized if the exception is granted.

Requests for exceptions regarding architectural and engineering, environmental, or civil rights issues must also include the review and comments of the applicable State Office Technical Staff. The Deputy Administrator, Single Family Housing will coordinate these exception requests with the applicable National Office technical staff prior to submission to the Administrator.

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**ATTACHMENT 1-A  
INFORMAL ADMINISTRATIVE REVIEW**

(DATE)

We appreciated the opportunity to review the facts relative to your [request for assistance, or reduction or termination of benefits, or foreclosure]. We regret the outcome did not grant the assistance you requested [or will terminate or reduce the assistance you are currently receiving, or will give you relief from foreclosure].

If you believe that facts used in this case are in error, you may pursue the alternative options listed in the attached adverse decision letter within 30 days of receipt of this letter.

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U. S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Attachment (adverse decision letter)

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases

**ATTACHMENT 1-B  
AN APPEALABLE ADVERSE DECISION**

(DATE)

The described action in the attached letter [did not grant you the assistance you requested or will terminate or reduce the assistance you are currently receiving]. If you believe this decision or the facts used in this case are in error, you may pursue any or all of the following three options below. All three options may be requested simultaneously and must be requested in writing within **30 days** from the date adverse decision letter is received. If all options are requested and a resolution is reached the next available option can be canceled; however; if an option is skipped you will automatically waive the right to the previous option.

***Option 1 - Request an Informal Administrative Review***

You may request an Agency official review of this determination by filing a written request no later than 30 days after you receive this notice. If you request a review reconsideration, you have the right to an informal hearing which you or your representative may attend either personally or by telephone. If you choose to seek reconsideration, you may later appeal the determination to the National Appeals Division. To request reconsideration, write to the following address and explain why you believe this determination is erroneous. The address of the Field Office:  
(Insert applicable address.)

***Option 2 - Request Mediation (Alternative Dispute Resolution)***

Mediation is available as part of Rural Development's informal appeal process. Mediation may enable us to narrow the issues and resolve the matter by mutual agreement. If your state does not have a participating USDA-funded mediation program, you may have to pay all or part of the cost of mediation. If you request mediation, the continuation of the time frame in which you may request an appeal stops. When mediation closes, the clock restarts and you will have the balance of the days remaining in that period to request an appeal. To request mediation, you must submit your written request no later than 30 days after you receive this notice. To request mediation, write to the RD State Director at the following address:

- (Insert applicable address.)[Rural Development State Director]

### **Option 3 - Request an Appeal Hearing to the National Appeals Division (NAD)**

You may appeal this determination to NAD by filing a written request no later than 30 days after you receive this notice in accordance with the NAD Appeal procedures found at [7 CFR Part 11](#). If you appeal to NAD, you have the right to a hearing which you or your representative may attend. Once a hearing with NAD begins, you waive any rights you might have to reconsideration and mediation. To appeal, you must write to NAD at the following address, explain why you believe this determination is erroneous, and provide a copy to RD. You must personally sign your written appeal to NAD and include a copy of this letter or file an appeal online at the following website <https://www.usda.gov/oha/nad/appeals>

:

[NAD Assistant Director Address] [Rural Development State Director]

If you do not timely exercise one of the preceding options, this shall be the final administrative determination with respect to this matter in accordance with the regulations at [7 CFR Part 11](#).

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U. S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Attachment (adverse decision letter)

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases

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**ATTACHMENT 1-C**  
**AN ADVERSE DECISION THAT CANNOT BE APPEALED**

The decision described in the attached letter did not grant you the assistance you requested or will terminate or reduce the assistance you are currently receiving. If you believe that this decision is erroneous, you have the following options.

***Option 1 - Request an Informal Administrative Review***

You may request an Agency official review this determination by filing a written request no later than 30 days after you receive this notice. If you request reconsideration, you have the right to an informal hearing which you or your representative may attend either personally or by telephone. If you choose to seek reconsideration, you may later appeal the determination to the National Appeals Division. To request reconsideration, write to me at the following address and explain why you believe this determination is erroneous. The address of the Field Office:

*(Insert applicable address.)*

**Option 2 - Request a Review by the National Appeals Division (NAD)**

Applicants and borrowers generally have the right to appeal adverse decisions, but decisions based on certain reasons cannot be appealed. We have determined that reasons for this decision cannot be appealed under our regulations. You may request ~~an appeal for the~~ a review of the accuracy of our findings, that the decision cannot be appealed, to NAD by filing a written request no later than 30 days after you receive this notice in accordance with the NAD Appeal procedures found at [7 CFR Part 11](#).

[NAD Assistant Director Address] [Rural Development State Director]

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade.

Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U.

S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Attachment (adverse decision letter).

Copies for: State and/or National Office Program Director Servicing Office for SFH servicing cases

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**ATTACHMENT 1-D**  
**NOTIFICATION TO APPLICANTS OR BORROWERS OF THE**  
**ASSIGNMENT OF THEIR CASE TO A MEDIATION SERVICE**  
**PROVIDER**

DATE:

TO: [Program Participant]

FROM: Rural Development State Director

SUBJECT: Request for Mediation Services

This replies to your request for the mediation of your adverse decision. Your request has been referred to a [USDA-funded State mediation program] [Community-Based Mediation Center] or [you must select from the attached list of certified mediation providers].

As indicated in our adverse decision letter, there may be a cost for the mediation. The following is an estimate, but you will be advised by the mediation service provider if there will be a cost. Rural Development policy is to pay 50 percent of the reasonable cost for mediation.

\$ USDA-funded State mediation program [and address]

\$ Community-Based Mediation Center or Other Mediation Service Provider [and address]

Attached is an alphabetical list of certified mediators to select a mediator, or subject to our concurrence you may request the use of another mediator.

**Within 10 days of the date of this letter, you must** provide this office, in writing, with the concurrence/selection of the mediator. If you do not, you will waive your right to mediation. Rural Development will then contact the mediator, who in turn will contact you to determine if they can mediate the issues in your case. You will then have 45 days to complete the mediation.

When the mediation is concluded, you may file an appeal of the original adverse decision by immediately contacting the National Appeals Division (NAD):

[NAD Assistant Director Address]

Once you have been contacted by the mediation provider and if you decide not to pursue mediation, you must immediately contact this office (address at the top of this letter). You are responsible for all costs incurred by the mediation provider from the time of selection until your cancellation.

Mediation, or the cancellation of mediation, does not affect your rights to seek an appeal with NAD.

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U. S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases  
State ADR Coordinator

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**ATTACHMENT 1-E**  
**REQUEST TO A MEDIATION SERVICE PROVIDER**

DATE:

TO: [Mediation Service Provider] FROM: Rural Development State Director

SUBJECT: Request for Mediation

CUSTOMER: [Name of the Rural Development customer requesting mediation] [Customer contact information]

The above Rural Development customer has received an adverse decision from our Agency and has requested mediation. Attached is a copy of the adverse decision letter and the customer's request for mediation.

**Informal Administrative Review**

\_\_\_\_\_ The Customer was provided with the opportunity for an informal administrative review with the Agency; however, the customer chose not to exercise this option.

\_\_\_\_\_ An informal administrative review was conducted; however, the Agency did not reverse its decision.

**Jurisdiction of the Case**

The adverse decision in this case was made by the following office. You should contact this office for further information on the case:

[Agency contact: program, individual, address phone and email]

**Payment for Service**

The Rural Development policy is to pay 50 percent of the reasonable cost of the mediation service and the customer will pay 50 percent. In addition, we encourage the mediation service to consider the customer's ability to pay. The customer is solely responsible for their portion of the cost of this service and should be billed directly. The bill for the Agency's portion should be submitted to this Rural Development State Office:

[State ADR Coordinator Name and Address]**Jurisdiction of case:**

**Mediation must be completed within 45 days** from the date of this letter, unless both parties agree to an extension. We also request a teleconference prior to your acceptance of this case to determine whether the adverse decision lends itself to mediation by your service.

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U.

S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Attachments (2): Adverse decision letter

Customer's request for mediation

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases  
State ADR Coordinator

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**ATTACHMENT 1-F**  
**ATTACHMENT FOR NOTIFYING CUSTOMERS OF EXPIRATION OF**  
**THE 10 DAYS TO SELECT A MEDIATION SERVICE PROVIDER**

DATE:

TO: [CUSTOMER]

FROM: [State Director]

SUBJECT: Expiration of Selection of Mediation Service Provider

On [date], you requested mediation of the adverse decision as outlined in the attached letter which did not [grant the assistance you requested or will terminate or reduce the assistance you are currently receiving, or will give you relief from foreclosure]. You were also informed that you had 10 days from [date] to either concur in the mediation service assigned by Rural Development to your case, or name another mediation service for our consideration.

The 10 days to acknowledge the selection of the mediation service provider has expired. Your request for mediation therefore has expired, and Rural Development will begin to process the initial adverse decision as outlined in the attached letter.

**Request an Appeal Hearing**

Your request for mediation did not take the place of, or limit your right to request an appeal to the National Appeals Division (NAD). You may request an appeal hearing by NAD as long as there are days remaining from the original 30 days to request an appeal as outlined in the original adverse decision letter. You must immediately contact the NAD Assistant Director for your region (at the following address) to determine if you can file for an appeal hearing.

[NAD Assistant Director Address]

There is no cost for an appeal hearing. Your request must state the reasons why you believe the decision is wrong, be personally signed by you, and include a copy of the attached original decision letter. A copy of your request must also be sent to the Rural Development State Director:

[Rural Development State Director Address]

You, or your representative or counsel, may contact this office at anytime during regular office hours to examine or copy the Agency's record relative to the adverse decision. Photocopies will be provided to you. Your representative or counsel must have your written authorization to represent you and review your file. The NAD Administrative Judge will contact you regarding a time and place for the hearing.

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U. S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.  
Attachments (2)

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases  
State ADR Coordinator

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**ATTACHMENT 1-G**  
**ATTACHMENT FOR CUSTOMER NOTIFICATION OF UNRESOLVED**  
**RESULT OF THE MEDIATION OF THE ADVERSE DECISION**

DATE:

TO: [CUSTOMER]

FROM: [State Director]

SUBJECT: Unresolved Result of the Requested Mediation

Your request for mediation has been completed. We regret that mediation did not result in resolution of the issues. [We are unable to grant the assistance you requested, or will terminate, or will reduce the assistance you requested].

If you believe the decision or facts used in the case are in error, you may continue to pursue your right to an appeal by the National Appeals Division (NAD). There is no cost for an appeal.

Please follow the guidance in the paragraph indicated with an "X."

☐ You requested an appeal hearing to NAD prior to entering into mediation. You must immediately write to the Assistant Director of NAD at the address below to determine the number of days remaining, if any, to schedule the appeal hearing.  
[NAD Regional Assistant Director Address]

☐ You did not request an appeal hearing to NAD prior to entering into mediation. If you wish to schedule an appeal hearing, you must immediately write to the Assistant Director of NAD at the address below to determine the number of days remaining, if any, to schedule the appeal hearing. Your appeal request must be received within the remaining days, as determined by NAD, from the date when you requested mediation.

[NAD Regional Assistant Director Address]

## **Information Regarding Appeals**

If NAD determines that you have appeal rights and you want to exercise those appeal rights, you, or your representative or counsel, may contact this office at anytime during regular office hours to examine or to have copied the Agency's record relating to the original adverse decision. Photocopies will be provided. Your representative or counsel must have your written authorization to represent you and review your file.

The NAD Administrative Judge will contact you regarding a time and place for the hearing. You may also request a teleconference hearing in lieu of the face-to-face hearing. At any time before the scheduled hearing, you may also request that the Administrative Judge make a decision without a hearing.

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The federal agency that administers compliance with this law concerning this creditor is the Federal Trade Commission. If a person believes he or she was denied assistance in violation of this law, they should contact the Federal Trade Commission, Washington, D.C. 20580.

The Fair Housing Act prohibits discrimination in real estate related transactions, or in the terms or conditions of such a transaction, because of race, color, religion, sex, disability, familial status, or national origin. The federal agency that is responsible for enforcing this law is the U. S. Department of Housing and Urban Development. If a person believes that they have been discriminated against in violation of this law, they should contact the U. S. Department of Housing and Urban Development, Washington, D.C. 20410 or call (800) 669-9777.

Copies for: State and/or National Office Program Director  
Servicing Office for SFH servicing cases  
State ADR Coordinator

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## CHAPTER 2: REGULAR SERVICING

### 2.1 INTRODUCTION

Once loan funds are fully disbursed, the loan is transferred to the Servicing and Asset Management Office (Servicing Office) for servicing, as described in Section 1 of this Chapter. While “servicing” can have connotations of special actions taken to deal with borrowers who are behind in their payments, the bulk of the loans serviced by the Servicing Office will be current loans that require normal day-to-day and year-to-year attention. The Servicing Office undertakes a wide variety of regular servicing activities as discussed below.

- **Handling payments and fees.** Each month the Servicing Office must ensure that each borrower knows how much to pay and when the payment is due. The Servicing Office must process the payment and credit it to the proper account. The Servicing Office also must assess fees for late payments and payments that do not clear. Section 2 of this chapter describes policies for conducting these basic payment collections and handling activities, including paper check processing through electronic funds transfer (EFT) as required by Check 21.
- **Approving borrower actions.** During the term of the loan, the borrower may request permission to undertake actions that could affect the value of the security property. Section 3 of this chapter describes these policies and working with the Field Office to act upon the borrower’s request.
- **Reviewing escrow, taxes, and insurance.** All borrowers are required to pay real estate taxes and maintain acceptable hazard insurance and flood insurance, if applicable. For borrowers with Agency escrow accounts, the Servicing Office is responsible for tracking the escrow funds and paying tax and insurance bills on behalf of the borrower. For borrowers who do not have escrow accounts, the Servicing Office must be prepared to act when the Agency learns that the borrower is not carrying out these obligations. Chapter 3 outlines the Agency’s policies for maintaining escrow accounts for taxes and insurance. Although this is a regular servicing activity, it is discussed in a separate chapter because of the technical nature of the information provided.

- **Assessing eligibility for payment subsidy.** Borrowers who are receiving payment assistance or interest credit subsidies must have their incomes reviewed annually to ensure that they are receiving the appropriate amount of payment subsidy. In addition, borrowers who are not receiving payment subsidy may request it if their financial situation changes. Chapter 4 describes the Agency's policies for annual reviews of a household's income and for providing payment subsidies during the course of the loan. Like handling escrow, taxes, and insurance, assessing eligibility for payment subsidy is generally a regular servicing activity, but the technical nature of the discussion requires a separate chapter.
- **Refinancing with private credit.** Because Agency credit is not intended to replace private credit sources, borrowers who have the means to obtain private financing are required to do so. Every 2 years, the Field Office must review a borrower's ability to refinance with private credit. The Servicing Office's role in facilitating the Field Office's review is outlined in Section 4 of this chapter.
- **Calculating recapture amounts.** The Agency's subsidy recapture policy requires borrowers to repay some or all of the subsidy received over the life of the loan. When borrowers pay off the principal and interest balance of their loan, subsidy recapture must be calculated and the borrower informed of the recapture amount. Borrowers can elect to defer recapture as long as they occupy the property as their permanent residence and do not transfer title. Upon ceasing to occupy the property or transfer of title, they will be required to repay the recapture within 60 days. If the recapture is not paid within 60 days, the account will be referred to the Foreclosure Unit to collect subsidy recapture due. Section 5 of this chapter describes the recapture policy and provides an explanation of the formula used to calculate the precise amount of recapture due.
- **Deceased borrower.** During the term of the loan, the Servicing Office may become aware that a borrower is deceased. In these cases, the Servicing Office will contact the persons responsible for the deceased borrower's estate to request a death certificate and legal documents showing appointment of a personal representative, administrator, or an executor. The Servicing Office will inform such persons of available servicing options, such as same rates and terms assumptions described in Section 3 of this Chapter, and service the account accordingly. In cases where there was a joint borrower and only one borrower is deceased, the loan servicing system will be coded to reflect the deceased borrower. No further servicing actions are necessary. When the Servicing Office determines that all borrowers associated with an account are deceased, the Servicing Office will code the account to reflect the deceased borrowers and determine if there is an open active loan or a recapture receivable account. If a recapture receivable account, the account will be referred to the Foreclosure Unit to recover the subsidy recapture due.

## Paragraph 2.1 Introduction

- **Final payment.** Section 6 of this chapter describes policies regarding how payoff amounts are calculated and provided to the borrower. It also covers how the Field Office releases the security instruments and the Servicing Office processes the final payment.
- **Servicing borrowers with both Rural Housing Service (RHS) and Farm Service Agency (FSA) Farm Credit Program (FCP) loans.** Through our predecessor Agency, the Farmers Home Administration, several loans were made to borrowers who had agricultural and housing loans. The majority of these loans is cross-collateralized and described on the same mortgage deed of trust. Reorganization shifted agricultural loans to the Farm Service Agency, another Agency within USDA. Ownership of these loans is now divided between the two Agencies which requires that separate case files and servicing procedures be maintained. Attachment 2-C of this Chapter provides guidance on how to handle servicing for these borrowers.
- **Servicemembers Civil Relief Act of 2003 (SCRA).** Formerly known as the Soldier's and Sailor's Civil Relief Act of 1940 (SSCRA), this federal law gives military members certain rights when mobilized to active duty status. A major benefit of SCRA is the ability to reduce pre-service consumer debt and mortgage interest rates to 6 percent when a service member is called to active duty. The difference between the full note rate and the 6 percent required under this Act is not subject to recapture. If a borrower qualifies for a payment subsidy after reduction to 6 percent, the amount of subsidy during this period of reduced interest rate would be the difference between the payment subsidy and the 6 percent interest, not the full note rate payment. To obtain a reduction to the 6 percent mortgage interest rate, the borrower must submit a written request and a copy of their mobilization orders to:

USDA, Servicing and Asset  
Management Office FC-244 ATTN:  
SCRA  
P.O. Box 66818  
St. Louis, MO 63166-6818

FAX: (314) 457-4545


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## SECTION 1: GETTING STARTED WITH NEW BORROWERS

### 2.2 GETTING A BORROWER INTO THE SERVICING OFFICE SYSTEM

#### A. Types of Loans

All loans are originated at the Field Office. Borrowers receive either permanent or construction loans, depending on when they will be able to occupy the property. As a result, funds are disbursed differently for permanent loans and construction loans.

- **Permanent loan.** Borrowers receive permanent loans if they can occupy the property within 30 days. The funds are requested in a single advance and disbursed in full at closing. If funds for repairs are not fully disbursed at loan closing, the undisbursed loan proceeds are deposited into an escrow account supervised by the closing agent, or into a supervised bank account and disbursed in accordance with RD Instruction 1902-A. 
- **Construction loan.** Borrowers receive construction loans if the funds will be used to build a new dwelling or to undertake repairs that will prevent them from occupying the dwelling for more than 30 days. Funds for construction loans are disbursed in multiple advances that begin to accrue daily simple interest at the borrower's Equivalent Interest Rate (EIR) as of disbursement. Because borrowers cannot afford to repay the Agency loan while paying for other housing, payments are deferred during the construction period. Once the construction is completed, the Loan Originator adjusts the principal amount reflected on the borrower's promissory note to include the interest accrued during the construction period and amortizes the loan. The loan is then converted from a construction loan to a permanent loan.

## **B. Loan Activation**

Loans are passed on to the Servicing Office for servicing once loan funds are fully disbursed. To begin servicing a loan, the Servicing Office must obtain key information gathered or generated during the origination process. Basic applicant information used for closing the loan will be automatically uploaded to LoanServ from the local UniFi systems on a daily basis. This means that applicant information will be available on LoanServ before the loan is closed. The Loan Originator activates the loan in LoanServ on the day of loan closing as either a permanent or a construction loan. The Servicing Office begins servicing permanent loans immediately; construction loans are not serviced until they are converted to permanent loans.

## **C. Loan Docket**

The Loan Originator provides the Servicing Office with a Loan Docket that contains copies of key documents for servicing legal documents and other documents that are not automated, such as the applicant's insurance policy and *Form RD 3550-15, Tax Information* after all funds

have been fully disbursed. The Loan Originator should complete *Form RD 3550-19, Transmittal-Closing Documents*, and attach copies of the required documents. The check received for the escrow account also should be sent with the Loan Docket. For construction loans, the Loan Originator should not wait until the loan funds are fully disbursed to send the check for the escrow account, but should send it immediately after loan closing.

When the Loan Docket arrives, the Servicing Office must first ensure that all required documents are present. Then, the Servicing Office must scan them into LoanServ, verify that the information contained in the system is consistent with the loan documents, and enter any additional information not keyed in during the loan origination process. If there are any inconsistencies or missing documents, the Servicing Office will work with the Field Office to coordinate corrections or to obtain the missing documentation. For example, tax and insurance information used for the initial escrow calculations needed at closing will be entered into LoanServ by the Loan Originator, but the Servicing Office will need to enter detailed information about taxing authorities and the insurance company into LoanServ. If the Loan Originator has mistakenly provided original documents, they should be returned to the Field Office for placement in the borrower's case file.



### **Loan Docket**

Remember, the Field Office only provides copies of the documents in the Loan Docket. The originals are kept at the Field Office.

## **2.3 INTRODUCING THE BORROWER TO THE SERVICING OFFICE**

Throughout the origination process, the borrower's only contact with the Agency is the Field Office. Once the loan funds are fully disbursed, the borrower needs to understand that the Servicing Office will be the primary contact.

The borrower's transition from Field Office to the Servicing Office should begin at the Field Office level. During the applicant orientation, the Loan Originator should explain that the transition to the Servicing Office will take place after the funds are fully disbursed and instruct the borrower to direct all servicing-related communication to the Servicing Office.

Once the permanent loan is closed, the Servicing Office must contact the borrower in writing before the first billing statement to explain the role the Servicing Office will play and the Agency's servicing policies, and provide the 1-800 numbers the borrower may need in the future. The borrower should receive this information before or with the first billing statement.

## **2.4 WORKING WITH BORROWERS OVER THE LONG TERM**

Part of the Agency's mission is to provide supervised credit and counseling to help borrowers succeed as homeowners. The Servicing Office's rigorous system of follow ups and reminders for borrowers who are late with their payments is a key to enhancing the likelihood of success.

The quality of contact with borrowers who have difficulty keeping up with their payments is as important as the frequency of those contacts. The Servicing Office must help borrowers understand the seriousness of making late mortgage payments and identify any special servicing actions that could aid borrowers experiencing particular difficulties.

The counseling effort hinges on the ability of the Servicing Office staff to work as a team. Because the borrower may speak with different representatives during each contact, notes in the borrower's file must be thorough and accurate so the next Servicer can avoid duplication of effort. The goal of thorough documentation is not developing large quantities of notes; rather, it is to ensure that any Servicer who picks up the file will be able to offer immediate high-quality service to the borrower.

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**SECTION 2: PAYMENTS AND FEES [7 CFR 3550.152 AND 3550.153]****2.5 FREQUENCY OF PAYMENTS**

Borrowers must make monthly payments unless the loan documents specify other repayment terms. The borrower's scheduled payment consists of principal, interest, taxes, and insurance (PITI) for borrowers who have an escrow account, and principal and interest (PI) only for borrowers who do not have an escrow account. Payments are not credited to a borrower's account until the scheduled payment is received.

Some loans have annual payment terms that require the borrower to make a single annual payment. Annual-pay borrowers may submit partial payments at any time during the year.

**2.6 PAYMENT METHOD**

In general, borrowers make loan payments monthly, either through preauthorized debits or in response to billing statements. Preauthorized debit is the preferred method, since payments are automatically withdrawn from a borrower's checking or savings account, which increases the likelihood of receiving payments on time. If a borrower has multiple loans secured by a single property, a single billing statement or debit will cover all payments due. Annual-pay borrowers are not eligible for preauthorized debit.

**A. Preauthorized Debit**

Under the preauthorized debit payment method, payments are automatically withdrawn from a borrower's checking or savings account. After a borrower's account has been debited, the borrower receives a statement, indicating the amount of the debit. An annual statement that summarizes the total amount debited from the account also will be provided.

New borrowers can authorize preauthorized debit at loan closing by completing Form RD 3550-28A, Authorization Agreement for Preauthorized Payments. Existing borrowers can convert to a preauthorized debit to establish, change financial institutions, request a modification to an existing agreement or terminate having mortgage payments withdrawn from their checking or savings account with verbal authorization at any time, as long as their account is current but not ahead of schedule by contacting the Servicing Office at 1-800-414-1226 during business hours. Once the transaction has been processed, the borrower will receive written confirmation of the requested action from the Servicing Office. The borrower must continue to remit the monthly mortgage payment until notification is received.

When the Agency asks a bank to transfer funds from a borrower's account under a preauthorized debit, no transfer is made unless the scheduled payment amount is available in the borrower's account. If funds are not available, the borrower will be notified that payment must be mailed to the lockbox, and if payment is not received at the lockbox within 15 days of the due date, a late fee will be assessed.

### **B. Billing Statement**


Billing statements are sent at least 2 weeks before payment is due to borrowers who are not subject to preauthorized debit. The borrower sends the payment, along with the coupon attached to the billing statement, to the lockbox address indicated on the statement. Borrowers who pay on a monthly basis should receive a statement each month. Borrowers who pay annually should receive a billing statement at least 2 weeks before the annual payment is due. If an annual pay borrower makes a partial payment during the course of the year, the borrower should be notified of the remaining amount owed.

### **C. Conversion from Annual to Monthly Payments**

Annual-pay borrowers should be encouraged to convert to monthly payments and may request conversion at any time. Whenever a borrower's payment schedule is converted from an annual to monthly basis, the borrower must agree to accrue interest on an amortized schedule, and establish an escrow account.

Annual-pay borrowers **must** convert to a monthly payment schedule, if the borrower has monthly income or the ability to make monthly payments and:

- Obtains a subsequent loan;
- Requires any servicing action that results in reamortization of the loan or obtains new payment subsidy; or
- Must establish an escrow account.



#### **Subsequent Loans**

Whenever an annual borrower obtains a subsequent loan to be repaid monthly, the Field Office must inform the Servicing Office so that the payment schedule on the existing loan can be converted from an annual to a monthly basis. Good communication between the Field Office and the Servicing Office is vital to the process.

## Paragraph 2.6 Payment Method

Borrowers who are converted will be notified by the Servicing Office to contact the local field office for an appointment to sign *Form RD 3550-18, Reamortization Agreement*. The Servicing Office will process the reamortization and forward the original and a copy of the agreement to the field office with a letter outlining handling instructions. The field office will provide a copy to the borrower and place the original in the borrower's case file.



If the borrower is currently receiving subsidy, the Servicing Office will continue with the existing agreement unless it appears the borrower's circumstances have changed sufficiently to process a new agreement.

## 2. 7 ACCEPTABLE FORMS OF PAYMENT

Acceptable forms of payment include checks, money orders, or bank drafts. Foreign currency is not an acceptable form of payment. Cash payments are discouraged but must be accepted. Any cash payment should be accompanied by a fee to cover the conversion to a money order. If the borrower does not provide extra money for the conversion to a money order, the conversion fee is deducted from the payment.

## 2. 8 LOCKBOX SERVICES

Borrower payments are received by a lockbox service which processes them on behalf of the Agency. When the payment is received it is date-stamped. The lockbox service data captures the payment information and the loan account number, endorses payment, prepares it for deposit, records the payment amount, and downloads the information to an electronic file for the Servicing Office. If any excess, partial, or "miscellaneous" payments are received, the lockbox reports these to the Servicing Office, which is responsible for determining how the payment should be handled.

### A. Crediting Accounts at The Servicing Office

Once the Servicing Office receives payment information from the lockbox, the data is uploaded to LoanServ. The upload updates the accounts for which payments were received. If the amount received was less than the scheduled payment and the remainder is not received by the 15th day after the due date, LoanServ automatically assesses a late fee, which appears on the borrower's next statement.

## **B. Payments Received at The Servicing Office**

While most borrower payments are sent directly to the lockbox, funds occasionally arrive at the Servicing Office. In the rare case that the Servicing Office does receive a borrower's payment, the payment will be processed by the Servicing Office and forwarded to the lockbox for final processing. If the payment arrives at the Servicing Office more than 15 days after the due date, the borrower is responsible for the late fee.

Employees are personally accountable for losses that occur while funds are in their custody. Exceptions can be made only when a loss occurs without fault or negligence on the part of the employee. To avoid problems, all cash, checks, and money orders received at the Servicing Office will be recorded and secured immediately.

## **2.9 IRREGULAR PAYMENTS**

From time to time, borrowers submit payments that do not meet the definition of a scheduled payment, such as partial or excess payments, or payments on a closed account. The lockbox processes irregular payments and reports them to the Servicing Office. The payments should be applied as described below.

### **A. Partial Payments**

If a borrower makes a payment that is less than the scheduled payment, the payment is held in suspense in the borrower's account. Suspense means that the payment is deposited (for example, check cashed), but not "credited" to the borrower's account until an amount equal to the scheduled payment is received. When subsequent payments are received in an amount sufficient to equal a scheduled payment, the payment is applied.

#### ***1. Loans on an Annual Payment Schedule***

Any partial payment made on an annual-pay loan is held in suspense until the full payment is received. A letter is sent to the borrower, indicating the amount of the payment received and the remaining balance.

#### ***2. Multiple Loans***

When a borrower with multiple loans for the same property makes less than the combined scheduled payment for all loans, the payment is applied when the scheduled payment for the oldest loan is received. Additional payments are applied to the borrower's other loans in order of declining age.

## Paragraph 2.9 Irregular Payments

**B. Excess Payments**

When a payment in excess of the scheduled payment is received, it is applied first to any outstanding fees or charges. Any additional funds should be used to reduce the principal balance. A borrower's year-end statement must indicate how any excess payments were applied.

If a borrower wishes to prepay a scheduled installment, the payment must be for exactly the scheduled amount and must be accompanied by an indication from the borrower that it is intended as a payment rather than as a reduction of principal.

If the borrower makes excess payments that total 10 percent of the loan balance, or excess loan funds from a construction loan total 2 percent of the loan balance, the borrower's account may be reamortized to reduce the borrower's monthly payment.

**C. Payments on Closed Accounts**

Occasionally, payments are made on accounts that are closed. When a payment is received for an account that has been charged off or canceled as described in Section 3 of Chapter 7, the Agency accepts the payment and credits the appropriate account accordingly.

**2.10 FEES [7 CFR 3550.153]**

The Agency will assess late fees and insufficient funds fees when appropriate. The fees will appear on the borrower's next statement.

- Late fees equal to 4 percent of the principal and interest due are assessed for any scheduled payment not received at the lockbox by the 15th day after the due date unless State law imposes other requirements.
- A \$15 fee is assessed for checks returned for insufficient funds. This fee is in addition to any late fee.



In very limited circumstances, fees may be waived. A waiver may be appropriate as a tool to encourage a borrower to agree to a delinquency workout agreement. A waiver also may be appropriate if a late payment fee is assessed due to circumstances beyond the borrower's control. The Servicing Office should follow consistent standards in determining when a waiver is appropriate. The reason for a waiver should be documented carefully.



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## **SECTION 3: BORROWER ACTIONS REQUIRING APPROVAL**

### ***[7 CFR 3550.159]***

#### **2. 11 OVERVIEW**

A borrower must obtain approval from the Agency before taking actions that may affect the security value of the property. Since these actions involve security property, they are handled in Field Offices. Key actions that require approval from the Agency include subordination, lease of mineral rights, partial release of security, lease of security property, and assumption of indebtedness.

When the Servicing Office becomes aware of borrower actions requiring approval, they will refer the customer to the local Field Office and cue the Field Office regarding the borrower's request. The Servicing Office will provide any information needed by the Field Office to process the request. Field Offices will approve or disapprove the actions outlined in this section and will cue the Servicing Office with the outcome.

This section first covers general guidelines and procedures for evaluating a borrower's request for approval of an action, with the exception of assumptions of indebtedness. Specific guidelines for each of the actions, including assumptions, follow the discussion of general guidelines.

#### **2. 12 GENERAL GUIDELINES**

##### **A. Reviewing Requests**

To request approval for subordination, mineral leases, partial release of security, and lease of security property, a borrower must submit *Form RD 465-1, Application for Partial Release, Subordination, or Consent*, to the local Field Office. If the information provided is not sufficient to allow for a thorough evaluation, the Field Office will request additional information from the borrower. The Servicing Office may be cued by the Field Office, as necessary, to supplement the borrower's information.

##### **B. Obtaining an Appraisal and an Environmental Review**

An appraisal is required for the Agency to subordinate its interests or to approve a partial release of security if the amount of consideration exceeds \$5,000. The borrower must pay for the appraisal, although the cost for an appraisal can be charged to the borrower's account.

An existing appraisal may be used if it is less than 1 year old and appears to reflect market value. An Agency appraisal is not required if a lender is involved and can provide an appraisal that adequately reflects market value.

Actions requiring Agency approval of mineral leases are subject to the environmental requirements of RD Instruction 1970 series prior to approval.

### **C. Evaluating and Approving the Request**

Once the information needed to evaluate the request has been submitted, the Field Office must analyze the effect of the proposed action on the security property and document the conclusions on *Form RD 465-1*. Some factors to consider in the analysis include:

- The market value of the property before and after the transaction;
- The physical effects of the action on the security property; and
- The assignment of initial and subsequent payment proceeds.

If the analysis indicates that the Agency's security will not be put at risk by the action, an approval official in the Field Office may sign *Form RD 465-1*. The Office of General Counsel (OGC) may need to provide relevant forms needed to complete the approval. Signed copies of *Form RD 465-1* should be distributed to the Servicing Office, the borrower and lender, as appropriate. The original should be maintained in the borrower's case file at the Field Office.

### **D. Using Proceeds**

Proceeds that arise from the sale of a portion of the security, granting an easement or right-of-way, damage compensation, and all similar transactions should be used in the following order.

- To pay customary and reasonable costs related to the transaction that must be paid by the borrower, such as:
  - ◊ Real estate taxes that must be paid to conclude the transaction;
  - ◊ Cost of title examination, survey, abstract, and reasonable attorney's fees; and
  - ◊ Costs necessary to determine a reasonable price, such as appraisal of minerals, when the necessary appraisal cannot be obtained without costs.



## Paragraph 2.12 General Guidelines

- To be applied on a prior lien debt, if any.
- To be applied to the Agency indebtedness or used for improvements to the security property in keeping with the purposes and limitations applicable for the use of Agency loan funds. Proposed development will be planned and performed in accordance with RD Instruction 1924-A and supervised to ensure that the proceeds are used as planned.



The use of proceeds should be reflected on *Form RD 465-1* and agreed to by the borrower and the Agency. Proceeds from the transaction to be applied to the Agency indebtedness will be remitted to the Cash Management Branch in the Servicing Office by Field Offices using *Form RD 3550-17, Funds Transmittal Report*, with Reason Code “00,” together with a brief statement as to the source of proceeds, a copy of *Form RD 465-1*, and any related documentation. The Field Office will also notify the Servicing Office using Task 178, “Legal Description Correction.”

## 2.13 SUBORDINATION [7 CFR 3550.159(b)]

The Agency will consider subordination of its lien position to allow a borrower to gain access to private sources of credit. Subordinations are generally handled by the Servicing Office. The most common type of subordination request will be when a borrower refinances their Agency loan with private credit, and the borrower elects to defer payment of recapture. Field Offices are responsible for handling subordination requests in cases where the borrower is obtaining a subsequent loan for repairs or improvements to the property (not associated with refinancing). In cases where a borrower is refinancing, and has included in the refinancing package additional funds for repairs or improvements, the Servicing Office will coordinate such requests with the Field Office.

### A. Criteria for Subordination

Requests for subordination can be approved if:

- The other lender verifies that the funds will be used for Agency-eligible purposes;
- Based on repayment ratios, the prior lien debt will be on terms and conditions that the borrower can reasonably be expected to meet without jeopardizing repayment of the Agency indebtedness;



#### Nonprogram Borrowers

Subordination cannot be authorized for nonprogram loans.

- Any proposed development will be planned and performed in accordance with Agency construction standards, as described in RD Instruction 1924-A or directed by the other lender in a manner that is consistent with that subpart; and
- The prior lien holder agrees in writing to provide at least 30 days prior written notice to the Agency before initiating any foreclosure action on the prior lien.



To document that the subordination conforms to the Agency's requirements, the borrower should ask the other lender to provide the Agency with a memorandum that states the purpose of the loan, along with its terms and conditions.

### **B. Amount of Subordination**

The total amount of debt permitted when the Agency subordinates its interest depends on whether the borrower pays off the Agency loan.

- **Repay Agency loan but defer recapture.** If the borrower will repay the loan and is requesting that the Agency subordinate only a deferred recapture amount, the prior lien debt plus the deferred recapture amount must not exceed the market value of the security. These cases are handled by the Servicing Office.
- **Retain Agency loan.** If the borrower is obtaining a subsequent loan from another source and will not pay off the Agency debt, the prior lien debt plus the unpaid balance on all Agency loans, exclusive of recapture, must not exceed the market value of the security. These cases are handled by the Field Office.

## **2.14 MINERAL LEASES [7 CFR 3550.159(a)]**

Borrowers must obtain Agency authorization before leasing mineral rights on their security property. Such requests are rare, but do occur in situations such as a property in a town located above a coal mine or a property located on a water source. OGC should be involved in mineral lease decisions because State and local laws vary. In addition, an environmental review is required in accordance with RD Instruction 1970 series, prior to approval. Subordination of an Agency loan to a mineral lease does not entitle the leaseholder to any proceeds from the sale of the security property. If the lease of mineral rights is approved, rental proceeds not assigned to the Agency are treated as income and any payment subsidy must be adjusted accordingly.



## Paragraph 2.14 Mineral Leases [7 CFR 3550.159(a)]

The Field Office will consent to the lease of mineral rights and the subordination of its liens to the lessee's rights and interests in the mineral activity if the security property will remain suitable as a residence, and the Government's security interest will not be adversely affected.

To make this determination, the Field Office must consider the effects of leasing on the security property, including the potential for the lessee's rights of surface entry on the property. They also must ensure that the property remains decent, safe, and sanitary and the value of the security property is not decreased below the amount of the loan.

- **No decrease in value.** If the proposal is not likely to decrease the value of the security property, the lease may be approved if the borrower agrees: (1) to use any damage compensation received from the lessee to repair damage to the site or dwelling; or (2) to assign it to the Agency to be applied to reduce principal.
- **Likely decrease in value.** If the proposed activity is likely to decrease the value of the security property, the Field Office may consent to the lease of mineral rights only if: (1) the borrower assigns 100 percent of the lease income to the Agency to be applied to reduce principal; and (2) the rent to be paid is at least equal to the estimated decrease in market value.

When an assignment of income is required, the borrower must submit an assignment of income in a format that is designed to comply with State law and approved by OGC.



## 2.15 PARTIAL RELEASE OF SECURITY [7 CFR 3550.159(c)]

A borrower may request a partial release of security to accommodate a need to sell or exchange part of the property or grant a right-of-way across the security property. For example, the owner of an adjoining property may want to trade 10 feet of the side yard for 10 feet of the back yard, or the local government may wish to purchase land that borders a highway slated for widening.

The Agency may consent to transactions affecting the security and grant a partial release of security if the following conditions are met.

- The borrower will receive adequate compensation:
  - ◊ The sale of any part of the security property must result in a payment equal to the value of the security being released or rights granted;
  - ◊ The exchange of security property must result in another parcel of property acquired that has value equal to or greater than that being released; or
  - ◊ The granting of an easement or right-of-way must result in benefits that are equal to or greater than the value of the security property being released.
- The security property, after the transaction is completed, must be adequate, decent, safe, and sanitary. For a program loan, the security after the transaction is completed must also remain modest.
- Repayment of the Agency debt must not be jeopardized.



In accordance with RD Instruction 1970-A, 1970.8 (e), “servicing actions are directly related to financial assistance already provided, do not require separate NEPA review, and are not actions for the purposes of this part”.

- .

To process a partial release, the Field Office must complete the following actions.



- Complete any required State release forms. The unrecorded documents will be uploaded to the imaging repository as “Loan Documents Class – Deeds of Trust Mortgages” as part of the borrower’s permanent record. The party requesting a partial release is responsible for recording costs.
- For an **exchange** of all or a portion of the security property, obtain title clearance for the new security before the release of the existing security. Security instruments must be obtained for the new property.
- For a **sale** of all or a portion of the security property, deliver the release when full payment is received.
- Update the legal descriptions of the property, as necessary.

## Paragraph 2.15 Partial Release of Security [7 CFR 3550.159(c)]

The Field Office may approve, after notifying the Servicing Office of the approval, the following releases:

- **Additional security.** At any time prior to payment of the loan in full, the Agency may authorize a release from the Agency's lien any real estate taken as additional security. This is authorized provided the market value of the remaining security is adequate to secure the loan balance. Additional security does not include any part of the tract purchased with Section 502 loan funds or part of the minimum adequate site on which the dwelling is located.
- **Mutual Mistake.** The Agency may authorize the release of property from the Agency's lien caused through mutual mistake when substantiated by facts and when the Agency can determine, with the advice of OGC, that a mutual error existed at the time the property was included in the security instrument.
- **No evidence of indebtedness.** The Agency's lien may be released in situations where there is no evidence of an existing secured indebtedness in the Field Office or in the Servicing Office. Before releasing the lien, the Field Office should consult with the Borrower Assistance Branch in the Servicing Office.
- **Valueless Lien.** In liquidation cases, if a net recovery valuation indicates the Agency's lien is valueless (that is, there is no or a negative potential recovery), the lien may be released. The Field Office will contact the Borrower Assistance Branch in the Servicing Office to ensure that taxes and insurance are no longer paid by the Agency, and a debt settlement package is sent to the borrower by the Servicing Office.

## 2.16 LEASE OF SECURITY PROPERTY [7 CFR 3550.159(d)]

Program borrowers must notify the Agency if they lease the property. If the Agency becomes aware of a borrower who is leasing their property, the borrower is not eligible for payment subsidy or special servicing benefits during the period of the lease. Field Offices will notify the Servicing Office, and provide any applicable documentation, if they become aware that a borrower has leased the security property. The Agency also should assess the borrower's ability to refinance with private credit. If the lease is for a term of more than 3 years or contains an option to purchase, the Agency may liquidate the loan. Nonprogram borrowers are free to lease their properties without restriction.

## 2. 17 ASSUMPTION OF INDEBTEDNESS [7 CFR 3550.163]

### A. New Rates and Terms Assumptions

In most cases, Agency indebtedness is only assumed as part of a sale. In these situations the debt is assumed on new rates and terms as part of loan origination and is handled by the Field Office. Field Offices are authorized to release the former borrower from personal liability for the amount of debt being assumed utilizing *Form RD 3550-16, Release from Personal Liability*. In cases where the debt is not being assumed in full, the Servicing Office will handle the settlement of the remaining debt and any release of liability for the portion of debt not being assumed.

### B. Same Rates and Terms Assumptions

In certain limited cases, generally those involving transfers of title between family members, a standard industry assumption is permitted. It is known in the Section 502 program as a ***same rates and terms assumption***. Same rates and terms assumptions are handled and approved in the Field Office. Under this type of assumption, the loan is not reamortized and the existing note terms, including the interest rate and the remaining repayment period, do not change. If the account is past due at the time an assumption is executed, the Field Office will refer the new owner to the Servicing Office. The account may be brought current by using any of the servicing methods discussed in Chapter 5 for which the new owner is eligible.

The new owner need not have a low or moderate income. However, payment subsidy can be continued for the new owner only if he or she is eligible for assistance and only at the level for which the new household qualifies. If the transferee is a very low- or low-income person, it may be more beneficial for the transferee to assume the loan under new rates and terms. For example, if current interest rates are lower or a longer repayment period is necessary, a new rates and terms assumption may be of benefit to the new owner. In those cases, if the new owner applies and is program-eligible, the loan will be assumed under new rates and terms. In cases where the assuming party has a moderate- or above moderate-income, the party will be informed of the Agency's refinancing requirements, and if applicable, the loan will be reviewed for refinancing.

Same rates and terms assumptions are permitted for the following types of transfers:

- A transfer from the borrower to a spouse or children not resulting from the death of the borrower;

## Paragraph 2.17 Assumption of Indebtedness [7 CFR 3550.163]

- A transfer to a relative, joint tenant, or tenant by the entirety resulting from the death of the borrower;
- A transfer to a spouse or ex-spouse resulting from a divorce decree, legal separation agreement, or property settlement agreement;
- 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;
- A transfer into an inter vivos trust in which the borrower does not transfer rights of occupancy in the property; and
- Any subsequent transfer of title, except upon death of the inheritor or between inheritors to consolidate title, will be treated as a sale.

**C. Agency Approval**

The due-on-sale clause contained in all Agency mortgages stipulates that the borrower must obtain approval from the Agency before the title of a security property can be transferred with an assumption of the indebtedness.

The Agency will approve a transfer of title and assumption of indebtedness if it is in the best interest of the Government. The new owner will be liable for the loan, and the terms and conditions of the assumption depend upon the eligibility of the new purchaser and the property's characteristics.

In most cases, if the borrower sells a security property with a due-on-sale clause without obtaining prior authorization from the Agency, the assumption will not be approved and the loan may be liquidated. If the Agency determines it is in the best interest of the Government to continue the loan, the account will be serviced in the original borrower's name, and the original borrower will remain liable for the loan under the terms of the security instrument.

A new owner who obtains property through a transaction eligible for a same rates and terms assumption is not required to obtain Agency approval or assume the loan. The Agency is not permitted to liquidate the loan if the new owner continues to make scheduled payments and meets all other obligations of the loan. However, a new owner who does not assume the loan is not eligible for payment assistance or a moratorium.

#### **D. Procedural Requirements**

The new owner must sign *Form RD 3550-22, Assumption Agreement Single Family Housing*. For assumptions, the original note is not returned to the seller. Instead, the note is filed with other original notes, with the original *Form RD 3550-22* attached.

#### **E. Releasing a Departing Borrower From Liability**

Changes in household composition may trigger the need to adjust who is responsible for repayment of the loan. The need for a change most often occurs when one party to the note wishes to be released of liability. For example, after a divorce the departing spouse may wish to be relieved of responsibility for the balance of the mortgage. The Agency will authorize such a release only when:

- The divorce decree or property settlement document did not make the departing borrower responsible for loan payments;
- The departing borrower's interest in the security property is conveyed to the person with whom the loan will be continued; and
- The remaining borrower meets the maximum total debt ratio requirements and credit history requirements or, the account has been current for at least six months.

*Form RD 3550-16* is used to release the departing borrower from liability. The Servicing Office generally handles these releases, but may cue the Field Office for assistance.

The following items need to be submitted to apply for a release of liability:

1. A written request from the departing borrower to be released of liability;
2. New address and phone number of the departing borrower;
3. Divorce decree and property settlement (if applicable);
4. Recorded deed conveying ownership to the remaining borrower(s);
5. Financial Statement of remaining borrower;
6. Verification of all income sources (such as pay stubs, award letters, etc. as described in HB1, Chapter 3.15) for remaining borrower; and
7. Copy of latest Federal income tax return, including W2 form, for remaining borrower.



## SECTION 4: REFINANCING WITH PRIVATE CREDIT [7 CFR 3550.160]

### 2.18 OVERVIEW

The Agency's loan programs are not intended to compete with or replace private *credit* sources. To ensure that Section 502 loans are only used to assist borrowers unable to obtain credit from other sources, periodic reviews are conducted to determine borrowers' ability to refinance 100 percent of their Agency loans with private credit. This process was formerly known as "graduation." A borrower who fails to comply with requests for information to determine their ability to refinance, or who fails to refinance upon request by the Agency, is in default of the mortgage agreement and is subject to liquidation.

The Servicing Office staff determines whether a borrower is able to refinance with private credit and when a borrower will be reviewed. The Servicing Office will compile a list of borrowers and generate all appropriate letters to applicable borrowers pertaining to the refinance process. The Servicing Office will answer borrower inquiries and provide all payoffs and recapture information when requested. If a borrower fails to cooperate in this process, the Servicing Office may initiate acceleration of the account.

### 2.19 SELECTING BORROWERS FOR REVIEW

#### A. Criteria

All Section 502 borrowers are considered for refinancing once every 2 years. The Servicing Office reviews the borrower's payment history, and outstanding loan balance to determine whether they can possibly refinance with private credit. If there is a reasonable likelihood that a borrower will be able to refinance based on indicators available on LoanServ, the borrower is selected for further review.

A borrower's ability to refinance may also be reviewed any time the Agency becomes aware that a borrower's circumstances have changed. Such change in circumstances might include: an inheritance, a new job, or any other change that might lead to a substantial increase in household income. The Agency must be consistent when initiating reviews where information is obtained that indicates a possible change in circumstances. The Servicing Office will initiate selection for a refinancing review based on the following criteria:



- Loan is active
- Program borrower

- Not under Servicemembers Civil Relief Act of 2003 (SCRA)
- Credit score equal to minimum used for loan origination
- Not a 504 loan
- Account not in foreclosure
- Account not in bankruptcy
- Account not on a Delinquency Workout Agreement
- No court action pending
- Not subject to approved adjustment action
- Account not on a moratorium
- Not a collection only account
- Principal balance equal to or more than \$15,000
- Borrower is not over one month delinquent
- Account has not been delinquent more than once in the past 12 months
- Refinancing is not currently pending
- No reamortizations in the past two years
- 16 percent difference from original loan vs. unpaid principal and interest
- Full note or subsidized interest rate is two percent over 30-year fixed conventional rate
- Loan is not within 5 years of maturity
- Account is not in a county declared a disaster in the past 12 months

## **B. Subsequent Credit**

If field staff is in the process of reviewing a borrower's request for a subsequent loan when that borrower is selected for a refinancing review, the subsequent loan should be processed before initiating the review. If the review for the subsequent loan shows that the borrower would be able to get private credit for the amount of the subsequent loan, the

borrower's request for a subsequent loan should be denied. The refinancing review should then be initiated to determine the borrower's ability to obtain credit to refinance the existing loan.

### **Subsequent Loan**



Borrowers who have been asked to refinance will not be considered for additional credit until the refinancing issue is resolved, unless additional assistance is necessary to protect the Government's interest in the property.

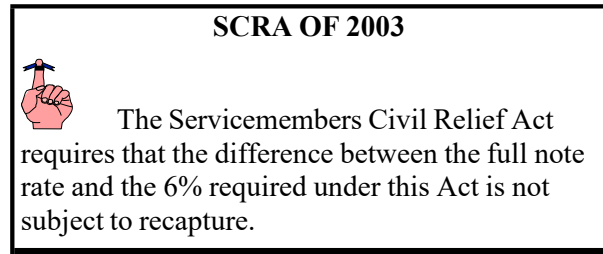
## **C. Subordination of Recapture**

When a borrower refinances a Section 502 loan, recapture will be calculated. The recapture may be paid at the time of refinancing, or if the borrower will continue to occupy the property, the Agency may subordinate its interest in any deferred recapture amount to facilitate a borrower's efforts to refinance with private credit, as long as: (1) the total value of all secured

## Paragraph 2.19 Selecting Borrowers for Review

loans does not exceed the market value of the property; (2) the borrower continues to occupy the property; and (3) title does not transfer. The amount to which the Agency's loan may be subordinated can include:

- The amount required to repay the Agency debt, exclusive of recapture;
- Reasonable closing costs;
- Up to one percent of the loan amount for the lender's loan servicing costs; and
- The cost of any necessary repairs or improvements to the security property.



## 2.20 PROCESSING REQUEST TO REFINANCE

When a borrower is reviewed for refinancing and it appears they can refinance with private credit, the Servicing Office will send *Handbook Letter 111 (3550), Request for Borrower to Refinance With Private Credit* to request that the borrower refinance with private credit within 90 days from the date of the letter. This letter supplies the borrower with telephone numbers necessary for obtaining payoff and subsidy recapture information. It also instructs borrowers who are unable to secure private credit to provide a rejection letter from at least one lender. The rejection letter should contain the following information:

- Lender's name;
- Amount of the loan requested;
- Information the borrower provided to the lender regarding purpose of the loan; and
- Rates and terms offered by the lender, and specific reasons why credit was denied.

If the rejection letter is sufficient to document the borrower's inability to refinance, the Servicing Office will send *Handbook Letter 110 (3550), Notification that the Agency Will Continue With Loan*, advising that the Agency will continue with the loan and the borrower's ability to refinance will be reviewed again in 2 years.

## 2.21 UNCOOPERATIVE BORROWERS AND ACCELERATION

If the borrower fails to respond, the Servicing Office will send *Handbook Letter 112 (3550), Reminder Letter*, 45 days after the initial letter is sent. This letter reminds the borrower of the 90-day deadline and warns them of violation of their security instruments for failure to respond. The Servicing Office may elect to contact these borrowers via a calling campaign to remind them of their obligation.

During the 90-day refinancing review period, the borrower may contact the Servicing Office to provide financial information. The next appropriate action by the Servicing Office depends on an analysis of the financial information provided.

- The borrower may not qualify for refinancing with a private lender based on their credit report. In this case, *Handbook Letter 110 (3550), Notification that the Agency Will Continue With Loans*, will be sent by the Servicing Office indicating that the Agency will continue with the loan and the borrower's ability to refinance will be reviewed again in 2 years.
- If the borrower's income and debt shows the potential to refinance depending on current market conditions but the borrower fails to do so, *Handbook Letter 113 (3550), Follow up Request for Borrower to Refinance With Private Credit*, will be sent to encourage the borrower to take advantage of refinancing opportunities. If the borrower fails to refinance or respond to the Servicing Office within the 90-day review period, *Handbook Letter 114 (3550), Unresponsive*, will be sent to further encourage the borrower to refinance and to advise that the loan remains subject to refinancing.

## **SECTION 5: RECAPTURE [7 CFR 3550.162]**

Many borrowers receive substantial amounts of payment subsidy over the course of their loan repayment period. The Agency's subsidy recapture policy is required by statute and is designed to require borrowers to repay some or the entire subsidy received, yet provide borrowers with the opportunity to realize a benefit from increased equity in their properties. Borrowers who repay a loan are permitted to defer payment of the recapture amount as long as they continue to occupy the property and retain title. Loans approved prior to October 1, 1979, are not subject to recapture unless they were assumed on new rates and terms after that date.

### **2. 22 TRIGGERING RECAPTURE**

Once the principal and interest on a loan is paid in full, subsidy recapture must be repaid whenever the borrower ceases to occupy the property or transfers title. When repayment of recapture is triggered, the Servicing Office will send a notification to inform the borrower of

the amount of recapture due. If the borrower's current address cannot be located, the notification letter should be sent to the last known address. If the borrower does not pay the recapture amount within 60 days of the date of the notification letter, the account should be referred for acceleration and foreclosure, regardless of the amount of recapture owed.

#### **A. Ceasing to Occupy the Property**

Recapture will be collected when the borrower ceases to occupy the property. Ceases to occupy the property is defined as the borrower is no longer using the dwelling as their permanent residence. In cases where the borrower has elected to defer recapture, upon receipt of notice that the borrower may have vacated the property, the Servicing Office will investigate to determine if all borrowers associated with the recapture account have ceased to occupy the property. If it is determined that all borrowers cease to occupy the property, the foreclosure process will begin to recover the recapture due. If the property is temporarily unoccupied for reasons that are acceptable to the Agency recapture is not triggered.

#### **SCRA OF 2003**



The Servicemembers Civil Relief Act requires that the difference between the full note rate and the 6% required under this Act is not subject to recapture.

#### **The Servicing Office may become aware of rented or vacated property by:**

- Borrower notice to the Servicing Office
- Field Office referral
- Completed change of address form
- Returned mail
- Insurance policies
- Tax notices

## **B. Deceased Borrowers**

During the term of the loan, the Servicing Office may become aware that a borrower is deceased. In these cases, the Servicing Office will contact the persons responsible for the deceased borrower's estate to request a death certificate and legal documents showing appointment of a personal representative, administrator, or estate. The Servicing Office will inform such persons of available servicing options, such as a same rates and terms assumption as described in Section 3 of this chapter. The Servicing Office will also open a task to the field office to notify receipt of the deceased borrow information.

In cases where there is a joint borrower and only one borrower is deceased, the Servicing Office will code the account to reflect the deceased borrower. No further servicing actions are necessary.

When the Servicing Office determines that all borrowers associated with an account are deceased, the Servicing Office will code the account to reflect the deceased borrowers and determine if there is an open active loan or a recapture receivable account. If a recapture receivable account, the account will be referred to the Foreclosure Unit to recover the subsidy recapture due.

## **C. Transferring Title**

Recapture is usually triggered when the borrower transfers title. However, the way in which title is transferred can affect the recapture rules.

**Cash sale.** If the purchaser is not obtaining a loan from the Agency, the recapture amount will be paid by the seller.

- **Assumed loan, new rates and terms.** When a loan subject to recapture is assumed under new rates and terms, the recapture amount will either be paid by the seller or assumed by the purchaser. If the recapture amount is assumed, it will be capitalized so that it will accrue interest.
- **Deferred subsidy amount only.** When a borrower repays an Agency loan, exclusive of recapture, the deferred recapture amount may later be assumed by a purchaser who obtains Agency financing. If the purchaser does not obtain Agency financing, the deferred subsidy amount must be paid in full.
- **Assumed loan, same rates and terms.** When a loan subject to recapture is assumed under the same rates and terms, recapture will *not* be calculated or collected. When the new borrower transfers title or ceases to occupy the property, all subsidy subject to recapture before and after the assumption is due.

## Paragraph 2.23 Calculating Recapture Owed

**2.23 CALCULATING RECAPTURE OWED**

The recapture calculation is automated. However, it is important for Servicers to understand the recapture calculation well enough to be able to explain it to borrowers who have questions. Attachment 2-A contains a Final Payoff Worksheet to illustrate how the final payoff amount, including recapture, is calculated for cases other than foreclosure and deed in lieu of foreclosure. Attachment 2-B contains a case study that illustrates the recapture concepts discussed in this section.

**A. Recapture Formulas**

Generally, the amount to be recaptured is determined by a calculation specified in the borrower's subsidy repayment agreement and is based on the borrower's equity in the property at the time of loan pay off. The recapture calculation includes the amount of Principal Reduction Attributed to Subsidy (PRAS) (applicable only to certain loans that received interest credit between October 1, 1979 and December 31, 1989), plus the lesser of:

- The amount of subsidy received, including all payment subsidy and deferred mortgage assistance; or
- The portion of value appreciation in the property subject to recapture.

If there is no equity based on the recapture calculation, the amount of PRAS is not collected.

However, in the case of foreclosure or deed in lieu of foreclosure, the amount to be recaptured is the full amount of subsidy received, not including PRAS. The recapture amount is only recoverable from the security property, not as a personal liability of the borrower.

In the case of foreclosure or deed in lieu of foreclosure sale, the funds received are applied or credited to the borrower's debt in accordance with the security agreement in the following order:

Recoverable costs (e.g. protective advances, foreclosure costs, negative escrow, late charges)  
Accrued interest  
Principal  
Subsidy (excluding PRAS).

**B. Principal Reduction Attributable to Subsidy**

Principal Reduction Attributable to Subsidy (PRAS) accrued on all Section 502 loans that were subject to recapture that were approved, and received interest credit, between October 1, 1979 and December 31, 1989. During this period subsidy (interest credit) was applied by reducing the effective interest rate. Because payments were applied at an interest rate below the Promissory Note interest rate, principal pay down was accelerated. PRAS is the difference between the actual principal balance and what the principal would have been had all payments been applied at the note rate. Because PRAS is directly attributable to subsidy, it is subject to recapture. PRAS continued to increase every month even after subsidy was no longer received. This occurred because the borrower was paying full note rate interest on a smaller principal

balance due to accelerated reduction in principal. Each subsequent payment resulted in a higher amount being applied to principal than if loan had never been subsidized. PRAS stopped accumulating on loans after December 1996. After subsidy was cancelled, PRAS could exceed the subsidy granted as there was always some principal reduction attributed to subsidy. The effect was greater on loans where subsidy was cancelled early in the loan and the loan continued at note rate for several years. At the end of the loan term, the system evens out the payments so that none of the principal reduction is due to subsidy. The system automatically begins to reduce the amount of PRAS after the loan is 15 years old. Loans made since January 1, 1990 do not have PRAS because the Agency changed the method of applying subsidy to loans.

### C. Value Appreciation

As mentioned, recapture, in cases other than foreclosure and deed in lieu of foreclosure, is PRAS plus the lesser of either the subsidy received or a portion of the value appreciation of the property subject to recapture. In order for the value appreciation to be calculated, the borrower will provide a current appraisal, including an appraisal for any capital improvements, or arm's length sales contract as evidence of market value upon Agency request. "Appreciation" is generally construed to mean the difference between the value of the property when it was purchased and its current market value. "Value Appreciation" for the purposes of recapture is calculated with a specific formula that accounts for the borrower's mortgage debt, settlement costs, and equity. Exhibit 2-1 provides the basic value appreciation formula contained in Part 1 of the Final Payoff Worksheet provided in Attachment 2-A. The following paragraphs explain each element of the formula. This formula does not apply to cases of foreclosure and deed in lieu of foreclosure.

Exhibit 2-1	
Calculation of Portion of Value Appreciation	
	<b>Current Market Value</b>
<i>LESS:</i>	Original amount of prior liens and subordinate affordable housing products Balance to be paid off on RHS loans Equity recapture due from Farmer Loan Program (FLP) loan (if applicable) Reasonable settlement costs Principal reduction at note rate Principal Reduction Attributable to Subsidy (PRAS) (if applicable) Original equity Capital improvements (if applicable)
<i>EQUALS:</i>	Value Appreciation (If this is a positive value, continue. If this is a negative value or "\$0", there is no recapture due.)
<i>TIMES:</i>	Percentage of outstanding balance of open loans (if applicable) Recapture Percentage Return on borrower's original equity
<i>EQUALS:</i>	<b>Portion of Value Appreciation</b> subject to recapture



## Paragraph 2.23 Calculating Recapture Owed

**1. *Current Market Value***

Value Appreciation is derived from the current market value of the property, whether it is being sold or not. The amount of recapture to be collected can only be reduced based on the Value Appreciation formula if the Agency has an accurate assessment of market value.

There are different methods of determining the market value. If a borrower requests a final payoff statement before making a final payment, the borrower is responsible for providing a current appraisal or arm's length sales contract. The Agency will use either of those to determine the market value and issue a final payoff statement, which will include the recapture amount.

If the borrower does not contact the Agency before making a final payment (which will likely not include the recapture amount), the Agency must determine the market value from an appraisal conducted by or for the Agency, an appraisal conducted by or for another lender, assessed value, tax records, or other reliable evidence. A broker's price opinion is not acceptable.

**2. *Original Amount of Prior Liens and Subordinate Affordable Housing Products***

Original amount of the prior liens and subordinate affordable housing products (grants, silent mortgages, forgivable loans, Community Land Trusts, etc.) that supplemented the Agency loan at the time of initial property acquisition and were used in determining original equity on the signed *Form RD 3550-12*.

**3. *Balance to be Paid Off on Agency Loans***

All amounts owed to the Agency that are being paid off, including principal and interest, late fees, insufficient funds fees, protective advances, and unauthorized assistance. These amounts are available in the FiServ loan servicing system.

**4. *Equity Recapture Due from Farm Loan Program Loan (if applicable)***

In rare cases, a borrower who previously had an FLP loan that was accelerated may have applied equity in the home to the farm debt. In such situations, the equity applied to the FLP loan must be included in the recapture calculation.

**5. *Reasonable Settlement Costs***

Reasonable and actual settlement costs incurred in selling or refinancing the property that are directly paid by the borrower without reimbursement from another party and are customary and typical for the type of transaction. Anticipated settlement costs for future transactions are not permissible.

## **6. *Principal Reductions***

- (a) Principal reduction at note rate is the amount of RHS loan principal paid by the borrower to date. This does not include principal payments that are attributed to the payment assistance subsidy.
- (b) PRAS is described in section 2.23(B).

## **7. *Original Equity***

Original equity, which is found on Form RD 3550-12, is calculated using the market value at the time of loan approval/obligation for both new and existing properties. Prepaid taxes and insurance are not considered original equity, nor are contributions toward settlement costs.

Original equity is the market value of the property at the time of original loan approval less prior liens, Rural Housing Service loans, and subordinate affordable housing products. For determining original equity, the definition of market value for Self-Help Loans is the appraised value as determined at the time of loan approval/obligation which is subject to completion per plans and specifications. For all other transactions (purchase with/without repairs/improvements, refinance with/without repairs/improvements, or new construction), the market value is defined as the lower of the purchase price, construction cost, or appraised value (as-is or as-improved, whichever is applicable) as determined at the time of loan approval/obligation.

## **8. *Capital Improvements***

Borrowers must identify any capital improvements in order to receive a credit for them. The value of a capital improvement will be determined by an appraiser based on the change in the property's value attributable to the improvement. The cost of making the improvement will ***not*** be considered when making this assessment. Borrowers who wish to receive credit for capital improvements will specifically request that the appraiser provide this service when the borrower or Agency obtains an appraisal for determining recapture.

## Paragraph 2.23 Calculating Recapture Owed

***9. Amount Due if There is No Value Appreciation***

If Part I of the Final Payoff Worksheet, Attachment 2-A, indicates that there has been no value appreciation, the amount due will be the amount of the loan to be repaid, and, if applicable, the amount of any equity recapture due from an FLP loan. Part II of the Final Payoff Worksheet, Attachment 2-A, provides a formula for this calculation.

***10. Percentage of Outstanding Balance of Loans (Percentage of Total Debt Subject to Recapture to be Paid-Off)***

Part III of the Final Payoff Worksheet, Attachment 2-A, is designed to recapture value appreciation in proportion to the size of the loan or loans subject to recapture. Loans not subject to recapture are not considered in the recapture calculation. For example, if the Agency loan to be repaid accounts for 75 percent of the balance of all loans on the property, recapture would be calculated on only 75 percent of the value appreciation in the property. The formula for determining the percentage of the value appreciation attributable to loans subject to recapture is:

$$\frac{\text{Balance of loans subject to recapture being paid off}}{\text{Balance of all open (including leveraged) loans}}$$

***11. Recapture Percentage***

Recapture percentage is determined by the number of months the loan has been outstanding and the average subsidized interest rate paid over the years. If more than one loan is being paid off, the recapture percentage is determined by a weighted average interest factor.

***12. Return on Borrower's Equity***

Return on the borrower's equity is the difference between 100 percent and percent of borrower's original equity.

***13. Portion of Value Appreciation Subject to Recapture***

Part IV of the Final Payoff Worksheet, Attachment 2-A, calculates the amount of value appreciation to be recaptured based on a recapture factor. The percentage of value appreciation that is recaptured ranges from 9 to 50 percent, depending on the number of months the loan has been outstanding and the average subsidized interest rate the borrower has paid over the years. In addition, borrowers are given credit for their original equity as a percentage of original

market value by multiplying the Value Appreciation by that percentage. *Form RD 3550-12* specifies the percentage of original equity.

#### ***14. Amount Due if There is Value Appreciation***

Part V of the Final Payoff Worksheet, Attachment 2-A, is designed to combine all costs the borrower must repay into a single payoff amount. This amount begins with the amount of the Agency loan or loans to be repaid. It also includes any FLP equity recapture, any PRAS, plus the lesser of the amount of subsidy received, or the Portion of the Value Appreciation subject to recapture.

### **2.24 COLLECTING RECAPTURE INFORMATION**

Subsidy Recapture is calculated upon request for a final payoff amount, or when an account is paid in full (exclusive of recapture). In most cases a borrower who wishes to pay off their loan will contact the Servicing Office and request a payoff statement. Initially a statement of loan balance is sent instructing the borrower to provide certain documentation including an appraisal or an arm's length sales contract to calculate the amount of subsidy recapture due. Upon receipt of the documentation the Servicing Office will calculate recapture due and issue a final payoff statement.

In the majority of cases the field offices have no involvement in this process.

#### **A. Payoff With Final Payoff Statement**

A final payoff statement including subsidy recapture will be issued by the Servicing Office upon receipt of the following items:

- **Payoff date.** The amount of subsidy received will vary depending on the date the loan is paid off.
- **Market value of the property.** The market value of the property on the payoff date must be documented by an arm's length sales contract or a current appraisal meeting Agency appraisal standards. A Broker's Price Opinion is not acceptable.

## Paragraph 2.24 Collecting Recapture Information

- **Added value of capital improvements.** A borrower will ask the appraiser to document the portion of any increase in the property's value attributable to capital improvements in a separate Addendum to the appraisal. The Addendum will itemize the capital improvement made. Receipts cannot be used to determine the value of the improvements but may be valuable in ascertaining what improvements were made by the borrower. No credit for capital improvements will be given without an appraisal documenting the value of the capital improvements.
- **Estimated settlement statement.** A borrower who is refinancing will receive credit for settlement costs, which are reasonable and customary in the area, if they are documented by a good faith estimate provided by the lender or an estimated settlement statement provided by the closing agent. A borrower who is selling their house will receive credit for settlement costs, which are reasonable and customary in the area, if they are documented by an estimated settlement statement provided by the closing agent. The documentation must itemize costs paid by the borrower. An estimate from a real estate agent is not acceptable in either situation.

**B. Payoff Without Contacting the Servicing Office for a Final Payoff Statement, or Final Installment Payment**

For borrowers that pay off their loan (regardless of why the loan is being paid off), without contacting the Servicing Office or the field office for a payoff statement, a "Congratulations" letter is sent from the Servicing Office informing them of the total amount of subsidy received along with instructions for calculating the actual subsidy recapture due. In these situations, the Agency is responsible for determining the market value for purposes of calculating subsidy recapture and the Servicing Office will request assistance from the field offices to determine the market value. Market value will be determined by an appraisal, an arm's length sales contract, assessed value, tax records, or other reliable evidence. If an appraisal is necessary, the costs associated with obtaining an appraisal will be paid by the Agency. If the borrower disagrees with the Agency's valuation, the borrower may provide their own appraisal for consideration meeting Agency standards.

***1. Determining Market Value***

States vary in the methods used for obtaining appraisals; some use contract appraisers, others do their own appraisals. An abbreviated or limited appraisal (shows the market comparison only) or assessed value may also be used if the field office believes that it accurately reflects the market value of the property. If an assessed value is used, a copy of the assessment

and a written statement from the field office indicating the assessed value and that it accurately reflects the market value should be provided to the Servicing Office. Either process is acceptable based on whatever is appropriate for the state.

If capital improvements are to be considered an appraisal and an addendum to the appraisal is required. The addendum must be completed by an appraiser and should include an itemization of the added value for each capital improvement.

If an outside appraisal is needed, the Agency will incur the costs and the borrower will not be charged an appraisal fee. Costs associated with obtaining an appraisal in these instances will be paid from Program Loan Costs Funds using the “Direct Loan Financing Account” (R funds) and code “S2B1” including the borrower’s account number.

## ***2. Borrower Notification – Servicing Office and Field Office Interface***

When the Servicing Office becomes aware that an account has paid off and recapture has not been calculated, they will task the field using task #590 *P & I PIF/Recap Receivable Established. DO NOT RELEASE THE SECURITY INSTRUMENTS*. The expiration timeframe will be 60 days. At the same time, task #589 *Early Payoff Notification* will be sent to the state office queue. The expiration timeframe will be 45 days to allow for follow-up before the 60 days expire. This will be an indication that the “Congratulations” letter has been sent from the Servicing Office and that the field should begin the process to have the market value established. An appraisal/evaluation should not be completed until the borrower has been given the opportunity to provide information about whether they are seeking credit for capital improvements. If the borrower does not reply within 15 days the field office can proceed in obtaining an appraisal/valuation of the property. Field offices should establish a “tickler” for the capital improvements form or contact the borrower directly for this information. The field office will have a total of 60 days to provide the market valuation to the Servicing Office. Once market value is determined, a request for calculation of recapture should be faxed to the Payoff Unit at 314- 457-4433. The information faxed to the Servicing Office should include a cover letter stating the purpose of the request, a contact person, fax and phone number, and a copy of all supporting documents.

## Paragraph 2.24 Collecting Recapture Information

The Servicing Office will calculate recapture due and send a letter to the borrower giving 120 days to either pay the recapture amount owed, or defer payment. If the recapture is paid within 120 days and the borrower retains title and continues to occupy the property, the borrower will receive a 25% discount. The Servicing Office will also fax a copy of the letter to the field office. The case file should be marked as a recapture receivable account. If the borrower pays the recapture amount due in full, the field office will get the standard queue to prepare the release of lien.

**2.25 DEFERRING PAYMENT OF RECAPTURE**

A borrower who repays a loan has the option of deferring payment of recapture as long as title does not transfer, and the borrower continues to occupy the property. Deferring payment of recapture typically occurs when a borrower refinances an Agency loan with private credit or pays the last loan installment.

If the borrower defers payment of recapture, an interest-free recapture receivable account must be established. The recapture receivable is not due unless the borrower ceases to occupy the property or transfers title, but payment may be made at any time. The Servicing Office must provide an annual statement indicating the unpaid recapture amount.

**A. Refinancing with Private Credit**

The Agency will subordinate its interests during the deferral to allow the borrower to refinance with private credit if the total amount of the proposed prior lien debt plus the recapture amount is less than or equal to the market value of the property. The amount to which the remaining Agency debt can be subordinated cannot exceed the total of: the amount required to repay the Agency debt, exclusive of recapture, reasonable settlement costs, up to 1 percent of the loan amount for servicing costs if required by lender, and the cost of any necessary repairs or improvements to the security property.

**B. Incentive to Pay Recapture**

It is to the Agency's advantage to reduce the number of recapture receivable accounts that must be tracked over the long term. As an incentive to encourage certain borrowers not to defer recapture, a 25 percent discount may be offered. The discount may only be offered to borrowers who are retaining title to the property and will continue to occupy the house. This generally occurs when the borrower is refinancing with private credit. The discount is not

Paragraph 2.25 Deferring Payment of Recapture

available for borrowers who sell their homes, transfer title, or no longer occupy the property. In cases where the recapture is triggered by the final installment payment or when the payoff was sent without contacting the Servicing Office for a final payoff statement, the borrower will have 120 days from the day of receipt of the letter that informs them of the recapture amount to receive the 25 percent discount.

## **2.26 TRUST ACCOUNTS**

A small number of former Agency loans that were sold to the Trust in the 1987 rural housing asset sale are no longer serviced by the Agency but are still subject to recapture. The Trust will work with their borrowers to calculate and collect recapture amounts. If a Trust borrower wishes to defer recapture payment, the account must be reassigned to the Agency. Once the Trust has reassigned the security instrument and note, and indicated the recapture amount, the Servicing Office can establish a receivable account. The Servicing Office should send the original reassigned security instrument and note to the appropriate Field Office with instructions to record the reassigned security instrument. Any costs associated with recordation are Non-recoverable.



Paragraph 2.27 Final Payments

## **SECTION 6: FINAL PAYMENTS** *[7 CFR 3550.161]*

### **2. 27 FINAL PAYMENT AMOUNT**

A borrower's account cannot be closed until the Agency receives payment in full. The final payment amount consists of:

- **Outstanding account balance**, including unpaid principal and interest, fees, charges, and any protective advances, FLP equity recapture, and unauthorized assistance; and
- **Recapture**, as calculated in accordance with Section 5, Paragraph 2.23. Borrowers with loans approved before October 1, 1979, are not subject to subsidy recapture.

Even if the borrower repays the full outstanding account balance, the account is not considered paid in full until recapture is paid. In cases where the Agency agrees to debt settlement as described in Section 3 of Chapter 7, the account will be considered satisfied when the settlement amount agreed to by the Agency is repaid.

Any funds remaining in a borrower's escrow account and any supervised bank account funds will be returned to the borrower separately.

### **2. 28 PAYOFF STATEMENTS**

Before paying the final payment amount due on a loan, the borrower should obtain a payoff statement from the Servicing Office. The person requesting the statement need not be the borrower as long as the borrower provides written authorization for the request. Written authorization is not needed from financial institutions or its agents as long as they can provide the borrower's social security number and account number. The Servicing Office will send a written statement to the requester (with a copy to the borrower, if the requester is someone other than the borrower, such as a real estate agent or lender). The Servicing Office will never provide a final payoff amount over the telephone. All final payment amounts must be provided through payoff statements.

Field Offices can request a payoff by completing Attachment 13-A contained in the Field Office Handbook (HB-1-3550). The attachment is faxed to the Payoff Section in the Servicing Office or payoffs may be requested by the Field Offices calling the 1-800 number.

Because the exact amount of the final payment is contingent upon the date final payment is received and the amount of recapture that must be paid, the Servicing Office will not be able to give an accurate payoff amount without specific information from the borrower. For this reason, two types of payoff statements will be provided.

#### **A. Statement of Loan Balance**

The statement of loan balance provides the current outstanding balances of the loan, which includes principal, interest, fees, late charges, and escrow (if applicable). The statement also includes the total amount of subsidy (including PRAS) granted over the life of the loan. The statement instructs the borrower to provide certain documentation including an appraisal or an arm's length sales contract to calculate the amount of recapture due.

#### **B. Final Payoff Statement**

The final payoff statement is based on the anticipated account balance at the proposed payoff date and the recapture amount calculated with whatever information has been provided by the borrower. This statement indicates the actual amount the borrower will be required to repay on the proposed payoff date.

Upon receipt of written confirmation of the information needed to calculate recapture, the Servicing Office will generate a final payoff statement and send it to the borrower. The statement will instruct the borrower where to send the final payment. If the borrower subsequently provides updated information (for example, a revised final payoff date or documentation of additional settlement costs) a new final payoff statement should be generated and sent to the borrower.

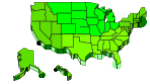
## 2.29 PROCESSING FINAL PAYMENTS

All payments will be date-stamped the day they are received and this date is used to recompute the final payoff amount. If the payoff amount based on the actual date the final payment was received is greater than the amount of the borrower's payment, the payment will be held in suspense until the borrower is contacted and the remaining funds are received. The Servicing Office should discuss the discrepancy with the borrower, agree on a new payoff date, and provide a new final payoff statement indicating the remaining amount due based on the new payoff date. If the borrower pays more than the payoff amount, the Servicing Office

After the correct payoff amount is received, the Servicing Office must take the following actions to close out the account.

### A. Release Security Documents

Since the methods and forms used to release security instruments vary by State, the Servicing Office will ask Field Offices to prepare the necessary documents when a final payment is received. Careful instructions need to be given to the Field Office in these cases since the Agency's security interests may be released. When a borrower's account is paid in full, including all subsidy recapture, all security instruments are generally released. When a borrower's loan balance is paid in full, and they defer the repayment of subsidy recapture, the security instruments are not released but may be subordinated to another lender. In these cases, clear instructions must be given to the Field Office on which documents to prepare.



## Paragraph 2.29 Processing Final Payments

**B. Release Insurance**

The Servicing Office must notify the property insurance company that the Agency's interest in the property has ended.

**C. Terminate Billing and Preauthorized Debits**

When the borrower pays off a loan, the Servicing Office must end its requests for payment through preauthorized debits or regular billing statements.

**D. Terminate Assignments of Income**

The Servicing Office must forward to the borrower any checks received as assignment of income on behalf of a borrower whose account is paid in full and notify the sender by letter that future payments should be made directly to the borrower.

## FINAL PAYOFF WORKSHEET

<b>Part I. Value Appreciation</b>	
<i>(If any calculation in this section yields zero or less, stop and go to Part II.)</i>	
1. Current market value	
2. <i>(less)</i> Original amounts of prior liens and subordinate affordable housing products	
3. Balance (Line 1 - Line 2)	
4. <i>(less)</i> RHS loans being paid off	
5. Balance (Line 3 - Line 4)	
6. <i>(less)</i> Equity recapture due from FLP loan	
7. Balance (Line 5 - Line 6)	
8. <i>(less)</i> Reasonable settlement costs	
9. Balance (Line 7 - Line 8)	
10. <i>(less)</i> Principal reduction (note rate) on RHS loan being paid off	
11. Balance (Line 9 - Line 10)	
12. <i>(less)</i> Principal reduction attributable to subsidy (PRAS) (if applicable)	
13. Balance (Line 11 - Line 12)	
14. <i>(less)</i> Original equity	
15. Balance (Line 13 - Line 14)	
16. <i>(less)</i> Capital improvements (if applicable)	
17. Value Appreciation (Line 15 - Line 16) ( If this is a positive value, continue. If this is a negative value or "\$0", there is no recapture due.)	
<b>Part II. Amount Due if There is No Value Appreciation</b>	
<i>(Complete only if there is no Value Appreciation)</i>	
18. RHS loans being paid off (Line 4)	
19. Equity recapture from FLP loan to be collected (lesser of Line 5 or Line 6)	
20. PRAS to be collected (lesser of Line 11 or Line 12)	
21. Amount due (Line 18 + Line 19 + Line 20)	
<i>(Stop here; do not go on to Line 22)</i>	

<b>Part III. Percentage of Total Debt Subject to Recapture to Be Paid Off</b>	
<i>(Complete only for borrowers with leveraged loans, or if some Agency loans are not subject to recapture or will not be repaid at this time)</i>	
22. RHS loans being paid off which are subject to recapture (Line 4)	
23. Outstanding balance of all RHS loans, prior non-Agency mortgage loans, and subordinate affordable housing products being paid off	
24. RHS loans being paid off as a percentage of all mortgage loans (Line 22 ÷ Line 23)	%
<b>Part IV. Value Appreciation Subject to Recapture</b>	
25. Dollar value of value appreciation attributable to loans subject to recapture (Line 17; or, if Part III was completed, Line 17 x Line 24)	
26. Recapture percentage	%
27. Value appreciation reduced by recapture percentage (Line 25 x Line 26)	
28. Percentage of original equity (from Subsidy Repayment Agreement)	%
29. Value appreciation, reduced by recapture percentage, attributable to original equity (Line 27 x Line 28)	
30. Portion of Value Appreciation subject to recapture (Line 27 - Line 29)	
<b>Part V. Amount Due if There is Value Appreciation</b>	
31. Amount of payment subsidy received	
32. Recapture amount (Line 12 + lesser of Line 30 or 31)	
33. Discounted recapture amount, if applicable (Line 32 x 75%)	
34. Final payoff amount (Line 4 + Line 6 + Line 32 or Line 33 as appropriate)	

## ATTACHMENT 2-B

HB-2-3550  
Attachment 2-B  
Page 1 of 4

### SUBSIDY RECAPTURE CASE STUDY

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#### A. THE SITUATION

John and Sharon Potter bought their home 10 years ago for \$50,500. The home appraised for \$50,500 but they only qualified for a loan of \$50,000. They borrowed \$50,000 through a 33 year Section 502 loan and paid the remaining \$500 of the purchase price and \$1,000 for closing costs out of their savings.

The Potters' Note Rate is 7 percent, but they have received payment subsidy throughout the 10 years. For the first 5 years they had interest credit and a subsidized interest rate of 1 percent. Then John got a big promotion. In the midst of the family's excitement they neglected to submit the income certification information required for payment subsidy renewal. Shortly after their interest credit agreement lapsed, they submitted their information and began receiving payment assistance with an Effective Interest Rate (EIR) of 4 percent.

In year 6 of the loan the roof developed major problems. It needed to be replaced and the interior needed repairs to address the water damage. The Agency agreed to subordinate its interests to allow the Potters to obtain a loan from Big Bank for the \$5,000 needed to take care of the problem.

Last year, the Potters added a deck. The materials cost \$1,250, but since they built it themselves, there were no labor costs.

Sharon just got a great new job, and the family is selling the house and moving to a bigger place on the other side of town. They are working with Big Bank to finance the new home. They are putting down \$5,000, paying \$1,000 in points, and are financing the rest of the closing costs.

In preparation for selling the house, the Potters spent \$3,000 on new wall-to-wall carpeting and installed a new high-efficiency water heater for \$500.

The Potters have found buyers for their house and have signed a sales contract for \$65,000. They must pay \$1,500 in closing costs.

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**B. INPUTS FOR VALUE APPRECIATION CALCULATION**

- **Current market value.** Since the house is being sold in an arm's length transaction, the \$65,000 from the sales contract can be used as current market value and no appraisal is required.
- **Balance due prior lien holders.** The Potters have been making regular payments on the prior lien to Big Bank and have reduced the outstanding balance to \$1,000.
- **Balance due Agency.** The remaining loan balance due the Agency is \$38,510.
- **Unreimbursed closing costs.** The Potters are paying \$1,500 in unreimbursed closing costs to sell their home.
- **Principal reduction.** The Potters' principal reduction at the note rate was \$5,605 and principal reduction attributable to subsidy (PRAS) was \$5,885.
- **Original equity.** The difference between the purchase price on the amount of the loan was \$500.
- **Capital improvement credit.** When the new buyer's appraiser appraised the property, the Potters asked if he would document the increased value attributable to the improvements they had made. They showed him their receipts for \$1,250 for the deck and described the labor they had put into it. However, the appraiser concluded that the deck only added \$500 to the overall value of the home.

They also provided receipts for the carpet (\$3,000) and the water heater (\$500) for a total of \$3,500. The appraiser concluded that these improvements added \$2,000 to the value of the property. However, since the carpet and water heater are not capital improvements, only the \$500 value increase from the deck can be counted.

**C. INPUTS FOR RECAPTURE CALCULATION**

- **Appreciation attributable to loans subject to recapture.** The Potters' outstanding Agency balance is \$38,510, and their Big Bank balance is \$1,000, for total outstanding loans totaling \$39,510. Only the Agency loan is subject to recapture.
  - **Recapture factor from subsidy repayment agreement.** The Potters' Subsidy Repayment Agreement stipulates that a factor of 50 percent will be used to calculate subsidy subject to recapture.
  - **Appreciation attributable to original equity.** The Potters' original equity was \$500 and the original market value was \$50,500.
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**POTTER FAMILY  
FINAL PAYOFF WORKSHEET**

<b>Part I. Value Appreciation</b>	
<i>(If any calculation in this section yields zero or less, stop and go to Part II.)</i>	
1. Current market value	\$65,000
2. (less) Original amounts of prior liens and subordinate affordable housing products	\$5,000
3. Balance (Line 1 - Line 2)	\$60,000
4. (less) RHS loans being paid off	\$38,510
5. Balance (Line 3 - Line 4)	\$21,490
6. (less) Equity recapture due from FLP loan	0
7. Balance (Line 5 - Line 6)	\$21,490
8. (less) Reasonable Settlement costs	\$1,500
9. Balance (Line 7 - Line 8)	\$19,990
10. (less) Principal reduction (note rate) on RHS loan being paid off	\$5,605
11. Balance (Line 9 - Line 10)	\$14,385
12. (less) Principal reduction attributable to subsidy (PRAS) (if applicable)	\$5,885
13. Balance (Line 11 - Line 12)	\$8,500
14. (less) Original equity	\$500
15. Balance (Line 13 - Line 14)	\$8,000
16. (less) Capital improvements (if applicable)	\$500
17. Value appreciation (Line 15 - Line 16) (If this is a positive value, continue. If this is a negative value or "\$0", there is no recapture due.)	\$7,500
<b>Part II. Amount Due if There is No Value Appreciation</b>	
<i>(Complete only if there is no Value Appreciation)</i>	
18. RHS loans being paid off (Line 4)	
19. Equity recapture from FLP loan to be collected (lesser of Line 5 or Line 6)	
20. PRAS to be collected (lesser of Line 11 or Line 12)	
21. Amount due (Line 18 + Line 19 + Line 20)	
<i>(Stop here; do not go on to Line 22)</i>	

<b>Part III. Percentage of Total Debt Subject to Recapture to Be Paid Off</b>	
<i>(Complete only for borrowers with leveraged loans, or if some Agency loans are not subject to recapture or will not be repaid at this time)</i>	
22. RHS loans being paid off which are subject to recapture (Line 4)	\$38,510
23. Outstanding balance of all RHS loans, prior non-RHS mortgage loans, and subordinate affordable housing products being paid off	\$39,510
24. RHS loans being paid off as a percentage of all mortgage loans (Line 22 ÷ Line 23)	97.47%
<b>Part IV. Value Appreciation Subject to Recapture</b>	
25. Dollar value of value appreciation attributable to loans subject to recapture (Line 17; or, if Part III was completed, Line 17 x Line 24)	\$7,310
26. Recapture percentage	50%
27. Value appreciation reduced by recapture percentage (Line 25 x Line 26)	\$3,655
28. Percentage of original equity (from Subsidy Repayment Agreement)	0.99%
29. Value appreciation, reduced by recapture percentage, attributable to original equity (Line 27 x Line 28)	\$37
30. Portion of Value Appreciation subject to recapture (Line 27 - Line 29)	\$3,618
<b>Part V. Amount Due if There is Value Appreciation</b>	
31. Amount of payment subsidy received	\$15,000
32. Recapture amount (Line 12 + lesser of Line 30 or 31)	\$9,503
33. Discounted recapture amount, if applicable (Line 32 x 75%)	0
34. Final payoff amount (Line 4 + Line 6 + Line 32 or Line 33 as appropriate)	\$48,013

## ATTACHMENT 2-C

### UNITED STATES DEPARTMENT OF AGRICULTURE SERVICING BORROWERS WITH BOTH RURAL HOUSING SERVICE (RHS) AND FARM SERVICE AGENCY (FSA) FARM CREDIT PROGRAM (FCP) LOANS

---

#### 1 Overview

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##### A

##### Background

Before reorganization, borrowers who had both RHS and FSA FCP loans, were handled according to RD Instruction 1965-A. The majority of these loans is cross-collateralized and described on the same mortgage or deed of trust. Since reorganization split the ownership of these loans into two separate Agencies, the case files and servicing procedures must also be split. FSA will now service all FCP loans and the RHS of the Rural Development mission area will service all Rural Housing (RH) (Section 502 loans and 504 loans and grants) and Labor Housing (LH) loans.

---

##### B

##### Purpose

This attachment provides guidance to Field Offices on how to handle the following servicing actions for borrowers with both RHS and FSA FCP loans.

- Separating borrower case files and flagging the account. See paragraph 2.
- Identifying and servicing RH loans for FSA buildings (RHF). See paragraph 3.
- General servicing procedures, such as graduation, refinancing, partial releases, releases, and determining lien position. See paragraph 4.

## 1 Overview (Continued)

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### **B Purpose**

- Servicing delinquent and financially distressed accounts. See paragraph 5.
- Handling foreclosures and voluntary conveyances. See paragraph 6.

A Memorandum of Understanding (MOU) is being developed that will outline how accounts will be handled in the future. Until this MOU is issued, servicing will be handled according to this attachment.

---

### **C Contact**

If there are questions regarding this attachment:

- Field Offices shall contact their State Office
  - FSA State Offices shall contact Kim Laris, LSPMD, through the Area Office
  - Rural Development State Offices shall contact the Deputy Administrator, Single Family Housing in the National Office.
- 

## 2 Initial Action

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### **A Separating Borrower Case Files**

Borrower case files must be split into two separate case files, if not already split. One file will be for the RHS loan and one file for the FSA FCP loan.

**Note:** RHF loans, identified with a fund code 41 and a kind code 10, are FCP loans and will be part of the FSA case file.

FSA shall retain the original case file, but move the following documents to the RHS file:

- all original documents pertinent to the RH or LH loan only

Examples: Promissory note, mortgage or deed of trust that describes only the RH or LH note, Payment Assistance Agreement

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## 2 Initial Action (Continued)

### A Separating Borrower Case Files (Continued)

- copies of all joint documents and running records that pertain to both the RHS and FSA FCP loans.

Example: Applications, farm and home plans, mortgages or deeds of trust, appraisals.

- copy of any Equity Recapture Agreement, FSA Instruction 1965-A, Exhibit D.

FSA will provide RHS with access to original documents from the borrower's case file upon request.

---

### B How Accounts Will Be Flagged

To help identify borrowers who have both RHS and FCP loans described on the same security instruments:

- both Agencies must mark the front of their case files in red with, "RHS/FSA Joint Security Instruments"
- the Management Record System shall be flagged.

The following Finance Office status reports and Automated Discrepancy Processing System (ADPS) inquiry screens reflect that the borrower has an RHS and FSA FCP loan:

- for FSA, the 540 Status Report will continue to show "RH" at the right of the report under the "Scheduled Annual Installments" column

for RHS, the Dedicated Loan Origination and Servicing (DLOS) System will be flagged to show that the borrower has FCP loans

Note: There is no identifier on the RC 580 and 582 reports.

---

## 2 Initial Action (Continued)

### B

#### How Accounts Will Be Flagged (Continued)

- for FSA and RHS, the Current/Past Debts Inquiry Screen will continue to show both the RHS and FSA FCP loans.

These reports and screens do not reflect that the security is cross-collateralized or that the loans are described on the same mortgage or deed of trust. Therefore, anytime the security will be subordinated, released, liquidated, etc., the security instruments will have to be carefully reviewed to determine whether both agencies must be involved.

---

### C

#### Release of Additional Security

To simplify servicing in the future, FSA may consider releasing nonfarm dwellings that were financed with RH or LH funds and taken as additional security for the FCP loan. FSA shall refer to FSA Instruction 1965-A, section 1965.25(d) for guidance.

RHS may also consider releasing any farm property that was taken as additional security for the RH or LH loan or that was cross-collateralized because of the FCP loans. RHS shall refer to 7 CFR part 3550 for RH loans. For LH loans, an exception to the requirements of RD Instruction 1965-B, §1965.77, must be requested from the RHS Administrator.

**Note:** The mortgage or deed of trust **cannot** be released of record if it describes both the RHS and FSA FCP loan. Refer to paragraph 4 D for issuing a letter of release to the non-releasing Agency for joint mortgages or deeds of trust.

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## 2 Initial Action (Continued)

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### D

#### **Insurance Policies**

Each agency shall notify their borrowers to contact their insurance company and have the lienholder or mortgagee name changed in the mortgagee clause or declaration page to read:

UNITED STATES OF AMERICA, ACTING THROUGH THE UNITED  
STATES DEPARTMENT OF AGRICULTURE  
ATTN: [AGENCY NAME]  
[ADDRESS]

Both RHS and FSA should be named as mortgagee and the addresses for both should be given so that each agency will receive notices from the insurance company of cancellation, loss claims, etc. Field Offices may want to contact the insurance company directly if the company name is available. A copy of the change must be filed in the borrower's case file. Follow-up action is necessary to assure the change was made.

---

## 3 RHF Loans

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### A

#### **Identifying RHF Loans**

RHF loans shall be serviced by FSA as an FCP loan. These type loans were made with RH funds before 1974 to construct farm buildings, such as chicken houses, silos, barns, etc. These loans were officially transferred to FSA on October 2, 1995 and should no longer show on the RC 580 and 582 reports. During the transfer, the fund code was changed from a 36 or 46, kind code 10, to a fund code 41, kind code 10. These loans are now shown on the 540 Status Report.

**Note:** If any of these loans have not been transferred, FSA State Offices should prepare a memorandum:

- to KCMO, St. Louis, attention Janet Marxkors, FAX 314-539-6447
- including the borrower's name, case number, fund code, loan number, existing kind code, date of original loan, and purpose of loan

### 3 RHF Loans (Continued)

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#### A

##### Identifying RHF Loans (Continued)

- requesting that the:
    - loan be transferred to FSA
    - fund code be changed to a 41
    - kind code be changed to a 10.
- 

#### B

##### Servicing RHF Loan

When making future Farm Ownership (FO) loans and providing loan servicing, RHF loans will:

- not be counted as an FO loan for determining FO loan limitations
  - be included in DALR\$ as a fund code 46 if being considered for restructuring and:
    - be charged the lower of the original note rate or the current RH loan rate
    - be amortized up to 33 years from the date of the original note
    - require the borrower to sign Form RD 1940-17, Promissory Note
- 

### 4 General Servicing Procedures

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#### A

##### Payoff Requests

When FSA and RHS are joint creditors and a request for payoff information is received, in addition to giving the payoff information, the contacted Agency should also alert the requestor that the other Agency also has a loan and how to secure the payoff information for that loan.

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#### **4 General Servicing Procedures (Continued)**

##### **B**

##### **Refinancing and Classification**

Refinancing and classification of accounts will be handled separately by each Agency based solely on the loans of each Agency. Copies of financial statements, cash flows, and other related documents may be shared with each Agency upon request.

##### **C**

##### **Partial Releases, Subordinations, and Consents for Joint Security Instruments**

Approval from both Agencies is required when issuing partial releases, subordinations, and consents against security instruments that describe both the RHS and FSA loan. Only one Form RD 465-1, Application for Partial Release Subordination, or Consent, is needed. The Agency receiving Form RD 465-1 shall take the lead in processing the request and obtaining the required approvals from the other Agency. The lead Agency will obtain any appraisals needed. Appraisals for farm tracts must meet the requirements of RD Instruction 1922-E, and appraisals for nonfarm tracts must meet the requirements of 7 CFR part 3550. Authority to execute these actions will be based on the established policies and procedures of each Agency.

If both Agencies cannot approve the request, it will be denied. Responses to the borrower's request may be issued in one letter by the lead Agency or separated in two letters, one from FSA and the other from RHS.

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#### **4 General Servicing Procedures (Continued)**

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##### **D**

##### **Release of Joint Security Instruments**

FSA and Rural Development State Office approval is required to release security instruments that describe both an RHS and FSA loan. If all the security cannot be released because of outstanding obligations by the other Agency, then the following steps must be taken:

- if FSA's debt is paid in full or satisfied first, then FSA will forward the original joint security instruments to the Rural Development State Office with a letter indicating satisfaction of the debt
  - if RHS's debt is paid in full or satisfied first, then Rural Development will send the FSA State Office a letter indicating satisfaction of the debt
  - return of promissory notes will be handled according to RD Instruction 1951-D (for FSA), Chapter 7 of HB-2-3550 (for RHS), and applicable State Instructions.
  - a copy of the releasing Agency letter, if applicable, will be attached to the security instruments in the borrower's case file.
  - the security instruments will be released by the remaining Agency when appropriate.
- 

##### **E**

##### **Determining Lien Position When Both RHS and FSA Loan Were Made at the Same Time**

The lien position shall be shared by both RHS and FSA when the RHS and FSA FCP loans were made at the same time, or the security was taken at the same time, and included on the same mortgage or deed of trust. The amount shared will be proportionate to the total amount of debt owed on these loans.

See the "Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages," at the end of this attachment for determining the amount to enter in DALR\$ if the borrower is being serviced under FSA Instruction 1951-S.

See "Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages," for sales by borrower, foreclosures, deeds in lieu of foreclosure (voluntary conveyances), or losses covered by insurance.

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#### 4 General Servicing Procedures (Continued)

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##### **F**

##### **Offsets**

Offsets for both Agencies will continue to be handled according to applicable Agency regulations. Payments received from administrative offsets that were established before reorganization will be paid to each Agency in order of lien priority. If both Agencies have the same lien priority, offset payments will be distributed on a prorata basis according to the “Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages,” at the end of this attachment.

IRS offsets established before reorganization will be paid to each Agency based on oldest delinquency date. If both Agencies have the same delinquency date, offset payments will be distributed on a prorata basis based on percentage of borrower debt. These payments will be processed to the appropriate Agency by the St. Louis Finance Office following review of the borrower's account by Program Reporting Branch representatives from both Agencies.

---

##### **G**

##### **Losses Covered by Insurance**

Both Agencies will handle losses according to RD Instruction 426.1 or 7 CFR part 3550, as appropriate. If insurance proceeds will be used to repair or replace joint security property, then both Agencies must decide who will oversee and approve the repairs and replacements and make all required inspections. Normally, the Agency who holds a prior lien will be responsible for seeing that any repairs or replacements are completed. However, these duties may be shared by both Agencies to the extent that FSA may handle all farm property and RHS may handle Single Family Housing (SFH) property.

Copies of development plans, inspections, etc. shall be shared with the other Agency. Proceeds to be applied against the debt will be applied based on lien priority. Both Agencies must approve any release of insurance proceeds of joint secured property.

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#### 4 General Servicing Procedures (Continued)

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##### **H**

##### **ADPS Inquiry Screens and Processing of Transactions**

Both Agencies still have access to all inquiry screens for both RHS and FCP loans.

Generally, ADPS transactions will be processed separately by each Agency. However, there are transactions, for example, the 5G, 5H, 3E, and 4D (flags, acquisitions, and name and address changes), that when processed, affect both the FSA and RHS accounts. For this reason, both Agencies will have to coordinate the processing of such transactions with each other to avoid duplication and problems in the future.

---

##### **I**

##### **Labor Housing Loans**

Generally, LH loans will be serviced by the RHS official responsible for managing the Multi-Family Housing program. However, if the security is the same for both the FCP and LH loan, releases and liquidations will be handled according to this attachment.

---

#### 5 Servicing Delinquent and Financially Distressed Accounts

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##### **A**

##### **Debt Servicing Responsibilities**

Each Agency shall be responsible for servicing its own loans. However, in cases where the loans are cross-collateralized, it will be necessary for both Agencies to work together to protect the Government's security interest.

**Note:** Loans are cross-collateralized when property is used to secure both the RHS and FSA loans. The extent of cooperation needed between the two Agencies will depend on whether both loans are described on the same security instruments.

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## 5 Servicing Delinquent and Financially Distressed Accounts (Continued)

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### **B**

#### **Security Is Not Cross-Collateralized**

When the security is **not** cross-collateralized, the following procedures shall be followed:

- RHS will service RH loans according to 7 CFR part 3550 and LH loans according to 7 CFR part 3560, and other RH and LH procedures.
  - FSA will service FCP loans according to FSA Instructions 1951-S and 1965-A, and other FCP procedures.
- 

### **C**

#### **Security Is Cross-Collateralized and Loans Are Described on Separate Security Instruments**

When the security **is** cross-collateralized, and the RHS and FSA loans are described on separate security instruments:

- normal debt servicing will be handled as described in paragraph 5 B
  - foreclosures and conveyances will be handled according to paragraph 6.
- 

### **D**

#### **Security Is Cross-Collateralized and RH and FCP Loans Are Described on Same Security Instruments**

FSA Instruction 1965-A, section 1965.26(c)(2) or (3) and the instructions in this paragraph must be followed by both Agencies when the security **is** cross-collateralized and RHS and FSA loans are described on the **same** security instrument.

Default on any one loan, whether RHS or FSA loan, constitutes default against the security instrument. Therefore, even if only one Agency's loan is in default, the borrower is in nonmonetary default with the other Agency.

## **5 Servicing Delinquent and Financially Distressed Accounts (Continued)**

---

**D  
Security Is  
Cross-  
Collateralized  
and RH and  
FCP Loans  
Are  
Described on  
Same  
Security  
Instruments  
(Continued)**

The following describes each Agency's responsibility for notifying the other when their loan is in default.

- If the FSA loan is in default for reasons other than the RHS loan is in default:
  - FSA shall notify the Rural Development Field Office when the borrower is sent the 1951-S servicing notices
  - RHS will consider the borrower for moratorium and payment subsidy.
- If RHS loan is delinquent or otherwise in default for reasons other than the FSA loan is in default:
  - RHS will service the RHS loan according to 7 CFR part 3550 up through acceleration
  - once the account is accelerated, RHS will notify FSA and send FSA a copy of the acceleration notice

**Note:** RHS will not proceed with foreclosure action until after FSA has completed its servicing process.

- after FSA is notified of the RHS acceleration, FSA will send the borrower FSA Instruction 1951-S, Exhibit A, Attachments 1, 3, and 4 for reason of nonmonetary default and service accordingly.

## **5 Servicing Delinquent and Financially Distressed Accounts (Continued)**

---

### **D Security Is Cross- Collateralized and RH and FCP Loans Are Described on Same Security Instruments (Continued)**

- The following are general rules that apply in all instances.
  - Each Agency will keep the other up to date on the status of the default and the servicing progress.
  - If it is determined necessary to bring the RHS account current or find a feasible farm plan, the RHS loan may be reamortized by RHS when the FSA loans are restructured. Reamortization of the RHS loan must be closed before or simultaneously with the FCP loans. Any new security instruments taken will be separate for each Agency's loans.
  - RHS will accelerate the account when notified by FSA that the borrower was notified of FSA's intent to accelerate (FSA Instruction 1951-S, Exhibit A, Attachments 1, 3 and 4, 5 and 6, 5-A and 6-A, 9 and 10, or 9-A and 10-A).
  - Acceleration notices must describe the reasons for acceleration, such as monetary or nonmonetary default, or both. Caution should be given to accepting an offer by the borrower that would deaccelerate the account as this could affect liquidation by the other Agency.
  - Each Agency shall send the other a copy of the acceleration notice. Appeals will be held separately since they are two separate adverse actions.
  - RHS will continue to flag the account "FAP," foreclosure action pending, when the RHS account is accelerated so that payments will not be credited to the RHS account.

## **5 Servicing Delinquent and Financially Distressed Accounts (Continued)**

### **D**

#### **Security Is Cross-Collateralized and RH and FCP Loans Are Described on Same Security Instruments (Continued)**

- If payments are received on the FCP account before FCP loans are accelerated, Field Offices should indicate on Form RD 451-2, Schedule of Remittances, which the payment should be applied since only the RHS account is accelerated.
- FSA will flag the account "ACL," accelerated, at the time the FCP account is accelerated.
- FSA will flag the account "FAP" in judicial foreclosures when the account is referred to OGC for foreclosure. In nonjudicial foreclosures, the account will be flagged "FAP" when the foreclosure sale is scheduled.
- If the FCP borrower is offered a buyout, and the RHS loan is delinquent, the RHS loan must be paid off at the same time the buyout is completed. RHS will be contacted for payoff information. FSA will handle collection of the RHS loan and distribute proceeds according to Notice FI-2139. The DALR\$ report must be modified to identify the RHS debt to be paid. If the RHS loan is not paid in full, the security instrument cannot be released. See subparagraph 4 D on how to handle releases of joint security instruments.

---

### **E**

#### **Special Instructions for DALR\$**

Follow these special instructions when primary loan servicing will be considered for a borrower with an RH loan.

- RHS loans will not be entered in the DALR\$ loan input screen. Instead, they will be entered as another lender's debt.
  - If the RHS loan will be reamortized, enter the reamortized RHS payment on Form FSA 431-2, Farm and Home Plan, Table K.
-



## **5 Servicing Delinquent and Financially Distressed Accounts (Continued)**

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### **E**

#### **Special Instructions for DALR\$ (Continued)**

- If RHS holds a prior lien to the FSA debt, then the amount of the RHS debt will be entered in the net recovery value screen.
- See paragraph 4 D and the “Guide for Calculating Proportional Share of Joint Security Interest for DALR\$,” at the end of this attachment to determine the proportionate share of each Agency when RHS and FSA loans were made at the same time, or the security was taken at the same time, and described on the same mortgage or deed of trust
- If RHS loan is junior to one loan and before other FSA loans, then enter only the amount of RHS debt less the prior lien debt of the FSA loan, if any.
- If the RHS loan is to be paid in full at the time of buyout according to paragraph 4 D, add the following statement to the DALR\$ report at the bottom of the summary page:

"If you choose to buyout your FCP loans, you must also pay off your RHS loan(s). The unpaid balance on this loan(s) as of \_\_\_\_\_ is \$\_\_\_\_\_."

---

### **F**

#### **Bankruptcy Filings With Joint Security Instruments**

Each Agency will handle bankruptcies separately according to their Agency regulations. Proof of Claim forms will be completed by each Agency. Any necessary legal coordination will be handled by OGC.

---

## **6 Handling Foreclosures and Voluntary Conveyances Against Joint Security**

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### **A**

#### **Loans Described on Separate Security Instruments**

The following procedures will be followed for voluntary conveyance, foreclosures by RHS and FSA, and third party foreclosures of cross-collateralized property when RHS and FSA loans are described on **separate** security instruments.

#### **Voluntary Conveyance**

If one Agency is proposing to accept a voluntary conveyance, (deed in lieu of foreclosure), the initiating Agency will obtain a current appraisal and a title opinion indicating lien position and send copies of both to the responding Agency with a request for release.

- If the lien is valueless, the responding Agency will prepare and send the initiating Agency a release.
- If the responding Agency holds a prior lien, the initiating Agency will voucher a check to pay off the responding Agency's lien before accepting the conveyance.
- If the responding Agency holds a junior lien, the initiating Agency will voucher a check to pay the responding Agency's lien up to the current market value of the security property, minus prior liens.

#### **Foreclosure**

If one Agency is initiating foreclosure, a determination must be made to do one of the following:

- pay off the other Agency's prior lien up to the current market value, minus other prior liens
  - obtain a release from the responding Agency, if their lien is valueless
-

## **6 Handling Foreclosures and Voluntary Conveyances Against Joint Security (Continued)**

---

### **A**

#### **Loans Described on Separate Security Instruments (Continued)**

- obtain an agreement to be named in the foreclosure suit, or given notice of the foreclosure.

**Note:** All efforts should be made to eliminate having to get the other Agency involved in the foreclosure.

#### **Third Party Foreclosures**

Third party foreclosures initiated by other than RHS and FSA will be handled separately by each Agency based on their regulations for handling third party actions.

- FSA will use FSA Instruction 1965-A, section 1965.11(c).
  - RHS will use RD Instruction 1965-B or 7 CFR part 3550, as applicable.
  - Both Agencies may bid according to RD Instruction 1955-A, section 1955.15(f) or 7 CFR part 3550, as applicable.
- 

### **B**

#### **Loans Described on the Same Security Instruments**

The following procedures will be followed for voluntary conveyances, (deeds in lieu of foreclosure) foreclosures by RHS or FSA, and third party foreclosures of cross-collateralized property when both the RHS and FSA loans are described on the **same** security instruments or a combination of separate and same security instruments.

#### **Voluntary Conveyance**

If one Agency is proposing to accept a voluntary conveyance (deed in lieu of foreclosure), the initiating Agency will obtain a current appraisal and a title opinion indicating lien position and send copies of both to the responding Agency with a request for release.

## **6 Handling Foreclosures and Voluntary Conveyances Against Joint Security (Continued)**

---

### **B**

#### **Loans Described on the Same Security Instruments (Continued)**

- if the lien is valueless, the responding Agency will prepare and send the initiating Agency a letter of release as described in paragraph 4 D and the original note (if required by State law to issue releases) and mortgage or deed of trust, if in that Agency's possession
- if the responding Agency holds a prior lien, the initiating Agency will voucher a check to pay off the responding Agency's lien before accepting the conveyance.
- if the responding Agency holds a junior lien, the initiating Agency will voucher a check to pay the responding Agency's lien up to the current market value of the security property, minus prior liens, including the initiating Agency's prior lien
- if the releasing Agency is partially secured with the acquiring Agency, the acquiring Agency will voucher a check to pay the releasing Agency its share of the amount of their debt up to the current market value, minus prior liens. See the "Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages," at the end of this attachment for determining the amount of credit to each loan when the RHS and FCP loan were made or secured with the same property at the same time and described on the same mortgage or deed of trust.

### **Foreclosure**

When foreclosure action is initiated by FSA, RHS, or a third party, the following procedures will be followed.

- If one Agency holds a separate security instrument filed before any joint security instruments, a decision must be made between the two Agencies about which one will bid to protect their security interest or foreclose.
  - If a separate security instrument was not filed before the joint security instruments and both Agencies share in lien priority, FSA will bid or initiate the foreclosure.
-

## **6 Handling Foreclosures and Voluntary Conveyances Against Joint Security (Continued)**

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### **B**

#### **Loans Described on the Same Security Instruments (Continued)**

- The Agency that determined not to bid or foreclose will assign its note or assumption agreement and security interest to the foreclosing or bidding Agency. The foreclosure complaint will identify all FSA and RHS loans.
- States shall request advice from their Regional OGC on preparing an assignment. The assignment shall contain language pertaining to the application of sale proceeds and cancellation of the assignment in the event foreclosure is canceled or the accounts decelerated or reinstated for any reason including bankruptcy. The assignment shall be recorded in the County records.
- The accounting system will not be revised to account for the assignment. The Agency that assigned its note and security interest will wait to debt settle the account after the foreclosure is completed and all proceeds or credits are applied.
- Proceeds from the sale of property or credit for acquisitions will be applied to the loans in the order of lien priority. See the “Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages,” at the end of this attachment for determining the amount to be applied or credited to each loan when the RHS and FSA loan were made or secured with the same property at the same time and described on the same mortgage or deed of trust.
- If the foreclosure is canceled and the accounts decelerated or reinstated, each Agency will resume servicing of their note.

Each Agency will handle debt settlements of their own loans.

## **6 <sup>C</sup> Handling Foreclosures and Voluntary Conveyances Against Joint Security (Continued)**

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### **Assigning Property ID Numbers**

Since the inventory property ID's cannot be duplicated, it will be necessary for each Agency within each State to use the following property ID numbers, along with their State and county code. The last 5 digits must be consecutively numbered within the following range:

- FSA - 00001-00499
- RHS - 00500-00599.

**Note:** The State and county codes are the same as those used for all St. Louis Finance Office purposes, not the former ASCS State and county codes.

Since the property ID numbers include the State and county code, the same numbers within the State can be used by all counties. Designating these ID numbers by Agency will eliminate discrepancies from occurring when counties attempt to assign a number that has already been used by the other Agency in the same county.

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### **D Processing ADPS 3E Transaction for Acquisitions**

The ADPS 3E transaction for acquiring property is a combined transaction that affects both a borrower's FCP and RHS account. Therefore, anytime property is acquired by FSA or RHS from a borrower that has both an RHS and FCP loan, the St. Louis Finance Office must process the 3E transaction. This is the case even if the property is not cross-collateralized. Under no circumstances can a property be acquired jointly.

When property is acquired by FSA or RHS, according to this paragraph, the acquiring Agency shall:

- complete the "ADPS 3E Transaction Form."
- FAX a copy of the "Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages," if applicable, and the "ADPS 3E Transaction" to the St. Louis Finance Office, attention Janet Marxkors, at 314-539-6447.

**Note:** If the security is cross-collateralized, a copy of "Guide for Calculating the Proportionate Share of Security Value/Proceeds from Joint Mortgages," and the "ADPS 3E Transaction" shall also be sent to the nonacquiring Agency

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**Guide for Calculating the Proportionate Share of Security Value/Proceeds From Joint Mortgages**

The proportionate share is based on the market value less prior liens and selling costs.

**Calculation of FSA Share:**

Step 1.  $\frac{\text{FSA Debt}}{\text{1/}} \div \frac{\text{Total RHS and FCP Debt}}{\text{2/}} = \frac{\text{FSA Percent of Debt}}{\text{X}} \times \frac{\text{Market Value/Sales Proceeds less prior liens}}{\text{=}} = \frac{\text{FSA Share of Market Value/Sale Proceeds}}{\text{=}}$

Step 2.  $\frac{\text{FSA Percent of Debt (from Step 1)}}{\text{X}} \times \frac{\text{Liquidation/Selling Expenses}}{\text{=}} = \frac{\text{FSA Share of Expenses}}{\text{=}}$

Step 3.  $\frac{\text{FSA Share of Market Value/Sale Proceeds (from Step 1)}}{\text{-}} - \frac{\text{FSA Share of Expenses (from Step 2)}}{\text{=}} = \frac{\text{Net FSA Share of Market Value/Sale Proceeds}}{\text{=}}$

- 1/ This is the unpaid debt that is equally secured with the other Agency's loan that were made at the same time or the security was taken at the same time to secure both type loans and described on the same mortgage or deed of trust.
- 2/ This is the total unpaid balance of the RHS and FCP loans that are equally secured. All other loans made before and after will not be counted in this calculation.

Note: Debt includes unpaid principal and interest and any recapture due, except RH recapture will not be included if acquired by RHS or FSA.



Guide for Calculating the Proportionate Share of Security Value/Proceeds From Joint Mortgages  
(Continued)

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Calculation of RHS Share:

Step 4. divided by  $\frac{\text{Market Value/}}{\text{of Debt}}$  =  $\frac{\text{X}}{\text{2/}}$  =  $\frac{\text{RHS Debt}}{\text{RHS Share of 1/ Sales Proceeds}}$   $\frac{\text{Total RHS}}{\text{Market Value/ less prior liens}}$   $\frac{\text{RHS Percent and FCP Debt}}{\text{Sale Proceeds}}$

Step 5.  $\frac{\text{RHS Percent of Debt (from Step 4)}}{\text{X}}$  =  $\frac{\text{Liquidation/ Selling Expenses}}{\text{RHS Share of Expenses}}$

Step 6.  $\frac{\text{RHS Share of Market Value/Sale Proceeds (from Step 4)}}{-}$  =  $\frac{\text{RHS Share of Expenses (from Step 5)}}{\text{Net RHS Share of Market Value/ Sale Proceeds}}$

- 1/ This is the unpaid debt that is equally secured with the other Agency's loan that were made at the same time or the security was taken at the same time to secure both type loans and described on the same mortgage or deed of trust.
- 2/ This is the total unpaid balance of the RHS and FCP loans that are equally secured. All other loans made before and after will not be counted in this calculation.

**Note:** Debt includes unpaid principal and interest and any recapture due, except RH recapture will not be included if acquired by RHS or FSA.

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ADPS 3E Transaction\_\_\_\_\_

**A**  
**ADPS 3E** Complete the following for all acquisitions when the borrower has both an  
**Transaction** RHS and FSA loan. **Do not process an ADPS 3E transaction.** Complete 1  
**Form** for each property acquired.

TO: Janet Marxkors, FAX Number 314-539-6447

FROM: \_\_\_\_\_  
Name of Preparer, Agency, and Telephone Number

SUBJECT: Acquisition - Borrower with FSA and RHS Loans

1) ACQUIRING AGENCY NAME (FSA OR RHS) \_\_\_\_\_

2) CASE NUMBER\_\_\_\_\_3) NAME OF BORROWER \_\_\_\_\_

4) OK CODE (Leave Blank) 5) DATE ACQUIRED \_\_\_\_\_

6) MOST SECURED FCP LOAN \_\_\_\_\_ 7) MOST SECURED RHS LOAN \_\_\_\_\_

8) PROPERTY ID OF ACQUIRING AGENCY \_\_\_\_\_

9) PROPERTY DESCRIPTION CODE \_\_\_\_ 10) PROPERTY SUITABILITY CODE \_\_\_\_

11) TAXPAYER ID \_\_\_\_\_  
\_\_\_\_\_

12) PROPERTY ADDRESS (Leave blank if chattel property being acquired)  
\_\_\_\_ Street or route City/Town, State

13) ACRES ACQUIRED: CROPLAND \_\_\_\_\_ PASTURE \_\_\_\_\_ WOODLAND\_\_\_\_OTHER  
\_\_\_\_\_

14) MARKET VALUE - ACQUISITION \_\_\_\_\_ 15) DATE LAST APPRAISAL  
\_\_\_\_\_

16) AMOUNT CREDITED-FSA \_\_\_\_\_ —RHS— TOTAL

17) DATE SUBMITTED \_\_\_\_\_ 18) BUSINESS CODE 19) HOW ACQUIRED

20) FORM CODE \_\_\_\_\_ 21) CARD CODE (Leave Blank)

22) LOANS TO ACQUIRE: (ENTER FUND CODE AND LOAN NUMBER, LEAVE  
BLANK IF ALL FSA AND RHS LOANS ARE TO BE ACQUIRED)  
FSA: \_\_\_\_\_ RHS: \_\_\_\_\_

ADPS 3E Transaction (Continued)

**B**  
**Instructions**      Complete ADPS 3E transaction form according to the following table

Item	Instructions
1-4	Self-explanatory.
5	Enter the date the deed was recorded.
6	Complete if FSA acquired the property or both Agencies will share in the market value credit, otherwise, leave blank.
7	Complete if RHS acquired the property or both Agencies will share in the market value credit, otherwise leave blank.
8	Enter the next available property ID of the acquiring Agency. The first 5 digits must be the first 5 digits of the borrower's case number. The last 5 digits must be in the following range: <ul style="list-style-type: none"><li>FSA - 00001 - 00499</li><li>RHS - 00500 - 00599.</li></ul>
9	Enter 1 of the following property description codes: <ul style="list-style-type: none"><li>01 - Single Family Residence</li><li>02 - Lot Only (Nonfarm tract without Residence)</li><li>03 - Farm (Includes Range or Pasture Land)</li><li>04 - Chattel Property</li><li>08 - Recreation Property</li><li>10 - Nonfarm Property Securing Farm Program Loan</li><li>11 - Other</li><li>15 - Farm with Secretarial Easement</li><li>17 - Indian Land Reservation</li><li>19 - Indian Land Reservation with Secretarial Easement.</li></ul>
10	Enter 1 of the following property suitability codes: <ul style="list-style-type: none"><li>1 - SFH-program/FCP-suitable</li><li>2 - SFH-nonprogram/FCP-surplus</li><li>5 - Other.</li></ul>
11-12	Self-explanatory.
13	Enter the number of acres acquired to the nearest tenth by type if item 9 is 03, 15, 17, or 19.

ADPS 3E Transaction (Continued)

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**B**  
**Instructions**  
**(Continued)**

Item	Instructions
14-15	Self-explanatory.
16	Enter dollars and cents. "TOTAL" must equal the FSA and RHS amount added together.
17	Enter the date the exhibit was prepared and Faxed to the St. Louis Finance Office.
18	<ul style="list-style-type: none"><li>• Enter 1 of the following if item 9 is 03, 15, 17, or 19:</li><li>• 0110 - Cash Grain</li><li>• 0130 - Field Crops other than Cash Grain</li><li>• 0160 - Vegetables</li><li>• 0171 - Berries</li><li>• 0172 - Grapes</li><li>• 0174 - Citrus Fruits</li><li>• 0175 - Deciduous Tree Fruits</li><li>• 0181 - Floriculture and Nursery</li><li>• 0182 - Food Crops Grown Under Cover (Greenhouse)</li><li>• 0211 - Beef Cattle Feedlot</li><li>• 0212 - Beef Cattle other than Feedlot (cow/calf, etc.)</li><li>• 0213 - Hog Farm</li><li>• 0214 - Sheep and Goats</li><li>• 0219 - General Livestock</li><li>• 0241 - Dairy Farm</li><li>• 0251 - Chickens-Broilers</li><li>• 0252 - Chickens-Layers</li><li>• 0253 - Turkeys</li><li>• 0270 - Special Enterprises (Veal, Rabbits, Mink, etc.).</li></ul>
19	<p>Enter 1 of the following codes:</p> <ul style="list-style-type: none"><li>• 1 - Foreclosure</li><li>• 2 - Voluntary Conveyance</li><li>• 3 - Third party Foreclosure (Other than FSA or RHS).</li></ul>

ADPS 3E Transaction (Continued)

B  
Instructions  
(Continued)

Item	Instructions
20	<div>Enter 1 of the following codes:</div> <div><div><div>•</div><div>1 - Released from Liability (Involved in Bankruptcy)</div></div><div><div>•</div><div>2 - Released from Liability (Not Involved in Bankruptcy)</div></div><div><div>•</div><div>3 - Not Released from Liability.</div></div></div> <div><div>Note:</div><div>This applies only to the Agency that acquired the property. Any remaining debt of the other Agency will not be written off with this transaction. It is the responsibility of each Agency to settle its own accounts after confirming that the acquisition was processed.</div></div>
21	Leave blank.
22	List the loan or recoverable cost items, if a separate loan number from the parent loan, to be credited in the order of lien priority. The first loan for each Agency entered must be the loan indicated as the most secured loan.

## **CHAPTER 3: ESCROW, TAXES, AND INSURANCE**

### **3.1 INTRODUCTION**

To protect the Agency's interest in the security property, the Servicing and Asset Management Office (Servicing Office) must ensure that real estate taxes and any other local assessments are paid and that the property remains adequately insured. To ensure that funds are available for these purposes, the Agency requires most borrowers who receive new loans to deposit funds to an escrow account. Borrowers who are not required to establish an escrow account may do so voluntarily. If an escrow account has been established, payments for insurance, taxes, and other assessments are made by the Agency. If an escrow account has not been established, the borrower is responsible for making timely payments.

Section 1 of this chapter describes basic requirements for paying taxes and maintaining insurance coverage; Section 2 provides procedure for establishing and maintaining the escrow account; and Section 3 discusses procedures for addressing insured and uninsured losses to the security property.

### **SECTION 1: TAX AND INSURANCE REQUIREMENTS [7 CFR 3550.60 and 3550.61]**

### **3.2 TAXES AND OTHER LOCAL ASSESSMENTS**

The Agency contracts with a tax service to secure tax information for all borrowers. The tax service obtains tax bills due for payment, determines the optimal time to pay the taxes in order to take advantage of any discounts, and provides delinquent tax status on the portfolio.

#### **A. Tax Service Fee**

All borrowers are charged a tax service fee. Borrowers who obtain a subsequent loan are not required to pay a second tax service fee. Refer to the tax service fee schedule shown in Attachment 3-B to determine the fee charged for new loans and new rates and terms assumptions.

**B. Borrowers Failure to Pay Taxes**

Borrowers not on escrow are responsible for paying their real estate taxes each year and submitting proof of payment to the Servicing Office. When the Agency is notified that a borrower has not paid real estate taxes on the property or other local assessments, the Servicing Office must notify the borrower that proof of payment must be submitted to the Servicing Office within 60 days. If the borrower fails to submit proof of payment, the Servicing Office taxes and any penalties and charge the cost as an advance to the borrower's account. The Servicing Office will not generally pay taxes and penalties in cases where there is another known lien holder, the security property also includes a farm, or net recovery is not anticipated unless it is determined to be in the best interest of the Agency. If the Agency advances funds to pay taxes or insurance, the borrower will be required to convert to escrow. When an escrow account is established, the advance will be repaid over the remaining term of the loan minus ten years. If the loan has less than 10 years remaining, the fee will be spread over 2 years or the remaining term, whichever is less.

**C. Recapture Receivable Accounts**

Delinquent tax notices/pending tax sale notices from taxing authorities on recapture receivable accounts should be forwarded to the Tax Unit at the Servicing Office for handling. The notices can be faxed to (314)457-4535. Upon receipt of a notice of pending tax sale, the Servicing Office will review the recapture receivable account to determine if it is in the best interest of the Agency to pay the taxes to avoid the tax sale and protect the Government's interest in the property. If the taxes are paid the Servicing Office will demand payment from the borrower. If payment is not made a foreclosure action will pursue.

**3.3 INSURANCE REQUIREMENTS**

Borrowers are responsible for obtaining and continuously maintaining insurance on the security property until the loan is paid in full. Evidence of insurance coverage for the first year of a loan must be provided at closing. In subsequent years, borrowers not on escrow are required

to pay insurance premiums and send proof of premium payment to the Servicing Office annually. For borrowers on escrow, the Servicing Office makes the premium payments.

**Insurance on Acquired Property**

Insurance will not be carried on properties that the Agency has acquired. After a foreclosure sale has been held or after a deed in lieu of foreclosure has been filed for record, insurance will not be canceled but will not be renewed. If the property becomes uninsured between the time when the borrower defaults on the loan and the time when the Agency obtains title, the Agency will force place insurance to protect its interests.

## Paragraph 3.3 Insurance Requirements

**A. Policy Requirements**

Borrowers must purchase policies from approved insurance companies. Attachment 3-A provides the minimum standards insurance policies must meet. When a loan is made, Field Staff are responsible for reviewing the applicant's proposed insurance coverage to determine whether it is adequate. The Servicing Office also reviews these policies for adequacy when closing documents are forwarded from the Field Office and approves any subsequent changes to borrower insurance policies. Borrowers may need to obtain three types of insurance.

**1. Hazard Insurance**

Most borrowers are required to maintain hazard insurance to protect the property against fire, wind, and weather-related damage. These policies may also be called "Fire and Extended Coverage," "Homeowner's," "All Physical Loss," or "Broad Form" policies.

Any borrower with a secured indebtedness in excess of \$15,000 at the time of loan approval must furnish and continually maintain hazard insurance on the security property, with companies, in amounts, and on terms and conditions acceptable to RHS and include a "loss payable clause" payable to RHS to protect the Government's interest."

For borrowers initially required to maintain hazard insurance, the Servicing Office may force place coverage for the benefit of the Agency and charge the cost to the borrower's account.

**2. Flood Insurance**

Flood insurance is required for all properties located in a Special Flood Hazard Area (SFHA), as identified by the Federal Emergency Management Agency (FEMA) and described in RD Instruction 426.2, except for loans and grants with an original principal balance of \$5,000 or less.



*FEMA's Standard Flood Hazard Determination* is used to document whether a property is in a SFHA and whether flood insurance is available under FEMA's National Flood Insurance Program. If the property is in a SFHA, the borrower should be notified using *Form RD 3550-6, Notice of Special Flood Hazards, Flood Insurance Purchase Requirements, and Availability of Federal Disaster Relief Assistance*. The borrower must sign and return the form. If the borrower in a SFHA cannot secure flood insurance through FEMA's National Flood Insurance Program, the property is not eligible for Federal financial assistance.



Dwellings located in the 100 year flood plain have additional requirements that must be met in regards to elevation levels, public utilities or on-site water supply and waste disposal systems requirements, and completion of the eight step decision making process for alternative consideration. (see RD Instruction 1970-F, section 1970.256 for further requirements).

### ***3. Builder's Risk Policies***

The borrower may elect to obtain a builder's risk policy that meets the Agency's requirements while the dwelling is under construction. An acceptable policy either: (1) names the borrower as the insured; or (2) contains a builder's risk endorsement for a policy issued to the borrower. A policy issued only to a contractor is not an acceptable substitute for the property insurance a borrower is required to provide.

The Servicing Office should ensure that the builder's risk policy automatically converts to full coverage when the dwelling is completed. Otherwise, acceptable insurance must be obtained to coincide with the expiration of the builder's risk provisions of the policy.

### **B. Acceptable Evidence of Insurance**

For loans secured by a first lien, the borrower must provide the original policy or declaration page. For loans secured by other than a first lien, a copy of the policy or declaration page, or other evidence of insurance, is acceptable. At loan closing the applicant may submit a written binder in lieu of the policy or declaration page, as long as the policy will be submitted to the Servicing Office within 60 days of closing.

### **C. Force Placed Insurance**

Force placed insurance is insurance coverage the Agency obtains for a security property when the borrower is unable or unwilling to provide adequate and acceptable insurance coverage. If the Agency force places insurance, the Servicing Office will make an advance to pay for the coverage and will inform the borrower of the new insurance. Borrowers must submit acceptable evidence of other insurance before the force placed insurance can be removed.

## **3.4 SERVICING ACTIONS RELATED TO INSURANCE**

### **A. Reviewing Policies for Acceptability**

After loan closing, Field Staff will send the borrower's policy to the Servicing Office along with other closing documents. The Servicing Office should review the policy to ensure that it meets the Agency's requirements as described in Attachment 3-A. If the policy is acceptable, the Servicing Office should image the policy and enter the policy information into LoanServ. If the borrower's policy is not acceptable, the Servicing Office should notify the borrower, explain why the policy is unacceptable, and request that the borrower submit an acceptable policy.

## Paragraph 3.4 Servicing Actions Related to Insurance

**B. Annual Payments**

For borrowers on escrow, the Servicing Office will pay annual insurance premiums from the escrow account. The borrower's insurance company must submit a renewal notice to the Servicing Office indicating the amount of the next year's insurance premium. SO must pay the required premium before the expiration date in order to prevent any lapse in insurance.

Borrowers not on escrow are responsible for paying insurance premiums and sending the Servicing Office evidence of payment and the declaration page. If the Servicing Office does not receive evidence of insurance coverage they will advise the borrower within 10 days after the policy's expiration date that the Agency will force place insurance if they fail to provide the necessary documentation within 60 days after the date of notification (45 days for flood insurance). Cost of the insurance will be charged to the borrower's account and the borrower will be required to escrow for taxes and insurance.

**C. Reviewing Changes in Insurance Coverage**

Borrowers who wish to change insurance policies must submit a replacement policy and evidence of payment to the Servicing Office at least 60 days before the current policy expires. If the replacement policy is received with less than 60 days notice and the Servicing Office has already disbursed a payment for the existing policy from the escrow account, the borrower is responsible for obtaining reimbursement of the paid premium.

The Servicing Office must review the replacement policy to ensure that it meets the Agency's requirements outlined in Attachment 3-A and may contact the applicable State Office to verify whether the insurance carrier is authorized to conduct business in the State. If the borrower's policy is not acceptable, the Servicing Office should inform the borrower of the reason (for example, there is not an adequate amount of coverage, it is not in the correct name, or the premium has not been paid) and request that the borrower submit an acceptable policy. If necessary, the Servicing Office will force place insurance.

**D. Cancellation of Insurance**

For borrowers on escrow, the borrower's insurance company must send to the Servicing Office any notice of cancellation or nonrenewal. Within 3 days of receiving the notification, the Servicing Office must notify the borrower of the need to get new insurance coverage before the existing policy expires.

The borrower must send an invoice to the Servicing Office for payment and should include a copy of the policy, if it is available. If the borrower does not submit a new hazard or flood policy and invoice within 10 days of the old policy's cancellation the Servicing Office will initiate action to force place insurance coverage on the property. If the borrower does not submit a new hazard or flood insurance policy and invoice within 70 days of the previous policy's expiration date (45 days for flood insurance), the Servicing Office will force place insurance.

If a borrower not on escrow receives a notice of cancellation or nonrenewal, the borrower must secure new insurance coverage before the current policy expires. The borrower must submit proof of insurance coverage and evidence of payment to the Servicing Office before the policy expires. Borrowers who cannot secure new insurance coverage should contact SO immediately. the Servicing Office will then force place insurance for the security property.

#### **E. Vacant or Leased Units**

If the Agency becomes aware that a security property is vacant or leased, the Servicing Office should review the policy to determine if it permits such conditions. If it does not, the Servicing Office should immediately notify the insurance carrier in writing. If the insurance carrier requires an additional premium because of the vacancy, tenant occupancy, or other increased hazard, the Servicing Office will pay the additional premium from the borrower's escrow account, if one exists. Borrowers not on escrow are responsible for paying the increased premiums. If the borrower is unable to pay the increased premium, the Agency may pay the additional premium and charge the cost to the borrower's account.

#### **F. Transfer of Property**

##### ***1. Assumptions***

In a transfer with assumption, insurance will be required in the same amount and according to the same provisions as for an initial loan of the same type. The new owner may obtain a new policy or have the current insurance company issue an endorsement to the current insurance policy, changing the name of the insured to that of the new owner.

##### ***2. Payment in Full***

When a borrower pays off the Agency's debt in full, the Agency releases its insurance interest in the security property. the Servicing Office should notify the insurance agency of record to remove the Agency's interests from the mortgagee or loss payable clause.

### ***3. Transfers Without Satisfying Agency Debt***

If the Agency becomes aware that the borrower has transferred title to the property without satisfying the Agency's debt, the Servicing Office should immediately notify the new owner that the mortgage requires the owner to provide and maintain adequate, acceptable insurance with the Agency listed as the mortgagee. In addition, the new owner should be informed that evidence of coverage and payment must be received by the Servicing Office within 30 days. If the evidence is not received in that time frame, the Servicing Office will force place insurance. The Agency will notify the borrower and new owner that acceptance of the new policy or endorsement will not constitute consent by the Government to the transfer.

HB-2-3550

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## SECTION 2: ESCROW REQUIREMENTS

### 3.5 OVERVIEW OF ESCROW REQUIREMENTS

#### A. Requirement to escrow

The Agency requires most borrowers who receive new loans to escrow funds for taxes and insurance.

Borrowers are exempt from escrow requirements if they:

- Are currently on an annual payment plan;
- Have a primary RHS loan with an existing escrow account;
- Have received only a Section 504 grant;
- Have Section 504 loans with a total outstanding balance of \$15,000 or less, and the Agency determines there is no risk to the Government's security interest in the property;
- Have a Section 504 loan and the Agency does not hold a mortgage interest in the property; or
- Assume a current loan (not past due) on same rates and terms; or
- Have security property which includes a farm and the property is not subdivided between farm and non-farm tract. In these cases, the Agency may still elect to require escrow where the housing represents the majority of the value of the security property or it is in the Agency's best interest to require escrow.



#### Escrow Statutes

The Agency administers escrow accounts in accordance with the Real Estate Settlement and Procedures Act of 1974 (RESPA) and section 501(e) of the Housing Act of 1949.

Existing borrowers who do not have escrow accounts may voluntarily establish an escrow account. Existing borrowers who pay on a monthly basis and annual-pay borrowers with monthly income must establish escrow accounts if:

- The borrower obtains a subsequent loan;
- The borrower requests a Delinquency Workout Agreement;
- The borrower's loan is reamortized as a servicing action; or
- Because of borrower failure to pay, the Agency must advance funds to pay for insurance, taxes, or other local assessments. The advance will be repaid over the remaining term of the loan minus ten years. If the loan has less than 10 years remaining, the fee will be spread over 2 years or the remaining term, whichever is less.

#### **B. Sources of Escrow Funding**

At the time the escrow account is established an initial deposit to the account is required. Once the escrow account is established, a portion of the borrower's monthly payment continues to fund the escrow account. Exhibit 3-1 illustrates the calculation of the initial deposit and monthly escrow payment.

### **3.6 ESTABLISHING ESCROW ACCOUNTS FOR NEW LOANS**

#### **A. Field Office Responsibilities**

No later than loan closing, the borrower must provide proof of insurance coverage. Field Staff will enter the borrower's estimated taxes and insurance premiums into UniFi, which automatically calculates the initial deposit and the monthly payment. The Closing Agent/Attorney collects escrow funds at closing and, in most cases, provides the funds to the the Servicing Office along with the closing documents. If real estate taxes are due within 60 days of the date of closing, the Closing Agent/Attorney will pay the real estate taxes and submit the remaining amount to the Servicing Office.

Exhibit 3-2 lists the closing documents related to taxes and insurance and provides processing instructions for each.

## Paragraph 3.6 Establishing Escrow Accounts for New Loans

**Exhibit 3-1****Escrow Account Funding**

The initial escrow balance and the escrow payment amount are calculated in accordance with RESPA. UniFi prepares *Form RD 3550-9, Initial Escrow Account Disclosure Statement* described in Paragraph 3.6 B.2. The following example is intended to show how escrow accounts are funded each year.

**Assumptions:**

- (1) The loan closing occurs on February 12, 1996 with the first payment due April 1, 1996.
- (2) Taxes of \$214.88 are paid in July and December.
- (3) Hazard insurance of \$319.00 is paid in January.
- (4) The Agency requires a cushion equal to 2 months of payments.

**Monthly Payment Calculation:**

\$214.88	
\$214.88	
<u>\$319.00</u>	
<u>\$748.76</u>	Total anticipated escrow disbursements divided by 12 equals
\$ 62.39	per month escrow payment

<u>Month</u>	<u>Payments to Escrow</u>	<u>Disbursements</u>	<u>Balance</u>
Loan Closing	\$249.64	\$ 0.00	\$249.64
April	\$ 62.39	\$ 0.00	\$312.03
May	\$ 62.39	\$ 0.00	\$374.42
June	\$ 62.39	\$ 0.00	\$436.81
July	\$ 62.39	\$214.88	\$284.32
August	\$ 62.39	\$ 0.00	\$346.71
September	\$ 62.39	\$ 0.00	\$409.10
October	\$ 62.39	\$ 0.00	\$471.49
November	\$ 62.39	\$ 0.00	\$533.88
December	\$ 62.39	\$214.88	\$381.39
January	\$ 62.39	\$319.00	\$124.78
February	\$ 62.39	\$ 0.00	\$187.17
March	\$ 62.39	\$ 0.00	\$249.56

The borrower will be required to pay \$62.39 per month and will also be required to fund the escrow account at closing in the amount of \$249.64. Part of the tax payment component of the initial escrow deposit will be contributed by the seller for the period from January 1st to the closing on February 12th.

According to RESPA, the lending institution at some time during the year must achieve an escrow balance that serves as a cushion but does not exceed 2 monthly escrow payments. In this example, the balance equal to 2 monthly payments (\$124.78), occurs in January after the payment for hazard insurance.

the Servicing Office is required to perform an escrow analysis within 12 months of the first payment and every year thereafter. The actual running escrow balance from the prior year will become the basis for projecting the necessary escrow payment for the next year. The low point achieved will be compared to the projected minimum of \$124.78. If the low point is below \$124.78, the loan will be deemed to have a shortage. If the low point is greater than \$50.00, the loan will have a surplus, which will be refunded to the borrower, if the surplus is less than \$50.00, it will be or credited to the next year's escrow.



**Exhibit 3-2****Closing Documents Related to Tax and Insurance**

- **Form RD 3550-19, Initial Escrow Account Disclosure Statement**, shows the amount of the initial escrow deposit.
- **Closing Disclosure.** The Servicing Office must verify that the real estate taxes have been properly pro rated between the buyer and seller by reviewing the Closing Disclosure.
- **Tax information.** The Servicing Office must enter into LoanServ the information on taxing authorities, parcel number, due dates, and tax information from *Form RD 3550-15 Tax Information*.
- **Title insurance policy.** The Servicing Office must verify that the legal description of the property is consistent with the closing documents.
- **Insurance documentation.** The Servicing Office must review the insurance documentation (either a policy, declaration page, or binder) and enter into LoanServ information such as the cost, coverage period, coverage amount, company, and beneficiaries.

**B.**  
**The**

**Servicing Office Responsibilities**

After reviewing the information sent by the Field Staff, the Servicing Office deposits the escrow funds and verifies the information on *Form RD 3550-15*.

**1. Notification to Tax Service**

Within 30 days of establishing the escrow account, the Servicing Office should send the completed tax worksheet to the tax service, along with the loan identification number, the parcel number, a legal description of the borrower's property, and the tax service fee. The tax service will set up the borrower's information in its system and generate a unique tax service contract number. The tax service will then send the borrower's contract number to the Servicing Office. This number will be entered into LoanServ to help identify the borrower's account.

**2. Initial Escrow Account Disclosure Statement**

The field office is responsible for completing the *Form RD 3550-9* "Initial Escrow Account Disclosure Statement". The statement will be initialed by the borrower at closing and the borrower will be provided a copy of the statement. The signed statement will be forwarded to the Servicing Office with the closing documents.

## Paragraph 3.6 Establishing Escrow Accounts for New Loans

The initial disclosure statement should include the amount of the borrower's monthly mortgage payment and the portion of the payment going into the escrow account. It should itemize the estimated taxes and insurance premiums to be paid from the account during the upcoming year. It also should show the cushion and a trial running balance for the account. (A trial running balance is a projected escrow balance for each month during the computation year.)

### ***3. Construction Loans***

When a borrower receives a construction loan, an escrow account is not established until after construction is complete. In addition, since loan payments are deferred during the construction period, monthly escrow payments are not paid. Two options are provided to loan applicants to handle taxes and insurance. One option is to include in the loan amount, subject to loan underwriting requirements, taxes which come due during construction and the amount to fund the initial escrow deposit. The other option is for the borrower to use personal funds to pay taxes when due and for the initial escrow deposit to be paid by the borrower in a lump sum when the construction loan is converted to a permanent loan. If the borrower does not pay tax bills or insurance bills which become due during construction or there are insufficient funds to establish the escrow account when the loan is converted, the Field Office will cue the Servicing Office and provide the estimated amount of the shortage, and the facts in the case. The Servicing Office will generally increase the monthly payment scheduled for the remainder of the escrow cycle to compensate for the shortage. The Servicing Office may also elect to charge the borrower's account for any shortage and reamortize the loan.

Borrowers must be counseled that they are ultimately responsible for payment of insurance premiums and while the costs may be included in the loan, the borrower is responsible to cover any shortage which may occur.

If construction is completed as planned, the course of construction (Builder's Risk) policy should remain in effect without an additional premium due during construction. However, if a second premium is due during construction, the borrower is responsible for this payment. Within 30 days of the anticipated construction completion date, the borrower will provide the Field Office with a copy of the binder for a hazard insurance policy and a receipt showing it has been paid in full for one year, OR a request for a draw from the construction loan to pay one year's hazard insurance premium in full, as applicable.

### **3.7 ESTABLISHING ESCROW ACCOUNTS FOR EXISTING LOANS**

#### **A. Determining the Escrow Amount**

To establish an escrow account for a borrower with an existing loan, the Servicing Office must gather the information discussed in the following paragraphs.

##### ***1. Insurance Information***

Current information on insurance coverage should be available in the Servicing Office records. If current information is not available, the Servicing Office should contact the borrower at least 30 days prior to establishing an escrow account, notifying them that they must provide proof of insurance coverage.

When the policy information is received, the Servicing Office must review it to ensure that it meets the Agency's requirements, as described in Attachment 3-A, and enter information about the insurance into LoanServ. If the borrower cannot or will not obtain insurance coverage, the Servicing Office will force place insurance.

##### ***2. Tax Information***

The Servicing Office will confirm with the borrower the taxing authorities to which taxes are due, the amount of taxes paid by the borrower last year, and the due dates. the Servicing Office will verify this information, enter it into LoanServ, and establish an escrow account.

Once the necessary information is entered into LoanServ, the escrow analysis unit will calculate the escrow amount (both the initial deposit and the monthly amount). The Servicing Office should change the tax service code in LoanServ to reflect that the borrower is now on escrow and within 30 days of setting up the escrow account, inform the tax service that the borrower has been converted to escrow. The tax service will then be changed to escrow.

#### **B. Obtain Funds for the Escrow Account**

Once the escrow account is set up, the Servicing Office must deposit the specified escrow funds into the borrower's escrow account. If the escrow account contains insufficient funds to pay the insurance and taxes when due, the Servicing Office will advance an amount equal to the difference between the amount due and the escrow balance. At the time of the annual escrow analysis, any negative balances or shortage will be spread over 12 months and collected with the escrow portion of the borrower's mortgage payments.

#### **C. Notify the Borrower**

Once the escrow account has been established, the Servicing Office must send written notification to the borrower which includes an explanation of the establishment and function of the escrow account and *Form RD 3550-9*. See Paragraph 3.6 B.2 for a description of this document. The disclosure statement must be sent within 45 days after creating the escrow account.

### 3.8 ESCROW PAYMENTS

The Servicing Office will disburse funds as necessary to pay tax and insurance bills, as well as other appropriate expenses. The Servicing Office will be responsible for ensuring that all escrow payments are made at the optimal time to take advantage of any discounts and avoid penalties.



#### Termination of Escrow Payments

Escrow disbursements will stop immediately upon debt settlement or release of security.

### 3.9 ANNUAL ESCROW ANALYSIS

RESPA requires the Servicing Office to conduct an annual escrow account analysis for each borrower that has an escrow account. RESPA also requires the Servicing Office to provide borrowers with an Annual Escrow Disclosure Statement that shows the account history and projects activity for the coming year. A borrower's monthly payment to the escrow account may increase or decrease as a result of the analysis. The Servicing Office must mail the disclosure statement at least 30 days prior to the new payment effective date.

#### A. Surpluses

Surpluses arise when the account balance does not reach the expected low point of two monthly escrow payments during the year. When a surplus for an escrow account is greater than or equal to \$50 and the borrower is current on the loan, the Servicing Office will generate a check and return the surplus to the borrower with the Annual Escrow Disclosure Statement.

#### B. Shortages

Shortages arise when the escrow balance is less than the expected low point during the year. Generally, the Servicing Office can recover shortages by adjusting the monthly payment to the escrow account and spreading the amount equally over the next 12-month period. If the borrower cannot make the resulting required payment, the Servicing Office may spread it out over a longer period. If a risk analysis reveals that the borrower is unlikely to be able to repay the amount, the Servicing Office may require payment within 30 days. The Servicing Office should consider special servicing options if the borrower is unable to repay the amount within 30 days.

### **C. Account History**

In general, the account history should include a description of the borrower's monthly mortgage payment and the portion going into the escrow account, the total amounts paid into and disbursed from the account, an explanation of how any surpluses or shortages will be handled, and the balance of the escrow account at the end of the year. Any differences in actual disbursements from amounts previously projected should be marked with an asterisk.



#### **Accelerated Accounts**

If a borrower's account is currently accelerated, the Servicing Office does not provide a disclosure statement.

### **D. Projection**

The Servicing Office should base its projection on last year's disbursement amount unless last year's statement includes items that are not paid annually such as flood insurance that is due every 3 years or quarterly tax assessments.

A projection statement should cover 12 months unless the loan will mature within the next 12 months. In this case, the projection need only cover the months through the maturity date.

## **3.10 DISCLOSURE STATEMENTS FOR PROPERTY TRANSFERS AND PAYOFFS**

### **A. Loan Assumptions**

Loan assumptions require the preparation of a statement for both the buyer and the seller.

#### ***1. Disclosure to the New Borrower***

For assumptions on the same rates and terms, the Servicing Office should provide the new borrower with *Form RD 3550-9* within 45 days of completing the name change on LoanServ. The disclosure for new purchasers who assume a loan on new rates and terms is handled the same as for any new loan as described in Paragraph 3.6 B.2.

#### ***2. Disclosure to the Previous Owner***

For either kind of assumption, a disclosure statement covering the period from the last disclosure until property transfer must be sent to the prior borrower within 60 days of completing the assumption.

### **B. Loans Paid in Full**

A disclosure statement that shows the account history from the date of the last disclosure to the date of payoff must be sent to a borrower who pays a loan in full.

## **SECTION 3: LOSSES [7 CFR 3550.61(d)]**

### **3.11 OVERVIEW**

When the Servicing Office learns of a loss to a security property, the actions to be taken depend upon whether the property is insured, whether the Agency is named as the mortgagee in the insurance policy, and the lien position of the Agency's loan. This section provides servicing instructions for dealing with both insured and uninsured losses.

#### **A. Reporting the Loss**

The borrower is responsible for immediately notifying the Servicing Office of any loss or damage to the security property and for collecting covered losses from the insurance company. The Servicing Office may ask the Field Office to inspect the property to verify that the borrower has taken the necessary steps to protect the property against further damage. If the borrower is unable to arrange for adequate protection, the Field Staff may recommend to the Servicing Office that a protective advance be used to arrange for emergency protection.

#### **B. Losses on Properties with Accelerated Loans**

Losses on properties in the process of foreclosure or deed in lieu of foreclosure will be handled in accordance with advice from the Office of the General Counsel (OGC). All loss payments should be applied to the borrower's real estate indebtedness before title to the property is taken by the Government, unless absolute assignment has been made by the borrower to the Government of all loss funds due from the insurance company.

If a borrower has improperly disposed of loss proceeds, the Servicing Office's escrow branch should consult with its risk management branch and OGC to determine what further action should be taken.

#### **C. Agency Subrogation of Its Rights**

Whenever a borrower willfully destroys a security property, the insurance company is not liable to the borrower but is still liable to the Agency (as the mortgagee). In such circumstances, the insurance company may ask the Agency to subrogate and assign some of its legal rights in the property to the insurance company. The Servicing Office will consult with OGC to determine whether subrogation is appropriate.

### **3.12 FILING THE INSURANCE CLAIM**

The borrower is responsible for submitting a claim to the insurance company. The insurance company will send an adjuster to evaluate the borrower's loss, establish the work to be completed, and develop an estimated cost to complete the work (by individual work item). To document the information, the adjuster will complete an adjuster's worksheet.

The borrower must negotiate the adjustment of the loss with the insurance company. The borrower may consult with the Agency, but the Agency will not enter into the negotiations with the insurance adjusters, make commitments, or sign any forms in connection with the adjustment. The Agency will not waive any rights that it may have against the company, except when the borrower's claim has been settled.

If, after the borrower has settled the claim, the Servicing Office determines that the adjustment agreed to by the borrower is significantly less than the amount to which the borrower is entitled under the terms of the policy, the Agency may consider reopening negotiations with the insurance company.

### **3.13 ADMINISTERING INSURANCE PROCEEDS**

The mortgagee or loss payable clause of borrower insurance policies ensures that the Agency's interest is protected. Checks for insurance proceeds (also called "loss drafts") are made payable jointly to the borrower and the Agency. Other lien holders also may be parties to the loss draft.

Borrowers with insurance claims must contact the Servicing Office to establish a plan to repair or rehabilitate the security property. If the insurance claim proceeds will not be used to redevelop the security property, the amount received must be applied to the account. Depending upon the amount of the loss, the Agency may require that the expenditure of insurance payments be supervised by a local Field Office. It is important that the Servicing Office and the Field Office work together to assure that any repairs are completed to protect the government's interest. The amount of Field Office involvement is dependent upon the amount of the insurance claim and the risk to the government.

#### **A. Loans Secured by a First Lien**

Once insurance proceeds are received, the borrower should endorse the loss draft and send it, along with the adjuster's worksheet, to the Servicing Office. The Servicing Office generally places the funds into a managed escrow account. However, when the amount of the loss claim is \$7,500 or less and the borrower's account is current, Field Offices are authorized to endorse the insurance claim check without recourse provided the borrower submits the adjuster's worksheet along with

## Paragraph 3.13 Administering Insurance Proceeds

documentation that the repairs will be made or have been completed. **Note:** Field offices should first review the adjuster's worksheet to ensure that the check is the total claim disbursement. If it is a partial disbursement, the check should be forwarded to the Servicing Office and not endorsed in the field.

For significant rehabilitation (having a total cost of more than \$30,000) all development will be completed under the supervision of the local Field Office. The insurance proceeds may be provided to the Field Office to establish a supervised bank account or retained for disbursement at the Servicing Office. Development will be managed by the Field Office in a like manner as development funded by loan proceeds. This could include *Form RD 1924-2, Description of Materials*, and *Form RD 1924-25, Plan Certification* or a building permit issued by the local jurisdiction. As noted in Paragraph 3.14, all repairs and replacements will be planned, performed, inspected, and paid for in accordance with RD Instruction 1924-A. Payment schedules will be established in the individual repair plan.

Written contracts, using *Form RD 1924-6, Construction Contract* are strongly recommended for all rehabilitation-related construction, and are required if there is construction involved that would affect the dwelling's structural integrity. Otherwise, a *Form RD-1924-1, Development Plan* or similar form, with cost estimates and specifications may be used. Unless the borrower method is used, funds will not be advanced for materials or other purposes until work is completed.

In summary, there are three different ways development with insurance claim proceeds is managed by the Servicing Office and Field Staff, depending on the amount and risk involved. Exhibit 3-3 presents a matrix summarizing these procedures.

- **Total claim of \$7,500 or less and the borrower's account is current:** Field Staff endorses the check to the borrower after reviewing the adjuster's worksheet;
- **Total claim exceeding \$7,500 but less than \$30,000, or claims of \$7,500 or less and the borrower's account is not current:** Field Staff forwards insurance proceeds to the Servicing Office's insurance escrow, and inspects the work as requested by the Servicing Office;
- **Total claim of more than \$30,000:** Field Staff establishes a supervised bank account or forwards insurance proceeds to the Servicing Office's escrow, and manages all steps of construction planning and performance in a like manner as development funded by loan proceeds.



<b>Exhibit 3-3</b>  <b>Administration of Insurance Proceeds when Redevelopment Work is to be Performed</b>			
<b>Total Claims</b>	<b>Account Status</b>	<b>Rehab Components</b>	<b>Insurance Claims Administration Procedure</b>
\$7,500 or less	Current	Not considered	Field Staff endorses check to borrower after reviewing the adjuster's worksheet.
\$7,500 or less	Not current	Not considered	Field Staff forwards insurance proceeds to the Servicing Office's insurance escrow, and inspects the work as requested by the Servicing Office.
More than \$7,500 but less than \$30,000	All accounts regardless of status	Single component	Field Staff establishes a supervised bank account or forwards insurance proceeds to the Servicing Office's escrow, and manages all steps of construction planning and performance in a like manner as development funded by loan proceeds. Work is inspected prior to any disbursements.
More than \$7,500 but less than \$30,000	All accounts regardless of status	More than one component	
More than \$30,000	All accounts regardless of status	All rehab work	

For construction contracts exceeding \$10,000, Department of Labor requirements also apply. Refer to RD Instruction 1924-A.

**B. Loans Secured by Other Than a First Lien**

If the loss draft does not include the interest of the prior mortgagee or if all other payees have endorsed the draft, the Servicing Office administers the claim as described above for loans secured by a first lien.

When the loss draft includes the interest of the prior mortgagee, oversight of repairs of any supervised account may be conducted by the prior mortgagee.

***1. When Proceeds Will Be Used to Repair or Replace the Property***

The Servicing Office should endorse the loss draft without recourse once the prior mortgagee has agreed to the use of the loss funds to repair or replace the damaged property and the borrower has provided satisfactory proof that the repairs have been made or satisfactory assurance that the work will be performed. Satisfactory assurance includes a signed construction contract, a final inspection report, or a contractor's release of liens.

If funds remain after the repairs are complete and the prior lien holder has agreed in writing that it will apply the funds as a payment on the borrower's prior lien indebtedness, the loss draft should be endorsed without recourse.

***2. When Proceeds Will be Used to Reduce Debt on the Property***

When the amount of the loss draft is less than the amount of the indebtedness secured by the prior lien and the holder of the prior lien has agreed in writing that it will apply such funds as a payment on the borrower's prior lien indebtedness, the Servicing Office may endorse the loss draft without recourse.

When the amount of the loss draft exceeds the amount of the indebtedness secured by the prior lien and the borrower has agreed in writing to pay such indebtedness from the loss funds, the loss draft should be endorsed without recourse only after all parties named as payees in the draft have signed an agreement to deliver the draft "in escrow" to a bank acceptable to the named parties. The agreement will specify the manner in which the funds will be disbursed by the escrow agent to the mortgagees named in the draft.

**C. If the Agency is Not Listed as a Mortgagee**

The Agency must always be listed in the mortgagee or loss payable clause. However, if through some oversight the Agency is not listed as mortgagee, the Servicing Office must contact the borrower to

determine if loss proceeds have been received. If the borrower has not yet received the funds, the Servicing Office should contact the insurance carrier to request that the loss proceeds be made payable jointly to the Agency and the borrower.

If the borrower already has received the proceeds but has not yet paid for repairs, the Servicing Office should notify the borrower that the loss proceeds must be used for repairs or other uses as required by the Agency. If the borrower fails to make required repairs, the account should be accelerated as soon as practical if the Government's security interest is threatened.

#### **D. When the Agency has No Claim on Insurance Proceeds**

If the indebtedness secured by the insured property has been paid in full, or the draft is in payment for a loss of property on which the Agency has no claim, any loss draft which includes the Agency as a payee may be endorsed and released without recourse and delivered to the borrower.

### **3.14 INSPECTING REPAIRS AND AUTHORIZING PAYMENTS**

All repairs and replacements will be planned, performed, inspected, and paid for in accordance with RD Instruction 1924-A. Payment schedules will be established in the individual repair plan and the construction contract.



#### **A. Progress Inspections and Payments**

When the loss claim is under the purview of the Servicing Office, Servicing Office should request that the Field Office inspect the repair work and complete *Form RD 1924-12, Inspection Report*. Before each inspection related to a progress payment, Field Staff should request a check from the Servicing Office. The check should be made payable to the borrower and the contractor. If work has been satisfactorily completed, Field Staff will instruct the borrower to endorse the check and give it to the contractor. If the inspection reveals that the work was not completed satisfactorily, Field Staff will void the check and return it to the Servicing Office. After each periodic inspection, Field Staff will send the inspection report to the Servicing Office and maintain a copy in the borrower's case file. Field Staff will follow up on the adjustment of all losses until satisfactory settlement has been made.

#### **B. Final Payment**

When all work has been satisfactorily completed, Field Staff will release the final check to the borrower and submit to the Servicing Office all documents completed as required in RD Instruction 1924-A, including: a final *Form RD 1924-12, Inspection Report*; *Form RD 1924-9, Certificate of Contractor's Release*; *Form RD 1924-10, Release By Claimants*; and *Form RD 1924-19, Builder's Warranty*.

### **3.15 POST REPAIR ACTIVITIES**

#### **A. If Insurance Funds Remain**

If insurance funds remain after all repairs, replacements, or other authorized corrections have been made, the funds will be applied in the following order of priority:

- Prior liens, including delinquent property taxes;
- Any delinquency on the account; and
- Advances for recoverable cost items.

If funds still remain after being applied in the above order and the Agency's debt is adequately secured, the Servicing Office should release the funds to the borrower.

#### **B. Reinstatement After Loss**

In cases where insurance in the amount of the loss is not reinstated automatically under the provisions of the policy, the Agency should ensure that the borrower reinstates the full amount of the coverage required by the Agency.

### **3.16 PRESIDENTIAL DECLARED DISASTERS**

After a presidential declared major disaster, borrowers may need quick access to all or a portion of the insurance proceeds.

#### **A. Repairs That Will Be Completed Within 30 Days**

If the insurance proceeds are \$10,000 or less and the repairs can be completed within 30 days, the Agency may endorse the entire check and the proceeds can be released to the borrower for repairs to the property. Before this is done, the borrower must provide a copy of the contractor's estimate of the repair costs.

If the insurance proceeds are more than \$10,000 and the repairs can be completed within 30 days, the Agency may release \$20,000 to the borrower for the repairs. The borrower must provide a copy of the contractor's estimate of the cost of repairs. The Agency will retain the balance of the proceeds for disbursement according to the borrower's individual plan.

## **B. Repairs That Require More than 30 Days to Complete**

If the repairs cannot be completed within 30 days and the insurance proceeds exceed the outstanding debt against the property, the Servicing Office may release to the borrower an amount equal to the difference between the amount of the insurance proceeds and the debt against the property. The Agency will retain the balance of the proceeds for disbursement according to the borrower's individual plan.

### **3.17 LOSSES NOT COVERED BY INSURANCE**

If a loss occurs while insurance is not in force, the Servicing Office should notify the borrower that failure to maintain insurance is a violation of the security agreement and instruct the borrower to make the needed repairs or replacements.

If the borrower is unable or unwilling to make needed repairs or replacements, the Servicer will prepare a problem case report and make recommendations on the following items:

- The advisability and possibility of making a subsequent loan to pay for needed repairs;
- Subordination of the Agency's real estate lien to permit the borrower to obtain funds from another source for needed repairs;
- The possibility of the borrower obtaining funds secured by a junior lien from another lender; and
- Whether a protective advance is necessary to protect the Government's interest.

When preparing the report, the Servicing Office Servicer should consider such factors as the borrower's previous repayment history, the amount of the loss, the nature of the repairs, and the threat to the Agency's security interest.

Recommendations to accelerate the loan should be processed in accordance with Chapter 6.

## ATTACHMENT 3-A

### INSURANCE POLICY REQUIREMENTS

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#### A. Authorized Insurance Providers

Borrowers must purchase their policies from approved insurance companies licensed to do business in the State where the property is located. If the required insurance is not available at comparable rates from a State-licensed insurance company, insurance from another company may be accepted if:

- The Office of the General Counsel (OGC) confirms that policies issued by the company are enforceable despite the fact that the company is not licensed to conduct business in the State, and the company is a legal entity that may be sued in the State where the property is located; and
- The State Director determines that the company is reputable and financially sound based on the company's financial statements, industry rating standards, or information available from the State insurance authority or other lending institutions.

The Servicing Office Servicers may contact the applicable State Office to verify whether the insurance carrier is authorized to do business in the state.

#### B. Loss or Damage Covered

Hazard insurance policies must insure buildings against loss or damage by fire, lightning, windstorm, hail, explosion, riot, civil commotion, aircraft, vehicles, and smoke. The flood insurance, if applicable, must cover any damage due to water or flooding conditions.

#### C. Amount

The borrower is required to insure the dwelling and any other essential buildings in an amount equal to the insurable values of the dwelling and other essential buildings. However, in cases where the borrower's outstanding secured indebtedness is less than the insurable value of the dwelling and other essential buildings, the borrower may elect a lower coverage provided it is not less than the outstanding secured indebtedness. If the borrower fails, or is unable to insure the secured property, RHS will force place insurance. The amount of the lender-placed coverage will generally be the last known insured value.

The policy must state whether or not the building is on a leasehold. State Supplements provide guidance on specific State insurance requirements pertaining to leasehold interests. The Servicing Office Servicers may contact the applicable State Office for further guidance.

#### **D. Borrower's Deductible**

The borrower's deductible must not exceed the generally accepted minimum based on the current industry standards and local market conditions. For flood insurance these deductibles apply unless the insurance carrier requires a higher amount.

#### **E. Term**

The policy must have a term of at least 1 year, with evidence that 1 year's premium has been paid.

#### **F. Effective Date**

If there are insurable buildings on the property (as opposed to vacant land to be built upon), the policy must be in force at the time the loan is closed. When a dwelling is to be constructed, the insurance coverage must be effective as of the date the materials are delivered to the property. No payments from loan funds for labor or materials can be made unless insurance coverage is in place.

#### **G. Construction Specifications and Use Conditions**

If the insurance policy specifies certain standards of construction or prescribes certain uses of the property, the policy will be acceptable only if the property meets the specifications or conditions.

#### **H. Names and Location**

The policy must include the legal names of all parties being insured. It also must contain a description of the property's location, although a legal metes and bounds description is not required.

#### **I. Mortgagee Clause**

A mortgagee clause ensures that the Agency will be reimbursed in the event of a loss by identifying the Agency as the secured party on the lien (the "mortgagee"). The standard mortgagee clause adopted by the State must be attached to or printed in the policy. It also must identify the Agency as the mortgagee. Specifically, the Agency must be identified as the "United

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States of America, acting through the Rural Housing Service or its successor agency.” The Agency, and all other mortgagees whose interests are insured under the policy, must be shown in either the mortgagee clause or on the declaration page in the order of priority of their mortgages. The address should be:

USDA, Rural Development  
Servicing Office Attn: Insurance Department  
P.O. Box 66876  
St. Louis, Missouri 63166

Whenever a new mortgagee clause is issued after the policy has been in force, the new mortgagee clause must be signed by an authorized agent or officer of the company that issued the policy.

When an approved mortgagee clause is not printed in the policy, a “loss payable clause” which lists all the parties that would receive payment in case of a loss is acceptable, provided the Agency will receive payment in case of loss, even in circumstances in which the company would not be liable to the borrower. The closing agent must verify that an authorized official of the insurance company has sent a signed letter to the State Director stating that all insurance policies issued by the company in the State incorporate all the provisions of the standard mortgagee clause and that the Agency is named in the loss payable clause (a State Supplement will be issued offering guidance on the requirements of this letter).

#### **Master Policies**

A master policy is one containing substantially the same standard provisions adopted or recommended by legislative action or by order of the State’s insurance authority. A master policy is required, unless State statutes exempt the company from the regulations requiring its use.

If a State has adopted a master policy, the State Director will submit a copy to the Servicing Office. The Servicing Office will compare individual policies to the master policy to determine whether they are sufficient to protect the Agency’s interest.



ATTACHMENT 3-B

TAX SERVICE FEE SCHEDULE

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The tax service fee will be charged according to the timetable listed below:

Tax Service Fee:	New Rates and Terms Assumptions *	\$10
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New Loans Approved	September 30, 2024 to September 29, 2025	\$82
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➤	09-30-2025 to 09-29-2026	\$84.05
➤	09-30-2026 to 09-29-2027	\$86.15
➤	09-30-2027 to 09-29-2028	\$88.31

(This fee remains in effect until further notice)

\* The charge for Tax Service on a New Rates & Terms assumption will remain \$10 unless otherwise notified.

## **CHAPTER 4: PAYMENT SUBSIDIES AND INCOME DETERMINATIONS**

### **4.1 INTRODUCTION**

The Agency uses payment subsidies to enhance borrower repayment ability for Section 502 loans. Many borrowers receive a payment subsidy at the time the loan is initially made and continue to receive it throughout the life of the loan. When a borrower begins to receive payment subsidy at the time the loan is made, the initial determination of the amount of payment subsidy for which the borrower qualifies is determined by the Field Office.

The Servicing and Asset Management Office (Servicing Office) is responsible for initiating payment subsidies for qualified borrowers not currently receiving payment subsidies and periodic reviews of borrowers already receiving payment subsidies.

Section 1 of this chapter describes policies and procedures related to the approval and renewal of payment subsidies. Section 2 provides detailed guidance on calculating annual and adjusted income, which are used to calculate the payment subsidies.

### **SECTION 1: PAYMENT SUBSIDIES [7 CFR 3550.68]**

### **4.2 OVERVIEW OF PAYMENT SUBSIDIES**

Payment subsidies are available only for Section 502 loans. The amount of subsidy is based upon the borrower's income. LoanServ calculates the borrower's payment subsidy. The sample calculations provided in this section are intended to help the Servicer understand how the calculation works so that the Servicer can explain the calculations to borrowers.

#### **A. Three Types of Subsidy**

##### ***1. Interest Credit***

A borrower who initially received subsidy in the form of interest credit can continue to do so as long as the borrower remains eligible and continuously receives interest credit

assistance. If the interest credit agreement expires but the borrower was continuously eligible for subsidy the borrower may continue to receive interest credit assistance provided the agreement is renewed within 6 months from the expiration date.

## ***2. Payment Assistance Method 1***

If a borrower receiving payment assistance under payment assistance method 1 receives a subsequent loan, payment assistance method 2 will be used to calculate the subsidy for the initial loan and subsequent loan.

## ***3. Payment Assistance Method 2***

All other eligible borrowers will receive payment assistance method 2. This includes: borrowers who receive new initial loans; borrowers obtaining subsequent loans who qualify for payment subsidy, but who are not currently receiving interest credit or payment assistance method 1; and borrowers who assume loans under new rates and terms. Borrowers who cease to receive interest credit or payment assistance method 1 for 6 months or more will receive payment assistance method 2 if they subsequently begin to receive payment subsidies. See Paragraph 4.3 B for calculating Payment Assistance Method 2.

# **B. Borrower Eligibility**

## ***1. Income Eligibility***

Borrowers who obtain loans on nonprogram terms are not eligible for payment subsidies. To be eligible at the time of origination, a borrower must be income-eligible for a Section 502 loan -- that is, have adjusted income that does not exceed the applicable low-income limit at the time of loan approval and the applicable moderate-income limit at the time of loan closing.

To be eligible during the term of the loan, a borrower not already on payment subsidy must have adjusted income at or below the applicable low-income limit. Once a borrower begins to receive a payment subsidy, the borrower may continue to do so until the applicable formula no longer provides such assistance.

## ***2. Occupancy Requirement***

A borrower who is receiving payment subsidy must personally occupy the dwelling during the term of the loan; the borrower may be temporarily absent from the property for a period of 6 months with a reason acceptable to the Agency, such as seasonal or migratory employment, military call ups, or hospitalization. In the case of a deceased

## Paragraph 4.2 Overview of Payment Subsidies

borrower, subsidy may continue for six months or until assumption of the loan is completed, whichever occurs sooner. The subsidy must be based upon income of the current occupants.

**3. *Nonprogram, Above-Moderate and Pre-August 1, 1968, Borrowers***

Payment subsidies cannot be provided in conjunction with loans made before August 1, 1968, or with loans made on above-moderate or nonprogram terms. Some of these borrowers may be eligible to refinance the loan in order to receive payment assistance, as described in Paragraph 5.3 A.

**C. Loan Requirements**

For borrowers to be eligible for payment subsidies, initial loans and subsequent loans made in conjunction with a new rates and terms assumption must have a term of at least 25 years. Borrowers are eligible to receive payment subsidies for subsequent loans with less than a 25 year term that are *not* made in conjunction with an assumption only if the borrower's initial loan had an initial term of at least 25 years.

**D. Borrower Reporting Requirements**

Each year borrowers receiving payment subsidies are required to report on household income, expenses, and composition. This enables the Servicer to determine whether the borrower should continue to receive a subsidy and the amount of subsidy to be provided.

Borrowers who receive payment subsidies must notify the Agency whenever an adult member of the household changes or obtains employment, the household composition changes, or if income increases by more than 10 percent. A borrower whose income decreases may report the change and ask the Servicer to determine whether the decrease entitles the borrower to additional payment subsidies.

The Servicer may establish an alternative review period to accommodate specific circumstances including the three circumstances described below.

**1. *Self-Employed Borrowers***

For a self-employed borrower, the initial payment assistance agreement should run from the effective date of the income determination to 3 months after the end of the

borrower's business fiscal year. This will allow subsequent agreements to coincide with the borrower's business fiscal year, with a 3-month overlap to provide sufficient time for the borrower to supply verification of the previous year's income. However, the review period may not exceed 12 months.

## **2. *Unemployed Borrowers***

For a borrower or adult household member receiving unemployment benefits, the benefit amount will be considered in the income calculation. Unemployment benefits will be calculated to project annual income regardless of the remaining eligibility of unemployment benefits. The term of the agreement will be no longer than 6 months.

## **3. *Annual Payment Borrowers***

For a borrower currently paying an annual installment who receives a subsequent loan, the initial payment assistance agreement, including assistance for the subsequent loan, will remain in effect until the next January 1st.

## **E. Recapture Requirement**

Once the principal and interest on a loan is paid in full, subsidy recapture must be repaid whenever the borrower ceases to occupy the property or transfers title. If the property is temporarily unoccupied for reasons that are acceptable to the Agency recapture is not triggered. Whenever the borrower qualifies for payment subsidy for the first time, the borrower must sign *Form RD 3550-12*. See Section 5 of Chapter 2 for a full discussion of the recapture requirements.

## **4.3 CALCULATING PAYMENT ASSISTANCE**

There are two (2) methods of payment assistance. They are payment assistance method 1 and payment assistance method 2. Payment assistance is calculated as follows:

### **A. Payment Assistance Method 1**

The amount of payment assistance is the difference between the installment due at the promissory note rate and the amount the borrower must pay, based upon income. Borrowers receiving payment assistance method 1 must pay the ***greater of:***

## Paragraph 4.3 Calculating Payment Assistance

- The loan payment amortized at the equivalent interest rate (EIR) applicable to the borrower; or
- Except for leveraged loans, a floor payment calculated as a percentage of adjusted income, less the cost of taxes and insurance.

Exhibit 4-1 provides an example of this calculation

**Exhibit 4-1**  
**Sample Payment Assistance Method 1 Calculation**  
(These calculations are done by LoanServ)

**The Jones family has been approved for a loan with a principal amount of \$60,000.**

The following financial information is needed to calculate the payment assistance:

**Loan term:** 33 years                      **Note rate:** 7%                      **Median income:** \$30,000

\$19,000 Adjusted income  
\$90                      Monthly taxes and insurance  
64%                      Percent of applicable median ( $\$19,000 \div \$30,000$ )

**(1) Calculate the Payment at the Note Rate**

\$389                      Payment at the note rate:  
(Amortized amount for \$60,000 @ 7% for 33 years)

**(2) Calculate the Floor Payment for PI\***

24%                      Floor payment percentage for borrower @ 64% of median income  
380                      Floor payment for PITI\* ( $\$19,000 \div 12 \text{ months} \times 0.24$ )  
\$290                      Floor payment for PI (\$380 - \$90 for taxes and insurance)

**(3) Calculate the Payment at the EIR\***

4%                      EIR for borrower at 64% of median  
\$273                      Payment at the EIR (amortized amount for \$60,000 @ 4% for 33 years)

**(4) Compute Monthly Payment Assistance**

\$389                      Payment at the note rate  
-\$290                      Required payment is the greater of (2) or (3)  
\$ 99                      Monthly payment assistance  
                              \*PI        ~        Principal and interest  
                              PITI       ~        Principal, interest, taxes, and insurance  
                              EIR        ~        Equivalent Interest Rate

## Paragraph 4.3 Calculating Payment Assistance

**1. Calculating the Payment at the Equivalent Interest Rate**

This payment uses the borrower's loan amount, the term of the loan, and an equivalent interest rate for which the borrower qualifies based upon income. Exhibit 4-2 provides the equivalent interest rates to be used.

<b>Exhibit 4-2</b>	
<b>Equivalent Interest Rates</b>	
Use the equivalent interest rate for the income range applicable to the borrower's adjusted annual income.	
<b>Median Income Range</b>	<b>Equivalent Interest Rate*</b>
0%-50%	1.0%
50.01%-54.99%	2.0%
55.00%-59.99%	3.0%
60.00%-64.99%	4.0%
65.00%-69.99%	5.0%
70.00%-74.99%	6.0%
75.00%-80.00%	6.5%
80.01%-89.99%	7.5%
90.00%-99.99%	8.5%
100.00%-109.99%	9.0%
110.00%-or more than adjusted median income	9.5%
*EIR can never exceed the note rate and in no case be less than one percent.	

**2. Calculating the Floor Payment**

Borrowers, except for those with leveraged loans, must pay a minimum for principal, interest, taxes, and insurance (PITI) of:

- 22 percent of adjusted income for very low-income borrowers;
- 24 percent of adjusted income for low-income borrowers with adjusted incomes at or below 65 percent of the applicable median income; or
- 26 percent of adjusted income for borrowers with adjusted income above 65 percent of the applicable median income.



## **B. Payment Assistance Method 2.**

The amount of payment assistance granted is the lesser of the difference between:

- (i) The annualized promissory note installments for the combined RHS loan and eligible leveraged loans plus the cost of taxes and insurance less twenty-four percent of the borrower's adjusted income, or
- (ii) The annualized promissory note installment for the RHS loan less amount the borrower would pay if the loan were amortized at an interest rate of one percent.

Borrowers receiving payment assistance method 2 must pay to RHS the greater of:

- 24% of their adjusted annual income less the amortized payment for the eligible leveraged loan less the cost of taxes and insurance; or
- A payment to RHS based on an interest rate of 1%.

An eligible leveraged loan is a loan with payments amortized over a period of not less than 30 years and an interest rate that does not exceed three percent.

Exhibit 4-3 provides an example of this calculation.

## Paragraph 4.3 Calculating Payment Assistance

**Exhibit 4-3**  
**Sample Payment Assistance Method 2 Calculation**  
 (These calculations are done by LoanServ)

**The Jones family received an RHS loan for \$60,000 and an Affordable Leveraged Loan for \$30,000.**

	<b>Principal amount</b>	<b>Payment Period</b>	<b>Note Rate</b>
<b>RHS Loan</b>	<b>\$60,000</b>	<b>33 Years</b>	<b>6%</b>
<b>Affordable Leverage Loan</b>	<b>\$30,000</b>	<b>30 Years</b>	<b>3%</b>

**The Adjusted Annual Income (AAI) is \$23,000; monthly Taxes and Insurance are estimated at \$150 per month.**

- 1. Calculate the combined Annual Payment at the Note Rate plus Taxes and Insurance less 24% of the AAI.**

**\$349 RHS (\$60,000 @ 6% for 33 years = \$4188)**  
**\$127 Affordable Leverage Loan (\$30,000 @ 3% for 30 years = \$1524)**  
**\$150 Estimated Annual taxes and insurance = \$1800**  
**\$626 Less**  
**\$460 AAI (\$23,000 x 24% = \$5520)**  
**\$166 Total monthly subsidy = \$166**

- 2. Calculate the annualized note installment less the annualized 1% installment.**

**\$349 RHS Note Payment = \$6000**  
**\$178 RHS 1% Payment (\$60,000 @ 1% for 33 years - \$2136)**  
**\$171 Total monthly subsidy = \$171**

**Payment subsidy will be based on option 1.**

**Calculate Borrower PITI**

**\$626 (Combined Note Rate Payments Plus Taxes and Insurance)**  
**\$166 Less Subsidy (option 1)**  
**\$460 Borrower Payment/PITI**

**Calculate Borrower RHS Payment**

**\$349 RHS Note Rate**  
**\$166 Less Subsidy**  
**\$183 Borrower Payment**

#### **4.4 CALCULATING INTEREST CREDIT**

For eligible borrowers, the amount of interest credit granted is the difference between the amount due at the note rate and a minimum required borrower payment. Borrowers receiving interest credit must pay at least the *greater of*:

- 20 percent of adjusted income, less the cost of taxes and insurance; or
- A loan payment reflecting the loan amount amortized at an interest rate of 1 percent.

Exhibit 4-4 provides an example of this calculation.

#### **4.5 PROVIDING PAYMENT ASSISTANCE METHOD 2 TO BORROWERS NOT CURRENTLY RECEIVING A PAYMENT SUBSIDY**

Borrowers not currently receiving payment subsidies generally become eligible for payment assistance as a result of a decrease in income. Borrowers may request assistance, or the Servicer may recognize that the borrower is now eligible for payment assistance as a result of interactions with the borrower.

##### **A. Eligibility**

To be eligible for payment assistance a borrower not currently receiving a payment subsidy must have income at or below the applicable low-income limit and personally occupy the dwelling. Payment assistance cannot be provided in conjunction with loans funded before August 1, 1968, or with loans made on nonprogram or above-moderate terms. However, such loans may be refinanced as a new loan to enable the borrower to obtain payment assistance, as described in Paragraph 5.3 A.

## Paragraph 4.5 Providing Payment Assistance Method 2 to Borrowers Not Currently Receiving a Payment Subsidy

**Exhibit 4-4**

**Sample Interest Credit Calculation**  
(These calculations are done by LoanServ)

The Joneses have received interest credit on their initial \$60,000 loan since it was approved.

The following financial information is needed to calculate the payment assistance:

Loan term: 33 years	Note rate: 7%	Median income: \$30,000
\$19,000	Adjusted annual income	\$90 Monthly taxes and insurance
64%	Percent of median ( $\$19,000 \div \$30,000$ )	

(1) Calculate the Annual Payment at the Note Rate

\$389 Monthly payment at the note rate:  
(Amortized amount for \$60,000 @ 7% for 33 years)

(2) Calculate the Minimum Payment for Principal and Interest

\$317 Minimum amount for PITI\* ( $\$19,000 \div 12 \text{ months} \times 0.20$ )  
\$227 Minimum amount for PI\* ( $\$317 - \$90$ )

(3) Calculate the Required Payment at 1 Percent

\$178 Monthly payment (amortized amount for \$60,000 @ 1% for 33 years)

(4) Compute Monthly Interest Credit

\$389	Monthly payment at the note rate
<u>- \$227</u>	Required payment is the greater of (2) or (3)
\$162	Monthly Interest Credit

\* PITI = Principal, interest, taxes and insurance.  
PI = Principal and interest.

## **B. Processing Requests for Payment Assistance**

To determine eligibility, the Servicer sends the borrower *Form RD 3550-21*.

Based on the information provided by the borrower, the Servicer uses LoanServ to compute the amount of payment assistance and, if the borrower is eligible, generates *Form RD 1944-14, Payment Assistance/Deferred Mortgage Assistance Agreement*. The Servicer notifies eligible borrowers by letter. The letter should include *Form RD 1944-14* and, if the borrower has not previously signed a subsidy repayment agreement *Form RD 3550-12*. This agreement requires the borrower to repay the subsidy when the borrower sells the property, refinances the loan, moves out of the property, or pays the loan in full.

## **C. Effective Date of Payment Assistance**

New payment subsidy is made effective on the due date following receipt and processing of executed documents from the borrower.

# **4.6 ANNUAL AND INTERIM REVIEWS OF PAYMENT SUBSIDIES**

## **A. Annual Reviews**

Subsidy agreements are effective for a period not exceeding 24 months. For agreements that exceed 12 months an annual review is conducted by the Servicing Office to determine the borrower's continued eligibility for subsidy.

Before the anniversary date of an existing subsidy agreement for a term exceeding 12 months, the Servicing Office Servicer will initiate an annual review. To complete this review the Servicer notifies the borrower that the current agreement will remain unchanged and continued for another 12 months unless there has been a 10 percent change in income. If the borrower notifies the Servicing Office of a change, the Servicer records the notification and requests verification of the new information provided by the borrower. Approximately 90 days before expiration of the current subsidy agreement, the Servicing Office will initiate a more extensive annual review process. Renewal processing should be completed in time for a new payment subsidy amount to be effective on the expiration date of the borrower's current subsidy agreement.

## Paragraph 4.6 Annual and Interim Reviews of Payment Subsidies

The LoanServ system will identify cases due for review. To complete the renewal process the Servicer sends each borrower Form RD 3550-21, “Payment Subsidy Renewal Certificate,” to request information on household income, expenses, and composition. When the borrower returns the information, the Servicer verifies the information provided as described in Paragraph 4.8 B.

When all necessary verifications are complete, the Servicer uses LoanServ to compute the amount of payment subsidy and, if the borrower is eligible, notifies the borrower by letter of the required monthly payment.

**B. Interim Reviews**

Borrowers who receive payment subsidies must notify the Agency whenever an adult member of the household changes or obtains employment, the household composition changes, or if income increases by more than 10 percent. A borrower whose income decreases may report the change and ask the Servicing Office to determine whether the decrease entitles the borrower to additional payment subsidy. A change in payment subsidy will not be made unless the scheduled principal and interest payment would change by at least 10 percent as a result of the change in household circumstances.

Whenever a borrower notifies the Servicing Office of a change, the Servicer records the notification and requests verification of the new information provided by the borrower, as necessary. The Servicer:



- Uses LoanServ to recompute the borrower’s payment subsidy and to generate the appropriate subsidy agreement.
- Notifies the borrower of any change in the required monthly payment.
- Makes increases in the required monthly payment effective after 30 days notice to the borrower. Decreases in the required monthly payment should be made effective with the next payment due.

The borrower’s next annual review is typically scheduled for 12 months after the effective date of the change in payments.

### **C. In-Depth Reviews**

The Servicing Office will conduct in-depth reviews of borrower income on a random basis of at least one percent of renewals completed for the purpose of quality control. In addition, an in-depth review will be conducted where a borrower's Form RD 3550-21 appears to be inaccurate or the Agency receives information which conflicts with the information provided by the borrower. Quality Control Reviews will be performed by using IRS Form 4506-T, "Request for Transcript of Tax Return". All adult members within the selected households are required to complete and submit IRS Form 4506-T to the Servicing Office to allow for independent verification of tax information with the IRS. Cases where unauthorized assistance has been reported may also be subject to review.

### **D. Trust Loan Borrowers**

If payment subsidy is processed to a borrower who also has a Trust loan, the Trust loan servicer should be notified to assure that the combined calculations are correct and to avoid possible duplication of efforts for the borrower, RHS, and the Trust.

## SECTION 2: EVALUATING BORROWER INCOME

### [7 CFR 3550.53(a) and (g), 7 CFR 3550.54]

#### 4.7 Overview

The Loan Servicer uses income information to help determine whether a borrower is eligible for payment subsidy and the amount of that subsidy. This section provides guidance for verifying and calculating income for each of these purposes. Additional examples are based on Housing and Urban Development (HUD) Handbook 4350.3

#### A. Key Concepts for Income Determinations

##### 1. Income Definitions

Three income definitions are used by the Agency. Whenever income determinations are made, it is essential that the Servicer uses the correct income definition and considers income from the appropriate household members. ***Repayment income*** is used during servicing only to determine if a borrower is eligible for a Moratorium or Reamortization. Only the income of parties to the note is considered when calculating repayment income. To determine whether a borrower is income-eligible for payment subsidies, the Servicer must use ***adjusted income***. Adjusted income is calculated in two steps. First, the ***annual income*** of all household members is calculated. Then, certain household deductions for which the household may qualify are subtracted from annual income to compute adjusted income.

- **Annual Income** is the amount of income that is used to determine a borrower's eligibility for assistance. Annual income is defined as all amounts, monetary or not, that go to, or are received on behalf of, the borrower, co-borrower, spouse or non-spouse of borrower (even if the household member is temporarily absent), or any other household member; all amounts anticipated to be received from a source outside the family during the 12-month period, all amounts that are not specifically excluded by regulations, and amounts derived (during the 12-month period) from assets to which any member of the family has access.



- **Adjusted Income** is used to determine whether a household is income eligible for payment assistance. It is based on annual income and provides for deductions to account for varying household circumstances and expenses.
- **Repayment Income** is used to determine whether a borrower has the ability to make monthly loan payments. It is based only on the income attributable to parties to the note and includes some income sources excluded for the purpose of adjusted income. Repayment Income is used during servicing **only** to determine if a borrower is eligible for a Moratorium or Reamortization as described in Paragraph 5.5.

## 2. Whose Income To Count

For repayment income, the Loan Servicer must consider only the income of household members who are parties to the note. For adjusted income, the income of all household members must be considered. For both repayment and adjusted incomes, live-in aides, foster children, and foster adults living in the household are not considered household members.

An individual permanently confined to a nursing home or hospital may not be applicant or co-applicant but may continue as a family member at the family's discretion. The family has a choice with regard to how the permanently confined individual's income will be counted. **The family may elect either of the following:**

- **Include** the individual's **income and receive allowable deductions** related to the medical care of the permanently confined individual; or
- **Exclude** the individual's **income and not receive allowances** based on the medical care of the permanently confined individual.

## Paragraph 4.7 Overview

Exhibit 4-5 is a table which lists whose income is to be counted.

<b>EXHIBIT 4-5</b>		
<b>INCOME TO BE COUNTED</b>		
<b>Members</b>	<b>Employment Income</b>	<b>Other Income</b> (including income from assets)
Borrower, Co-Borrower	Yes	Yes
Spouse, Co-Spouse/Non-Spouse	Yes	Yes
Other Adult	Yes	Yes
Permanently Confined Family Member	Optional*	Optional*
Dependents (children under 18)	No	Yes
Full-time Student over 18	See Note	Yes
<b>Non-Members</b>		
Foster Child	No	No
Foster Adult	No	No
Live-in Aide	No	No
<p><b>NOTE:</b> The earned income of a full-time student 18 years old or older who is not the Borrower, Co-Borrower or Spouse is excluded after it exceeds \$480.</p> <p><b>*Remember:</b> The family chooses at loan closing to include or exclude the permanently confined individual's income.</p>		

### 3. Income Limits

Some program rules differ according to the income of the borrower. Three different income limits are used for the Section 502 and 504 programs. The National Office provides the income limits and updates the limits whenever they are revised. The income limits are included in Appendix 9. *Adjusted income* should be compared to the income limit to determine the category in which each household falls. Income limits are as follows:

- The very low-income limit is established at approximately 50 percent of the median income for the area, adjusted for household size;

- The low-income limit is established at approximately 80 percent of the median income for the area, adjusted for household size; and
- The moderate-income limit is established by adding \$5,500 to the low-income limit for each household size.

To receive payment assistance, borrowers not currently receiving subsidy must have adjusted income at or below the applicable low income limit. Borrowers currently receiving payment subsidies do not have to meet an income threshold.

Whenever verification from a third party is requested, a copy of *Form RD 3550-1, Authorization to Release Information*, **must** accompany the request. Authorization from each adult household member on the *Form RD 3550-1* permits the Loan Originator/ Servicer to ask for, and verification sources to release, the needed information. The verification and certification formats that are provided in Appendix 2 are not official Agency forms. They are samples that may be adapted as needed for particular circumstances. In some instances the same format can be used whether a third party is providing the verification or the borrower is making a certification.

- **Wage and Salary Income.** Income from employment may include a base hourly wage or salary, overtime pay, commissions, fees, tips, bonuses, housing allowances, and other compensation for personal services of all adult members of the household. When the borrower demonstrates a stable or rising income, current income from each of these sources may be used unless there is evidence to the contrary (such as the employer's indication that such income is NOT likely to continue).

**Example – Stable Income**

Steven Green has been working for the last 6 months for LMN Contractors as a Construction Foreman. Before that, he worked for PDQ Building Supply for 8 months as a Shift Supervisor. There is a 6-week gap in his employment history that he explains as being the result of a lay-off after a large construction project (where he was employed for 15 months as a construction worker) was completed.

Mr. Green's income is considered stable because the reasons for his job changes were related to changes in job opportunities. Even though his job changed several times, his line of work was similar.

**Example – Dependable Income**

Mary Brown receives SSI income for her dependent child who is 17 years of age. The SSI income should not be counted as repayment income because it clearly cannot be expected to continue.

It would be counted as annual income since it is current verified income.

- **Self-employment Income.** Income based on a one-year history of self-employment, in the same line of work, is an acceptable indicator of stable and dependable income.

**Example – Self-Employment Income – (irregular income)**

Julie McAhren sells beauty products door-to-door on commission . She makes most of her money in the months prior to Christmas but has some income throughout the year. She has no formal records of her income other than a copy of the IRS Form 1040 she files each year. With no other information available, use the income reflected on Julie’s copy of her Form 1040 as her annual income.

Betty House sells real estate on commission. She makes most of her money during the summer months.

She has no formal records of her income other than a copy of a W-2 and the Tax Return (Form 1040) she files each year. The gross earning on the W-2 would be used as her annual income.

- **Other Sources of Income.** Income from public assistance, child support, alimony, or retirement that is consistently received is considered stable when such payments are based on a law, written agreement or court decree, the amount and regularity of the payments, the eligibility criteria for the payments, such as the age of the child (when applicable), and the availability of means to compel payments.

#### **Examples – Other Sources of Income**

Janis Phillips is not always well enough to work full-time. When she is well, she works as a typist with a temporary agency. Last year was a good year and she worked a total of nearly six months. This year, however, she has more medical problems and does not know when or how much she will be able to work.

Because Ms. Phillips is not working at the time, it will be best to exclude her employment income and remind her that she must report the date when she resumes work.

Sam Shah receives social security disability. He reports that he works as a handyman periodically. He cannot remember when or how often he worked last year; he says it was a couple of times. Sam's earnings appear to fit into the category of nonrecurring, sporadic income that is not included in annual income.

Mr. Shah's earnings will not be included in his annual income this year, but he must report any regular work or steady jobs he takes.

Ken Hammer receives social security disability. He reports that he works as a handyman periodically. He cannot remember when or how often he worked last year. He says it was a couple of times last year, however, his tax return does not indicate any gross wages from his handyman work.

Mr. Hammer's income would be considered nonrecurring and sporadic income and would not be included in annual income.

## Paragraph 4.7 Overview

- **Seasonal Income.** Seasonal job income may be considered stable income when the borrower has worked in the same line of seasonal work for at least one year. When the borrower receives seasonal unemployment compensation, it must be clearly associated with seasonal layoffs expected to recur and be reported on the borrower's federal income tax returns.

**Examples – Irregular Income (e.g. seasonal income)**

Ross Bosser is a roofer who works from April through September. He does not work in rain or windstorms. His employer is able to provide information showing the total number of regular and overtime hours Ross worked during the past two years.

To calculate Ross's anticipated income, use the average number of regular hours over the past three years times his current regular pay rate, and the average overtime hours times his current overtime rate.

- **Less Than Two Years of History.** In some cases, a history of less than two years is acceptable. The determination requires a careful analysis by the Loan Servicer. This may include a borrower who is either new to the work force or has returned to the work force after an extended absence. In these cases, the Loan Servicer must look at the period of time the borrower has been employed, the employer's evaluation of the likelihood of continued employment (if available), education or training that qualifies the borrower for his/her current position (typically applies to skilled positions), and reasons for absence from the work force in making a determination that income is stable and likely to continue. Information provided by the borrower must be verified by the Loan Servicer.

**Example – Less Than Two Years History**

For the last few years, Ellen Dixon has been a homemaker with no outside employment. Now that her children are old enough, she has taken a job as a teacher for which she has the necessary education and certifications. She completed her 6-month probation period and her employer considers that she is a permanent employee. Ms. Dixon's income can be considered stable and dependable.

It is important to note that had Ms. Dixon not met the employer's probation period, her income would be counted in annual and adjusted income since it is current verified income but not for repayment ability because it is not considered stable and dependable.

## **B. Using LoanServ and the Income Worksheet to Compute Income**

All three types of income are calculated in LoanServ using data entered by the Servicer. **Attachment 4-A**, a Worksheet for Computing Income calculator that helps the Servicer organize borrower's information for data entry and provides instructions to calculate each type of income -, If the worksheet is used to calculate income, place a copy in the borrower's file.

## **4.8 SOURCES & VERIFICATION OF INCOME**

The Loan Servicer will consider sources of income to determine annual and repayment income. This section provides guidance on income that will and/or will not be counted.

- A. For annual income, consider income from the following sources that are attributable to any household member. For repayment income, consider income from the following sources that are: attributable to parties to the note and represent a source of dependable income.
  - 1. The gross amount, before any payroll deductions, of base wages and salaries, overtime pay, commissions, fees, tips, bonuses, housing allowances, and other compensation for personal services of all adult members of the household. If a cost of living allowance or a proposed increase in income has been estimated to take place on or before loan approval, loan closing, or the effective date of the payment assistance agreement, it will be included as income. For annual income, count only the first \$480 of earned income from adult full-time students who are not the borrower, co-borrower, or spouse.

## Paragraph 4.8 Sources &amp; Verification of Income



**Employer paid and provided fringe benefits are not included in annual income regardless of whether the benefits are reported on the employee wage statement. Fringe benefits may include, but are not limited to:**

- Child care/pet-sitting
- Medical/life insurance
- Car/mileage allowance
- Stock options
- Discounts for merchandise
- Sport/concert/movie tickets or entertainment
- Charity donations in employee name
- Any reimbursement of actual work expenses



**Housing allowances may include, but are not limited to:**

- Cash or non-cash contributions paid on behalf of the applicant/borrower by persons not living in the house
- Allowances for members of the Armed Forces
- Allowances for members of the Clergy
- Allowances paid by Employer

2. The net income from the operation of a farm, business, or profession. The following provisions apply:

- Expenditures for business or farm expansion, capital improvements, or payments of principal on capital indebtedness shall not be used as deductions in determining income. A deduction is allowed in the manner prescribed by Internal Revenue Service (IRS) regulations only for interest paid in amortizing capital indebtedness.
- Farm and non-farm business losses are considered "0" in determining annual income. A negative amount must **not** be used to offset other family income.



- A deduction, based on straight-line depreciation, is allowed in the manner prescribed by IRS regulations for the exhaustion, wear and tear, and obsolescence of depreciable property used in the operation of a farm, business, or profession by a member of the household. The deduction must be based on an itemized schedule showing the amount of straight-line depreciation.
  - Any withdrawal of cash or assets from the operation of a farm, business, or profession, or salaries or other amounts distributed to family members from the farm, business, or profession, will be included in income, except to the extent the withdrawal is for reimbursement of cash or assets invested in the operation by a member of the household.
  - A deduction is allowed for verified business expenses, such as lodging, meals, and fuel, for business trips made by salaried employees, such as long-distance truck drivers, who must meet these expenses without reimbursement.
  - For home-based operations such as child care, product sales, and the production of crafts, housing related expenses for the property being financed such as mortgage interest, real estate taxes, and insurance, which may be claimed as business expense deductions for income tax purposes, will not be deducted from annual income.
3. Interest, dividends, and other net income of any kind from real or personal property, including:
- The share received by adult members of the household from income distributed from a trust fund.
  - Any withdrawal of cash or assets from an investment except to the extent the withdrawal is reimbursement of cash or assets invested by a member of the household.

4. The full amount of periodic payments received from Social Security (including Social Security received by adults on behalf of minors or by minors intended for their own support), annuities, insurance policies, retirement funds, pensions, disability or death benefits, and other similar types of periodic receipts. However, deferred periodic amounts from supplemental income and social security benefits that are received in a lump sum amount or in prospective monthly amounts are not counted.

**Example – Adjustment for Prior Overpayment of Benefits**

Dan Steven's social security payment of \$250 per month is being reduced by \$25 per month for a period of six months to make up for a prior overpayment.

Count Dan's social security income as \$225 per month for the next six months and as \$250 per month for the remaining six months.

5. Payments in lieu of earnings, such as unemployment and disability compensation, worker's compensation, and severance pay.
6. Public assistance **except** as indicated in **Paragraphs 4.8 C. and D.**
7. Periodic allowances, such as:
  - Alimony and child support awarded by the court in a divorce decree or separation agreement unless the applicant certifies the payments are not received, and the applicant provides documentation to the Agency that he or she has taken all reasonable legal actions to collect amounts due, including filing with the appropriate courts or agencies responsible for enforcing payment; or
  - Recurring monetary gifts or contributions from an organization or person who is not a member of the household.

**Examples – Regular Cash Contributions**

The father of a young single parent pays her monthly utility bills. On average, he provides \$100 each month. The \$100 per month must be included in the family's annual income.

The daughter of an elderly applicant gives her mother \$175 each month to assist with her living expenses. The daughter plans to continue subsidizing her mother's expenses. The \$175 per month must be included in the annual income.

8. All regular pay, special pay (except for persons exposed to hostile fire), and allowances of a member of the armed forces who is the applicant or spouse, whether or not that family member lives in the home.
- B. Consider these additional sources of income that are attributable to parties to the note and represent a source of dependable income for repayment income only.**
1. Housing Assistance payment (HAP). (HUD's Housing Choice Voucher- Homeownership Program sometimes referred to as Section 8 for Homeownership.) For additional information on the Housing Choice Voucher – Homeownership Program, visit [http://portal.hud.gov/hudportal/HUD?src=/program\\_offices/public\\_indian\\_housing/programs/hcv/homeownership](http://portal.hud.gov/hudportal/HUD?src=/program_offices/public_indian_housing/programs/hcv/homeownership)
  2. Adoption assistance payments in excess of \$480 per adopted child.
  3. Reparation payments paid by a foreign government arising out of the Holocaust.
  4. The full amount of student financial assistance received by household members or paid directly to the educational institutions who are parties to the note. Financial assistance *includes* grants, educational entitlements, work- study programs, and financial aid packages. It *does not include* tuition, fees, student loans, books, equipment, materials and transportation. Any amount provided for living expenses may be counted as **repayment income**.
  5. Amounts received by the family in the form of refunds or rebates under State or local law for property taxes paid on the dwelling unit.
  6. Any other revenue which a Federal statute exempts, will be considered **repayment income**. This includes:
    - The imminent danger duty pay to a service person borrower or spouse away from home and exposed to hostile fire.
    - Payments to volunteers under the Domestic Volunteer Service Act of 1973, including, but not limited to:

## Paragraph 4.8 Sources &amp; Verification of Income

- ◇ National Volunteer Antipoverty Programs which include Volunteers In Service To America (VISTA), Peace Corps, Service Learning Programs, and Special Volunteer Programs.
- ◇ National Older American Volunteer Programs for persons age 60 and over which include Retired Senior Volunteer Programs, Foster Grandparent Program, Older American Community Services Program, and National Volunteer Programs to Assist Small Business and Promote Volunteer Service to Persons with Business Experience, Service Corps of Retired Executives (SCORE), and Active Corps of Executives (ACE).
- Payments received after January 1, 1989, from the Agent Orange Settlement Fund or any other fund established pursuant to the settlement in the "In Re Agent Orange" product liability litigations, M.D.L. No. 381 (E.D.N.Y.).
- Payments received under the "Alaska Native Claims Settlement Act" or the "Maine Indian Claims Settlement Act."
- Income derived from certain sub-marginal land of the United States that is held in trust for certain American Indian tribes.
- Payments or allowances made under the Department of Health and Human Services Low-Income Home Energy Assistance Program.
- Payments received from the Job Training Partnership Act.
- Income derived from the disposition of funds of the Grand River Band of Ottawa Indians.
- The first \$2,000 of per capita shares received from judgment funds awarded by the Indian Claims Commission or the Court of Claims, or from funds held in trust for an American Indian tribe by the Secretary of Interior.
- Payments received from programs funded under Title V of the Older Americans Act of 1965.
- The value of the allotment provided to an eligible household under the Food Stamp Act of 1977.
- Any other income which is exempted under Federal statute.

7. 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 in the home.

8. The special pay to a family member serving in the Armed Forces who is exposed to hostile fire.

9. Income received from the Supplemental Nutrition Assistance Program (SNAP) may be considered to calculate repayment income in an amount **not to exceed 20 percent of the total repayment income** (“not to exceed” amount). The following provisions apply:

- Only the SNAP benefits attributable to the note signers can be considered for repayment income.
- Only **the lesser** of the “not to exceed” amount or the actual SNAP benefits can be included in the applicant’s repayment income.

**Example – Income from SNAP Benefits**

Eloise Thompson’s monthly income from employment is \$800. She also receives \$200 per month in child support payments for her 6-year-old daughter and \$200 per month in SNAP benefits. To consider the SNAP benefits in the repayment income calculation, the “not to exceed” amount must be calculated.

Monthly repayment income excluding SNAP benefits (\$800 + \$200):	\$1,000
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To calculate Income from SNAP benefits:

- |  |         |
|--|---------|
| 1. Equalize the repayment income (\$1,000 / .80):                            | \$1,250 |
| 2. Calculate the “ <b><u>not to exceed</u></b> ” amount (\$1,250 - \$1,000): | \$ 250  |
| 3. Compare to <b><u>actual</u></b> SNAP benefits received:                   | \$ 200  |

The <b><u>lesser</u></b> of the “not to exceed” amount or the actual SNAP benefits:	\$ 200
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Monthly repayment income after SNAP consideration:	\$1,200
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**C. The following sources are *never* considered when calculating **annual income** or **repayment income**:**

1. Income from the employment of persons under 18 years of age, except parties to the note and their spouses.

## Paragraph 4.8 Sources and Verification of Income

2. Income *received by* foster children or foster adults who live in the household, or live-in aides, regardless of whether the live-in aide is paid by the family or a social services program (family members cannot be considered live-in aides unless they are being paid by a health agency and have an address, other than a post office box, elsewhere).
3. Special-Purpose Payments. These are payments made to the borrower's household that would be discontinued if not spent for a specific purpose. Payments which are intended to defray specific expenses of an unusual nature and which are expended solely for those expenses should not be considered as income. Examples include, but are not necessarily limited to, the following:
  - a. Medical Expenses. Funds provided by a charitable organization to defray medical expenses, to the extent to which they are actually spent to meet those expenses.
  - b. Foster Children/Adults. Payments for the care of foster children or adults.  
NOTE: Foster children are not considered members of the family. Therefore, no adjustments to income are to be made because of their presence.
4. Temporary, nonrecurring, or sporadic income (including gifts).
5. Lump-sum additions to family assets such as inheritances, capital gains, insurance payments included under health, accident, hazard, or worker's compensation policies, and settlements for personal or property losses.
6. Amounts that are granted specifically for, or in reimbursement of, the cost of medical expenses for any family member.
7. Payments received on reverse amortization mortgages (these payments are considered draw-down on the applicant's assets).

8. Amounts received by any family member participating in programs under the Workforce Investment Act of 1998 (29 U.S.C. 2931):

- Amounts received by a person with a disability that are disregarded for a limited time for purposes of Supplemental Security Income eligibility and benefits because they are set aside for use under a Plan to Attain Self-Sufficiency (PASS).
- Amounts received by a participant in other publicly assisted programs which are specifically for or in reimbursement of out-of-pocket expenses incurred (special equipment, clothing, transportation, child care, etc.) and which are made solely to allow participation in a specific program.

9. Earned income tax credits.

- Incremental earnings and benefits resulting to any family members from participation in qualifying State or local employment training programs (including training programs not affiliated with a local government) and training of a family member as resident management staff. Amounts excluded by this provision must be received under employment training programs with clearly defined goals and objectives, and are excluded only for the period during which the family participates in the employment training program.
- Allowances, earnings and payments to AmeriCorps participants under the National and Community Service Act of 1990 (42 E.S.C. 12637{d}).

D. In addition, the following sources are *never* considered when calculating annual income:

1. Payments received for the care of foster children or foster adults (usually individuals with disabilities who are unable to live alone).
2. Deferred periodic payments of supplemental security income and Social Security benefits that are received in a lump sum amount or in prospective monthly amounts.
3. Any amount of crime victim compensation received through crime victim assistance (or payment or reimbursement of the cost of such assistance) because of the commission of a crime against the borrower under the Victims of Crime Act (42 U.S.C. 10602).

## Paragraph 4.8 Sources and Verification of Income

4. Any allowance paid under 38 U.S.C. 1805 to a child suffering from spina bifida who is the child of a Vietnam veteran.
5. Payments by the Indian Claims Commission to the Confederated Tribes and Bands of Yakima Indian Nation or the Apache Tribe of Mescalero Reservation (Pub.L. 95-433).
6. Housing assistance payment (Section 8 Homeownership Voucher).
7. Adoption assistance payments in excess of \$480 per adopted child.



### E. Verifying Sources and Amounts

Each borrower must provide information about income, expenses, and household composition to enable the Agency to make income determinations. For payment subsidy renewals borrowers must report income information using *Form RD 3550-21, Payment Subsidy Renewal Certification*, and provide the following documentation:



- Each adult household member listed on the certification must provide a copy of the latest Federal income tax return, and if the adult is employed, copies of the last two pay stubs. Where the amount of income verified through other means differs significantly from the last tax return, the borrower or employer, as appropriate, should be contacted to ascertain the correct income.
- Each adult household member must sign a copy of *Form RD 3550-1, Authorization to Release Information*. Copies of this form must accompany any request for verification from third-party sources. Appendix 2 provides sample certification and verification formats for a number of purposes.
- Any member that receives income from nonemployment sources such as pensions, Social Security, Supplemental Security Income, worker's compensation, public assistance, alimony, or child support must provide a copy of the latest award letter or other documentation of the income received from that source.

The Loan Servicer must review the information provided by the household and determine if any additional verification is required. Written verifications should be provided by third parties when the Loan Servicer determines that it is needed or when conducting quality control reviews. Oral verifications may be accepted if written verifications are not feasible but should be carefully documented. Appendix 2 contains several verification and certifications that may be used to verify various income and expenses.

Type of Income or Verification Source	Verification Requirements and Procedures
INCOME (If Preferred Source of verification can not be obtained without cost, Acceptable Alternative may be used.)	
<b>WAGES or SALARIES</b>	
<b>Verification of Employment</b> <i>Preferred Sources</i>	The borrowers must list all household members on <i>Form RD 3550-21, Payment Subsidy Renewal Certification</i> , and provide their employment status. Each adult household member listed on the certification must provide the latest year's Federal Income Tax Return(s), two current consecutive pay stubs, or earnings statements with year-to-date income. <u>IRS Form 4506-T, Request for Transcript of Tax Return</u> , may be used to obtain a copy of a transcript of tax return(s) if the borrower can not provide copies of actual returns filed.
<b>Paycheck Stubs or Payroll Earnings Statements for not less than two (2) weeks</b> <i>Acceptable Alternatives</i>	They must be the "most recent" as of the date the verification is submitted and must clearly identify the adult household member as the employee by name and/or social security number; must show the gross earnings for that pay period and year-to-date; and must be computer-generated or typed.  Form RD 1910-5, <i>Verification of Employment</i> , must be completed and signed by the employer. A signed statement from the employer may be used to support or clarify income information provided.
<b>Electronic Verification</b> <i>Acceptable Alternative</i>	Electronic printout must clearly identify the adult household member as the employee by name and/or social security number, cover the most recent pay period as of the date the verification is submitted, and show gross earnings for the most recent 30-day pay period and year-to-date.
<b>Oral Verification as permitted in Paragraph 3.15 A.2. of HB-1-3550</b> <i>Acceptable Alternatives</i>	Document the date of contact and list: The employer's name/address/phone number/contact person and title; the employee's name, date of employment, present position and probability of continued employment; the amounts of current base pay and other income such as overtime, bonus, commissions, etc. along with the likelihood that the level of current earnings will continue; and the name and title of the Rural Development employee that contacted the employer.

Type of Income or Verification Source	Verification Requirements and Procedures
<b>SELF-EMPLOYMENT</b>	
Income & Expense Statement <i>Preferred Source</i>	Self-employed adult household members must provide current documentation of income and expenses, which cannot be older than the previous fiscal year. The Loan Servicer must compare the income and expense information provided with the latest Federal Income Tax Return (IRS Form 1040) along with Schedules C & F and/or other applicable schedules, and clarify any discrepancies. For first year business, household member must provide Profit and Loss Statement (projected or actual). <i>IRS Form 4506-T</i> may be used to obtain a copy of a transcript of tax return(s) if the borrower can not provide copies of actual returns filed.
<i>Acceptable Alternative</i>	Two most recent bank statements showing the amount of monthly benefits received; or electronic printouts of federal tax forms & schedules (or State Return if gross income is itemized) showing the breakdown of gross income.

## Paragraph 4.8 Sources &amp; Verification of Income

Type of Income or Verification Source	Verification Requirements and Procedures
<b>SUPPLEMENTAL VERIFICATION</b>	
<b>Seasonal Employment</b> <i>Preferred Source</i>	A household member who is a seasonal worker must provide the most recent Federal Income Tax Return, the prior year's W-2s and/or prior year's 1098 statements. <i>IRS Form 4506-T</i> may be used to obtain a copy of a transcript of tax return(s) if the borrower can not provide copies of actual returns filed.
<b>Unemployment and Unemployment Benefits, Disability &amp; Worker's Compensation, Severance Pay (except lump-sum additions)</b> <i>Preferred Source</i>	<p>If a borrower has recently become unemployed, the Loan Servicer should contact the former employer to confirm that the borrower is no longer employed and that re-employment is not expected.</p> <p>Adult household members receiving <u>unemployment</u> benefits must provide the most recent award or benefit letter prepared by the authorizing agency to verify the <u>non-employment</u> income. Appendix 2 provides a sample format for requesting information about unemployment benefits.</p> <p>Must clearly identify the adult household member as the employee by name and/or social security number. Must cover the most recent earnings as of the date the verification is submitted.</p>
<b>Electronic Verification</b> <i>Acceptable Alternative</i>	Electronic verification for that period, copy of checks, or bank statements, all showing gross earnings. All authorized deductions must be added back to checks or bank statements to reflect gross amount.
<b>Regular, Unearned Income (e.g., Social Security (SS), SSI, Retirement Funds, Pensions, Annuities, Disability or Death Benefits) (except deferred periodic payments)</b> <i>Preferred Source</i>	The adult household member must provide a copy of the most recent award or benefit letter prepared by the authorizing agency. If the date of the letter is not within the last 12 months, require the borrower to submit information updating the award, for example, a cost-of-living (COLA) payment notice, Social Security Benefits Statement, or a notice of change in benefits. Appendix 2 provides sample formats for requesting this information.
<i>Acceptable Alternative</i>	Copies of SS or SSI checks, bank statements, or copy of SS Form 1099 or prior year's award letter plus COLA. If copies of SS or SSI checks or bank statements are provided, Medicare deductions must be added in. If the SSI income fluctuates, the household member must provide award letter stating historical amounts for previous six months.

Type of Income or Verification Source	Verification Requirements and Procedures
<b>SUPPLEMENTAL VERIFICATION</b>	
<b>Alimony or Child Support Payments</b> <i>Preferred Source</i>	The borrower (or adult household member) <b>must</b> obtain a payment history for the last 12 months from the court appointed entity responsible for handling payments. The average amount received will be used in the income calculations.
<b>Divorce Decree</b> <i>Acceptable Alternative</i>	If there is not a court appointed entity responsible for handling payments, the adult household member may provide a copy of the divorce decree, separation agreement, or other document indicating the amount of the required support payments. If the borrower reports that the amount required by the agreement is not being received, the borrower must provide adequate documentation of the amount being received (i.e. copies of the checks or money orders from the payer, etc.) and certify the payments are being received or not received.
<b>Cancelled Checks</b> <i>Acceptable Alternative</i>	If there is not a court appointed entity responsible for handling payments and formal documents were never issued, support payment can be certified as being received or not received.
<b>Support for Foster Children or Adults</b> <i>Preferred Source</i>	Payments received for the care of foster children or foster adults may be considered when calculating repayment income. Documentation must be provided indicating the amount of money received for the care of foster children or adults, and the anticipated period of time the support will be provided. Appendix 2 provides a sample format for requesting information.
<b>Verification of Assets and Income from Assets and Investments</b> <i>Preferred Source</i>	For some assets such as mutual funds or 401(k) accounts, copies of year-end statements can provide information about annual income.
<i>Acceptable Alternative</i>	The two most recent bank statements showing the income from investments must be provided; or Electronic printouts of Federal tax forms & schedules clearly identifying income from interest, dividends & capital gains.

## Paragraph 4.8 Sources &amp; Verification of Income

Type of Expense or Verification Source	Verification Requirements and Procedures
<b>DEDUCTIONS</b>	
<b>Disability Assistance Expenses</b> <i>Preferred Source</i>	To qualify for disability deductions, the borrower must describe the nature of the expense, provide documentation of the costs, and demonstrate that the expense enables a family member to work. <i>Form RD 1944-4, Certification of Disability or Handicap</i> should be used to verify the disability.
<i>Acceptable Alternative</i>	Completed and signed <i>Form RD 3550-21</i> .
<b>Medical Expenses</b> <i>Preferred Sources</i>	For elderly households only, allowable medical expenses may be deducted from annual income. Therefore, documentation of medical expenses is not generally required for non-elderly households. However, non-elderly households with unreimbursed medical expenses in excess of 3 percent of annual income may receive an exception to the asset limitations. In such cases, these medical expenses must be verified as well. Appendix 2 provides a sample format for documenting medical expenses.
<i>Acceptable Alternative</i>	Completed and signed <i>Form RD 3550-21</i> .
<b>Child-Care Expenses</b>	Reasonable child-care expenses may be deducted from annual income. To qualify for the deduction, the borrower must: <ul style="list-style-type: none"> <li>• Identify the children receiving the child care and the family member who can work or go to school as a result of the care;</li> <li>• Demonstrate there is no adult household member available to care for the children;</li> <li>• Identify the child care provider, hours of care provided, and costs (e.g., letter on the child care provider's letterhead or a copy of a signed child care contract); and</li> <li>• Identify the educational institution and provide documentation of enrollment (if appropriate).</li> </ul> Appendix 2 provides a sample format for requesting child-care information.
<i>Acceptable Alternative</i>	Completed and signed <i>Form RD 3550-21</i> .

## F. Projecting Expected Income for the Next 12 Months

Once an income source is verified, the Loan Servicer must project the expected income from this source for the next 12 months. This projection should be based on a comparison and analysis of the figures derived from using all applicable calculation methods. To establish earning trends and avoid underestimating income (especially from overtime); the more methods used the better. However, some income sources will only lend themselves to one method. The four calculation methods are:

1. Straight-based where the benefit or wage amount is converted to the annual equivalent. Income that may not last for a full 12 months should be calculated using a full 12 months projection, including any verified projected increases.
2. Average where the income as reported on the benefit statements or pay stubs for the last 30 days is averaged and then converted to the annual equivalent.
3. Year-to-date (YTD) where the YTD gross earnings are divided by the number of days worked then multiplied by 365. **This method can only be used if the person receiving the income has continuously worked for the same employer or received the benefit since January 1<sup>st</sup> and the reported YTD income is for a period ending after March 1<sup>st</sup>.**
4. Historical where the income as reported on the previous year's tax return is used.

After the Loan Servicer determines the suitable methods and performs the calculations, he/she must determine which figure is most representative of income likely to be received during the next 12 months. If the figures are disparate and one figure is not clearly the most representative, an average of the resulting figures may be used. Conservatively selecting the lowest figure without analysis is not acceptable. The selection must be carefully deliberated and may require additional verification.

## Paragraph 4.8 Sources &amp; Verification of Income

**Example - Projecting Expected Income for the Next 12 Months**

Ken Anderson has worked for B & N Auto for the last two years. According to the verification of employment, Mr. Anderson earns \$10/hour, works 40 hours per week, and is expected to work 25 hours of overtime in the next 12 months. Since Mr. Anderson is paid weekly, he submitted his last four pay stubs through the pay period ending February 20<sup>th</sup> that show gross pay (including overtime) of \$407.50, \$415, \$407.50, and \$437.50. Mr. Anderson's tax return for last year showed gross wages of \$22,100.

<b>Straight-based:</b>	Base pay: \$10/hour x 40 hours/week x 52 weeks/year = \$20,800 Overtime: \$15/hour x 25 hours/year = \$375 Total wages: \$21,175
<b>Average:</b>	$(\$407.50 + \$415.00 + \$407.50 + \$437.50) / 4 \times 52 \text{ weeks/year} = \$21,678$
<b>YTD:</b>	Not appropriate since the ending pay period is before March 1 <sup>st</sup> .
<b>Historical:</b>	\$22,100

The earning trend as supported by the average and historical calculations is that overtime is continuously earned at a rate greater than reported on the verification of employment. The Loan Servicer could use the historical figure of \$22,100 provided the employer confirms that last year was not an anomaly or they could take an average of the resulting figures. Clearly the Loan Servicer should not use the straight-based figure of \$21,175 unless additional documentation is obtained confirming that overtime will be reduced.

On August 30<sup>th</sup>, Mr. Anderson came to the office to say he had found a home to purchase and reported a new baby had increased the size of his family. He would like to have a review to see if his estimated house payment could be lowered. The current pay stub showed \$400.00 gross wages with no overtime identified and year-to-date earnings of \$16,773. A new verification of employment completed by Mr. Anderson's employer, B & N Auto, showed an hourly wage of \$10 and the same projection of 25 hours overtime for the next year.

<b>Straight-based:</b>	Base Pay: \$10/hour x 40 hours/week x 52 weeks/year = \$20,800 Overtime: \$15/hour x 25 hours/year = \$375 Total Wages: \$21,175
<b>YTD:</b>	\$25,299 (Based on YTD Calculation Sheet)
<b>Historical:</b>	\$22,100

Based on the new Verification of Employment completed by the employer, the year-to-date figure of \$25,299 should be used to project the income for the next 12 months.

**NOTE:** These calculations will be documented in writing and included in the case file. A web based work sheet is available at: <http://incomecalc.sc.egov.usda.gov/>



### **G. Income of Temporarily Absent Family Members**

Household members may be temporarily absent from the household for a variety of reasons, such as temporary employment or students who live away from home during the school year. The income of these household members is considered when computing annual income and, if the person is a party to the note, for repayment income.

If an absent person is not considered a member of the household and is not a party to the note, income attributable to the person should not be counted, and the person should not be considered when determining deductions for adjusted income and determining which income limit to use.

#### **Examples - Temporarily Absent Family Member**

James Brown and his wife have applied for a loan. At the moment, James is working on a construction job on the other side of the State and comes home every other weekend. He earns \$600/week and uses approximately one-third of that amount for temporary living expenses. The full amount of the income earned would be counted for both repayment and annual income.

Adam Watson works as an accountant. However, he suffers from a disability that periodically requires lengthy stays at a rehabilitation center. When he is confined to the rehabilitation center, he receives disability payments equaling 80% of his usual income. During the time he is not in the unit, he will continue to be considered a family member. Even though he is not currently in the unit, his total disability income will be counted as part of the family's annual income.

Desirae Bitz accepts temporary employment in another location and needs a portion of her income to cover living expenses in the new location. The full amount of the income must be included in annual income.

Terri Glass is on active military duty. Her permanent residence is her parents' home where her husband and children live. Terri is not currently exposed to hostile fire. Therefore, because her spouse and children are in the parents' home, her military pay must be included in annual income. (If her spouse or dependents were not in the parent's home, she would not be considered a family member and her income would not be included in annual income.)

## H. Wage Matching

In States where the Agency has the legal authority to do wage matching, the Loan Originator will use wage matching to verify income for 5 percent of those households that receive *Form 1944-59, Certificate of Eligibility*. The wage matching request should include all adult members of the household, whether or not they have reported taxable income. If the State does not have sufficient resources to conduct all required wage matching, the State Director should request that the Deputy Administrator, Single Family Housing, authorize a lower percentage.

If the wage matching information does not correspond closely with the income reported by the household, the Loan Originator/Servicer should discuss the discrepancies with the applicant and adjust the household's income, as appropriate.

## 4.9 Calculating ANNUAL AND ADJUSTED Income [7 CFR 3550.54 (b) AND (c)]

Annual income is used as a base for computing adjusted income. Income of all household members, not just parties to the note, should be considered when computing annual income. Adjusted income is used to determine eligibility for the amount of payment subsidies under Section 502 Programs.

### A. Calculating Deductions from Annual Income

Adjusted income is calculated by subtracting from annual income any of five deductions that apply to the household. Not all households are eligible for all deductions. Exhibit 4-6 summarizes these deductions. The remainder of this paragraph provides guidance on determining whether a family is eligible for each deduction and verifying and calculating these amounts.

<b>Exhibit 4-6</b>		
<b>Allowable Deductions from Annual Income</b>		
<b>Deduction</b>	<b>Elderly Households</b>	<b>Non-elderly Households</b>
Dependent Deduction	Yes	Yes
Child Care Expenses	Yes	Yes
Elderly Household	Yes	No
Medical Expenses	Yes	No
Disability Assistance	Yes	Yes

## **B. Dependent Deduction**

A deduction from annual income of \$480 is made for each household member who qualifies as a dependent. Dependents are members of the household who are not the borrower, co-borrower, or spouse, and who are age 17 or younger, an individual with a disability, or a full-time student. The borrower, co-borrower, spouse or non-spouse of borrower (even if the household member is temporarily absent) may never qualify as a dependent. A foster child, an unborn child, a child who has not yet joined the family, or a live-in aide may never be counted as a dependent.

If more than one family shares custody of a child, the family with primary custody can claim the dependent deduction for that child. If there is a dispute about which family should claim the dependent deduction, the family should provide copies of court orders or tax returns showing which family has claimed the child for income tax purposes.

## **C. Child Care Expenses**

Reasonable unreimbursed child care expenses for the care of children age 12 and under are deducted from annual income if: (1) the care enables a household member to work, actively seek employment, or go to school; (2) no other adult household member is available to care for the children; and (3) in the case of child care that enables a household member to work, the expenses deducted do not exceed the income earned by that household member. If the child care provider is a household member, the cost of the children's care cannot be deducted.

Childcare attributable to the work of a full-time student (except for borrower, co-borrower, spouse, or non-spouse of borrower) is limited to not more than \$480, since employment income of full-time students in excess of \$480 is not counted in the annual income calculation. Childcare payments on behalf of a minor who is not living in the household cannot be deducted.

## Paragraph 4.9 Calculating Annual and Adjusted Income

To qualify for the deduction, the borrower must:

- Identify the children who are receiving child care and the family member who can work, seek employment or go to school (academic or vocational) as a result of the care;
- Demonstrate there is no adult household member available to care for the children during the hours care is needed;
- Identify the child care provider, the hours of child care provided, and costs;
- Verify the expense is not reimbursed by an agency or individual outside the family; and
- If the expenses enable a family member to go to school, identify the educational institution. The family member need not be a full-time student.

**Verification of Child Care Expenses**

Childcare hours must parallel the hours the family member works or goes to school. Appendix 2 provides a sample format borrowers can use to document childcare. Other acceptable formats include a letter on the childcare provider's letterhead or a copy of a signed childcare contract.

**Example – Child Care Expense Not Counted**

Joshua Gladson pays \$200 per month in child support. It is garnished from his monthly wages of \$1000. After the child support is deducted from his salary, he receives \$800. The full monthly salary of \$1000 must be counted as income.

**Examples – Child Care Deduction**  
**Separate Expenses for Time at Work and Time at School**

Lou and Bryce have two children. Both parents work, but Lou works only part-time and goes to school half-time. She pays \$4 an hour for eight hours of childcare a day. For four of those hours, she is at work; for four of them she attends school. She receives no reimbursement for her childcare expense.

Her annual expense for childcare during the hours she works is \$4,000 and at school is \$4,000. She earns \$6,000 a year. Bryce earns \$18,000.

Lou's childcare expense while she is working cannot exceed the amount she is earning while at work. In this case, that is not a problem. Lou earns \$6,000 during the time she is paying \$4,000. Therefore, her deduction for the hours while she is working is \$4,000.

Lou's expense while she is at school is not compared to her earnings. Her expense during those hours is \$4,000 and her deduction for those hours will also be \$4,000. Lou's total childcare deduction is \$8,000 (\$4,000 + \$4,000). The total deduction exceeds the amount of Lou's total earnings, but the amount she pays during the hours she works does not exceed her earnings. If Lou's child care costs for the hours she worked were greater than her earnings, she would not be able to deduct all of her childcare costs.

**D. Elderly Household Deduction**

A single \$400 deduction is subtracted from annual income for any elderly household. To be considered an elderly household, a party to the note must be 62 years of age or older or an individual with a disability. Because this is a "family deduction," each household receives only one deduction, even if more than one member is elderly or disabled.

In the case of a family where the deceased borrower or spouse was at least 62 years old or an individual with disabilities, the surviving household shall continue to be classified as an "elderly household" for the purposes of determining adjusted income if:

- At the time of death of the deceased family member, the dwelling was financed by the Agency;
- The surviving household member occupied the dwelling with the deceased family member at the time of death; and
- The surviving spouse (if any) has not remarried.

**E. Deduction for Disability Assistance Expense**

Families are entitled to a deduction for un-reimbursed, anticipated costs for attendant care and “auxiliary apparatus” for each family member who is a person with disabilities, to the extent these expenses are reasonable and necessary to enable the person with disabilities or any household member 18 years of age or older to be employed. The borrower must describe the nature of the expense, provide documentation of the costs, and demonstrate that the expense enables a family member to work. Reasonable documented expenses for care of the individual with disabilities in excess of 3 percent of annual income may be deducted from annual income if the expenses:

- Enable the individual with disabilities or another household member to work;
- Are not reimbursable from insurance or any other source; and
- Do not exceed the amount of earned income included in annual income by the person who is able to work as a result of the expenses. If the disability assistance enables more than one person to be employed, the combined incomes of all persons must be included.

To qualify for this deduction, borrowers must identify the individual with a disability on *Form RD 3550-21, Payment Subsidy Renewal Certification*. *Form RD 1944-4, Certification of Disability or Handicap* should be used to request verification of the individual’s disability from a physician or other medical professional.

**Example – Eligible Disability Assistance Expenses**

The payments made on a motorized wheelchair for the 42-year-old son of the borrower enable the son to leave the house and go to work each day on his own. Prior to purchase of the motorized wheelchair, the son was unable to make the commute to work. These payments are an eligible disability assistance expense.

**NOTE: Auxiliary apparatus includes, but is not limited to, items such as wheelchairs, ramps, adaptations to vehicles, or special equipment to enable a sight-impaired person to read or type, but only if these items are directly related to permitting the disabled person or other family member to work. If the apparatus is not used exclusively by the person with a disability, the total cost must be prorated to allow a specific amount for disability assistance.**

- Include payments on a specially-equipped van to the extent they exceed the payments that would be required on a car purchased for transportation of a person who does not have a disability.
- The cost of maintenance and upkeep of an auxiliary apparatus is considered a disability assistance expense (e.g., veterinarian and food costs of a service animal and cost of maintaining equipment that is added to a car, but not the cost of maintaining the car).

Payments to a care attendant to stay with a disabled 16-year-old child allow the child's mother to go to work every day. These payments are an eligible disability assistance expense. When the same provider takes care of children and a disabled person over age 12, prorate the total cost and allocate a specific cost to attendant care. The sum of both child care and disability assistance expenses cannot exceed the employment income of the family member enabled to work.

**NOTE: Attendant care includes, but is not limited to, expenses for home medical care, nursing services, housekeeping and errand services, interpreters for hearing-impaired, and readers for persons with visual disabilities.**

**Example – Calculating a Deduction for Disability Assistance Expenses**

Borrower earned income	\$14,500
Co-Borrower earned income	<u>+\$12,700</u>
Total Income	\$27,200
Care expenses for disabled 15-year-old	\$ 3,850
Calculation:	\$ 3,850
(3% of annual income)	<u>-\$ 816</u>
Allowable disability assistance expenses	\$ 3,034

**(NOTE: \$3,034 is not greater than amount earned by co-borrower, who is enabled to work.)**

## Paragraph 4.9 Calculating Annual and Adjusted Income

**F. Deduction for Medical Expenses (for Elderly Households Only)**

Medical expenses may be deducted from annual income for elderly households if the expenses: (1) will not be reimbursed by insurance or another source; and (2) when combined with any disability assistance expenses are in excess of 3 percent of annual income.

If the household qualifies for the medical expenses deduction, expenses of the entire family are considered. For example, if a household included the head (grandmother, age 64), her son (age 37), and her granddaughter (age 6), the medical expenses of all three family members would be considered.

**Examples - Typical Medical Expenses**

- Services of physicians, nurses, dentists, opticians, chiropractors, and other health care providers
- Services of hospitals, laboratories, clinics, and other health care facilities
- Medical, Medicaid and long-term care premiums, and expenses to HMO
- Prescription and nonprescription medicine prescribed by a physician
- Dental expenses, x-rays, fillings, braces, extractions, and dentures
- Eyeglasses, contact lenses, and eye examinations
- Medical or health products or apparatus (hearing aids, batteries, wheel chairs, etc.)
- Attendant care or periodic medical care (visiting nurses or assistance animal and its upkeep)
- Periodic scheduled payments on accumulated medical bills
- Travel expense and lodging for medical treatment

**Examples – Excluded Medical Expenses**

- Unnecessary cosmetic surgery to improve the patient's appearance such as face lifts, hair transplants/removal, and liposuction
- Health Club or YMCA dues, steam baths for general health or to relieve physical or mental discomfort not related to a particular medical condition
- Household help even if recommended by a doctor
- Medical savings account (MSA)
- Nutritional and herbal supplements, vitamins, and "natural medicines" unless these can be obtained legally only with a physician's prescription
- Non-prescription drugs unless prescribed by a physician for a particular medical condition
- Personal use items unless it is used primarily to prevent or alleviate a physical or mental defect or illness



One of the most challenging aspects of determining allowable medical expenses is estimating a household's medical expenses for the coming year. While some anticipated expenses can be documented easily (for example, Medicare or other health insurance premiums and ongoing prescriptions), others need to be estimated. The Loan Servicer should use historical information about medical bills to estimate future expenses. However, the estimates should be realistic. For example, if the household has a significant medical bill, the Loan Servicer would count only that portion of the bill that is likely to be paid during the coming year.

#### **Example - Calculating the Medical Expense Deduction**



The Jensions are an elderly household with annual income of \$25,000 and anticipated medical expenses of \$3,000 that are not covered by insurance or another source. The allowable medical expenses would be:

Total Medical Expenses	\$ 3,000
(less) 3% Annual Income	- 750
( $\$25,000 \times 0.03$ )	
Allowable Medical Expenses	\$2,250

#### **Example – Medical Expense Paid over a Period of Time**

Chynna Ray and Justin Grog did not have insurance to cover Justin's operation four years ago. They have been paying \$105 a month toward the \$5,040 debt. Each year that amount ( $\$105 \times 12$  months or \$1,260) has been included in total medical expenses. A review of their file indicates that a total of \$5,040 has been added to total medical expenses over the four-year period. Over the four-year period they have missed five payments and still owe \$525. Although they still owe this amount, the bill cannot be included in their current medical expenses because the expense has already been deducted.

NOTE: For the calculation of assets discussed in Paragraph 4.11, all households are eligible for consideration of medical expenses, not just elderly households.

## Paragraph 4.10 Calculating Repayment Income

**4.10 Calculating Repayment Income**

Repayment income is the amount of household income available to repay the Agency's debt. To compute repayment income, the Loan Servicer should count only the income of persons who will be parties to the note.

The Standard PITI and TD ratio limitations are based on an assumption that borrower income is taxable. If a particular source of income is not subject to Federal taxes, for example, certain types of disability payments or military allowances, the amount of continuing tax savings attributable to the nontaxable income source will be added to the applicant's repayment income. Nontaxable income, such as Housing Choice Vouchers, social security, and child support (provided it is stable and is expected to continue for at least two years), will be multiplied by 120 percent to "gross up" such income.

**Example – "Grossing Up" Nontaxable Income**

The borrower's repayment income of \$22,000 includes \$5,000 of nontaxable income. The revised repayment income for the borrower would be calculated as follows:

\$17,000	Taxable income
<u>+ 6,000</u>	"Grossed-Up" Nontaxable Income (\$5,000 x 1.2)
\$23,000	Revised Repayment

**4.11 Calculating Income from Assets**

During the loan origination process, borrower assets are assessed to determine whether the borrower will be required to make a cash contribution. **After loan origination, only income from assets identified on the borrower's most recent income tax return will be used to determine income for borrowers requesting new or renewed payment subsidy.** Borrowers selected for in-depth quality control reviews will be required to provide sufficient information about household assets to enable the Loan Servicer to complete the review. Form RD 1944-62, *Request for Verification of Deposit*, provides basic information and two certification forms, Verification of Pensions and Annuities, and Certification of Disposition of Assets, can provide additional information about the borrower's assets. For the purpose of computing annual income, the income from assets of all household members is considered. Exhibit 4-7 provides types of assets which are/are not considered in annual income.

**Example – Assets that are Part of an Active Business**

Megan and Tylar Wasson own a copier and courier service. None of the equipment that they use in their business is counted as an asset (e.g., the copiers, the FAX machines, the bicycles).

**Exhibit 4-7**  
**Types of Assets**

**The following types of assets must be considered.**

**Non-retirement assets including:**

- Savings accounts; the average 2-month balance of checking accounts; safe deposit boxes and home;
- Stocks, bonds, Treasury bills, savings certificates, money market funds, and other investment accounts;
- Equity in real property or other capital investments;
- Revocable trust funds that are available to the household;
- Lump-sum receipts, such as inheritances, capital gains, lottery winnings and settlement on insurance claims (including health and accident insurance, worker's compensation, and personal or property losses);
- Assets held in foreign countries; and
- Personal property (such as jewelry, coin collection or antique cars) held as an investment.
- 

**Retirement assets (applicants only) including:**

- Amounts in voluntary retirement plans that can be withdrawn, such as individual retirement accounts (IRAs), 401(K) plans, and Keogh accounts; and
- Amounts in other retirement and pension plans that can be withdrawn without retiring or terminating employment.

**The following types of assets are not considered.**

- The value of necessary items of personal property, such as furniture, clothing, cars, wedding rings and other jewelry not held as an investment, and vehicles specially equipped for persons with disabilities;
- Assets that are part of any business, trade, or farming operation in which any member of the household is actively engaged;
- The value of an irrevocable trust fund, or the value of any trust over which no member of the household has control;
- Interests in American Indian restricted land;
- The value of tax advantaged health, medical savings or spending accounts, and college savings plans; and
- For income calculations, any assets on hand that will be used to reduce the amount of loan.

**Example – Withdrawals from IRAs or 401K Accounts**

Jim Dunn retired recently. He has an IRA account but is not receiving periodic payments from it because his pension is adequate for his routine expenses. However, he has withdrawn \$2,000 for a trip with his children. The withdrawal is not a periodic payment and is not counted as income.

**Example – Withdrawals from a Keogh Account**

Riley Hales has a Keogh account valued at \$30,000. When she turns 70 years old, she begins drawing \$2,000 a year. Continue to count the account as an asset. Determine the cash value and imputed income from the asset. Do not count the \$2,000 she withdraws as income.

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**ATTACHMENT 4-A**  
**WORKSHEET FOR COMPUTING INCOME**

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To access the worksheet and a tutorial on the worksheet, visit the [Forms & Resources](#) page for the Single Family Housing Direct Home Loans.

## CHAPTER 5: SPECIAL SERVICING

### 5.1 OVERVIEW OF SPECIAL SERVICING [7 CFR 3550.201]

The majority of Agency borrowers repay their loans without the need for special servicing. However, some borrowers will encounter financial or personal problems that make it difficult or impossible for them to meet the terms and conditions of the loan. Other borrowers may prove unwilling to do so. In either case, the Agency's response begins with special servicing activities that are designed to help the borrower become current and succeed in repaying the loan. Exhibit 5-1 summarizes the special servicing tools that can be used to help a borrower succeed in repaying a loan. Each of these tools is discussed in detail in this chapter. If, even with the special servicing assistance the Agency can offer, the borrower is unable or unwilling to continue with the loan, the Agency must take action to liquidate the loan in the most cost-effective manner.

Upon receipt of a new loan, the Servicing and Asset Management Office (Servicing Office) New Loan Unit will review the account to ensure it is properly identified as a leveraged/participation loan. A leveraged/participation loan classification will only be given to those loans where the Agency is in a junior lien position and participation loans that are amortized. However, no change will be made to the account that would result in granting a higher amount of payment assistance if the field office approved the loan without granting the EIR. The New Loan Unit will ensure the leveraged lender has been properly identified, including a Tax ID number and consistent spelling of the lender's name and address along with other identifying information, as necessary.

#### A. Time Frame for Servicing Action [7 CFR 3550.202]

An account is considered past due if the scheduled payment has not been received by the due date. A late fee will be assessed if the scheduled payment is not received by the 15th day after the due date. Monthly-pay accounts may be liquidated without further servicing when:

- An amount equal to three scheduled payments is past due; or
- An amount equal to two scheduled payments has been past due for at least 3 consecutive months. Exhibit 5-2 illustrates these time frames.

For annual-pay borrowers, the account may be accelerated without further servicing when at least three-twelfths of one scheduled payment has not been received by its due date.

## **Exhibit 5-1**

### **Special Servicing Tools**



#### **General Servicing**

- Regular followup and counseling for delinquent accounts.
- Conversion of delinquent annual-pay borrowers to monthly payments.



#### **Delinquency Workout Agreements**

- Through delinquency workout agreements of up to 2 years, borrowers agree to make the required monthly payment plus an amount that will bring the account current.



#### **Protective Advances**

- Most commonly used to pay taxes and insurance and initial contributions to a newly established escrow account.
- May also be used to provide funds for repairs to the security property if the borrower cannot qualify for a subsequent loan.
- Advances are repaid through a lump sum, payment schedule consistent with the borrower's ability to pay, or by reamortizing the loan.



#### **Payment Assistance**

- Payment assistance to reduce the borrower's required payment may be made available to eligible borrowers living in eligible units.
- Borrowers with program loans made before August 1, 1968, and nonprogram borrowers may be able to refinance in order to receive payment assistance.



#### **Moratoriums**

- A moratorium "stops the clock" on payments for up to 2 years to enable the borrower to recover from losses of income or unexpected expenses.
- Amounts that accrue during the moratorium are repaid in a lump sum or by reamortizing the loan and including the amounts accrued in the outstanding balance.



**Exhibit 5-2****Illustration of Past Due Time Frames**

Scheduled payment due is \$400 (principal and interest portion equals \$325; taxes and insurance portion equals \$75.)

Example 1: An amount equal to 3 scheduled payments is past due.

	<u>Account Balance Due</u>
April 1: No payment is received.	\$400
April 2: <i>This account is past due.</i>	
April 16: A late fee will be assessed.	\$413
May 1: No payment is received.	\$813
May 16: A second late fee will be assessed.	\$826
June 1: No payment is received.	\$1,226
June 2: An amount equal to 3 scheduled payments is past due.	\$1,226

Example 2: An amount equal to 2 scheduled payments is past due for at least 3 consecutive months.

	<u>Account Balance Due</u>
April 1: No payment is received.	\$400
April 2: <i>This account is past due.</i>	
April 16: A late fee will be assessed.	\$413
May 1: Borrower pays \$200.	\$613
May 16: A late fee will be assessed.	\$626
June 1: No payment is received.	\$1,026
June 2: <i>An amount equal to 2 scheduled payments is past due - first month.</i>	
June 16: A late fee is assessed.	\$1,039
July 1: Borrower pays \$300.	\$1,139
July 2: <i>An amount equal to 2 scheduled payments is past due - second month.</i>	
July 16: A late fee is assessed.	\$1,152
August 1: Borrower pays \$400.	\$1,152
August 2: <i>An amount equal to 2 scheduled payments is past due -- third month.</i>	

NOTE: These examples are presented to illustrate the time frame in which the Agency could initiate liquidation without further servicing. **But** in practice, the Agency should intervene with other servicing actions well before the date that liquidation is permitted.

## B. Identifying Special Servicing Accounts

Accounts that require special servicing should be identified well before either of these thresholds has been reached. In some instances, the borrower may notify the Servicing Office of a problem, such as the loss of employment, even before a single payment has been missed. In the case of a leveraged/participation loan the lender may contact the Agency when the borrower is past due on their account, before a single payment is missed on the Agency debt. In other cases, the Servicing Office will initiate regular followup and counseling with the borrower because of past due amounts. Generally, any borrower with past due amounts equal to two scheduled payments should be referred to a counselor for special servicing.

## C. Developing a Servicing Strategy

The circumstances of each borrower are unique, and the servicing strategy for each should be tailored to the individual circumstances. The special servicing tools in this chapter often may be used in combination.

For each special servicing account, the Servicing Office must work with the borrower to develop a reasonable servicing strategy with the borrower. Servicers must carefully document the strategy and each contact with the borrower.



### Example - Combining Special Servicing Tools

A borrower who loses employment may become delinquent before contacting the Servicing Office for assistance. Such a borrower may be eligible for new or increased payment subsidies or be eligible for a moratorium. Alternatively, the borrower may require a delinquency workout agreement to correct the past due amount.

A borrower may need a moratorium on payments in the case of a serious illness of a household member. The borrower may also need to reamortize the loan at the end of the moratorium period.

It is important when servicing leveraged/participation loans that the Agency be aware of the account status of the other lender. The Servicing Office will attempt to contact the borrower to determine why they are having difficulty making payments to the Agency and the status of the leveraged/participation loan. The Servicing Office will review the borrower's financial situation and determine the servicing action to take on the Agency debt that may include payment assistance and moratorium, Delinquency Workout Agreement, Promise to Pay, or protective advance. If the borrower is past due on the leveraged/participation loan, the Servicing Office must also consider servicing options available from the other lender to bring the account current when working with the borrower on the past due Agency debt.



**D. Borrowers Who Have Filed for Bankruptcy**

All servicing actions connected with a borrower who has filed for bankruptcy protection under any Chapter of the Bankruptcy Code should be handled on a case-by-case basis, with advice from the Office of General Counsel (OGC). This paragraph summarizes the key concepts surrounding the types of bankruptcies that most frequently affect Agency servicing actions.

When a borrower files a petition under the Bankruptcy Code, the court initially prohibits further collection actions by creditors by entering a stay. If the Servicing Office receives the petition, it should be forwarded to OGC with any supporting materials. When a borrower has filed for bankruptcy protection, the Servicing Office should obtain a Notice of Commencement of Bankruptcy from the bankruptcy court to document the bankruptcy activity for the borrower's file.

**Cease Collections**

Servicing Office must not pursue collection activities for borrowers who have filed for bankruptcy.

The Servicing Office should continue to send monthly statements to borrowers who have filed for bankruptcy unless notified by OGC to stop sending statements to borrowers in a particular jurisdiction. All other collection actions must be discontinued until approved by OGC. Payments made voluntarily by the borrower should be accepted.

**SCRA OF 2003**

Determine if borrower is protected by the Servicemembers Civil Relief Act of 2003. Check **CUS/CRE** screen in LoanServ. Field name: SCRA.

The Agency does not need to attend bankruptcy proceedings unless OGC advises it. If an Agency presence is required, Field Staff should be asked to attend the proceedings.

**1. Proof of Claim**

*Official Bankruptcy Form 10, Proof of Claim* is used to itemize the Agency's claims against the borrower for the bankruptcy court. It must be filed within 180 days after the date the bankruptcy was filed, unless the date is changed by the bankruptcy court. No *Proof of Claim* needs to be submitted for Chapter 7 no-asset cases or in cases where OGC determines that the Agency's claim, exclusive of recapture, is fully secured.

**2. Chapter 13 Cases**

Under a Chapter 13 bankruptcy plan, the borrower will continue to make scheduled monthly payments during the life of the plan. If the borrower was in default on an Agency debt at the time the plan was developed, the plan should specify a schedule under which the borrower will repay the delinquent amount during the term of the plan.

The Servicing Office may use special servicing actions, such as granting payment assistance or a moratorium, to help the borrower make scheduled monthly payments. If a borrower does not make scheduled payments according to the plan, the Servicing Office should request OGC guidance in working with the bankruptcy court to resolve the problem. The Agency is not permitted to accelerate the account without the consent of the bankruptcy court, even if the borrower meets the Agency's criteria for liquidation.

Normal servicing may be resumed when the stay is terminated and the trustee has released any interest in the Agency's security. This will automatically occur when the bankruptcy case is dismissed and closed or the plan is complete and the case is closed.

### **3. Chapter 7 Cases**

Under Chapter 7 bankruptcy, the borrower is given the option to liquidate property that he or she can no longer financially retain which may include the Agency's security property. The Agency is not permitted to accelerate the account without the consent of the bankruptcy court, even if the borrower meets the Agency's criteria for liquidation, until the property is no longer property of the bankruptcy estate. Property will cease to be part of the bankruptcy estate if the property is abandoned by the bankruptcy trustee and the borrower receives a discharge or, if the property has not been abandoned, on the earliest to occur of: (1) the date the case is closed; (2) the date the bankruptcy is dismissed; or (3) the date the debtor receives a discharge.

If the borrower will retain the security property, the Servicing Office should request that the borrower execute a "reaffirmation agreement." Under this agreement, the borrower promises to resume payments to the Agency once the bankruptcy case is discharged and would again be personally liable for the debt. If the borrower does not execute a reaffirmation agreement before discharge, *Handbook Letter 102(3550)*, *Continuation with Unreaffirmed Debt After Discharge in Bankruptcy*, must be sent to the borrower after discharge. The Servicing Office should resume normal servicing procedures for borrowers who have received discharges under Chapter 7, and who have executed a reaffirmation agreement or who have received *Handbook Letter 102(3550)*. A borrower who is discharged under Chapter 7 of the Bankruptcy Code and has not signed a reaffirmation agreement is no longer personally liable for the debt.

### **E. Developing a Problem Case Report**

When special servicing is required, the borrower's case will typically be referred to a Servicer who specializes in counseling. In order to become familiar with the case, the Counselor should review the borrower's information and begin a problem case report

## Paragraph 5.1 Overview of Special Servicing [7 CFR 3550.201]

The problem case report is an automated screen that consolidates basic information about the loan and borrower. While some information may not be available when the problem case report is started, all information should be provided before a recommendation for liquidation is made. The problem case report:

- Summarizes the status of the loan and the servicing actions taken or considered;
- Identifies delinquent taxes and other liens against the security, all borrowers and cosigners, and any others who may have an interest in the property;
- Provides information on borrower income and assets and the value of the security property;
- Makes recommendations regarding foreclosure and how other lien holders will be handled.

The problem case report is a living document. It should be updated at key points in the servicing process to summarize all servicing actions that are taken. In this way, the problem case report can serve as an organized reference to the status of the account -- making it easy for the Counselor to review the case and discuss it with supervisors. When the Counselor determines that the borrower cannot be successful or if the borrower fails to cooperate by refusing: (1) to provide information; (2) to agree to a reasonable repayment schedule for the deficiency; or (3) to meet the terms of the agreed upon delinquency workout agreement, the Counselor will complete the problem case report and make a recommendation for liquidation when it is in the best interest of the Government. The problem case report will be submitted to the Counselor's supervisor for review and approval.

## **5.2 DELINQUENCY WORKOUT AGREEMENTS [7 CFR 3550.205]**

Delinquency workout agreements permit borrowers to stop liquidation action by agreeing to pay, in addition to the scheduled payment, an extra amount that will bring the account current within 2 years or the remaining term of the loan, whichever is shorter.

### **A. Eligibility**

Delinquent borrowers with either program or nonprogram loans may be eligible for a delinquency workout agreement. However, a Servicer cannot approve more than one agreement with a particular borrower within a 2-year period without approval from a supervisor. As a condition for approval of a delinquency workout agreement, monthly pay borrowers must be on

escrow and annual-pay borrowers with monthly income must convert to a monthly payment schedule and be on escrow.

## **B. Related Servicing Actions**

Before proceeding with a delinquency workout agreement, it is important to understand the reasons for the delinquency. If the borrower has had difficulty making regular payments because the borrower lost income or had unexpected expenses, a delinquency workout agreement alone will not solve the problem. In such cases a moratorium, rather than a delinquency workout agreement, may be the appropriate servicing strategy. For eligible borrowers, new or additional payment subsidy also may be needed.



### **Realistic Promises to Pay**

An important aspect of a Servicer's counseling role is to help borrowers avoid entering into unrealistic delinquency workout agreements. Delinquency workout agreements should not be used unless available information supports the borrower's promise to pay.

## **C. Processing Delinquency Workout Agreements**

### **1. Determining a Reasonable Payment**

Any time a borrower requires over 60 days to repay a delinquency, the Servicing Office conducts an analysis of the borrower's financial circumstances based upon necessary and essential family expenses to determine a reasonable monthly payment amount and repayment term (not to exceed 24 months). The borrower should provide to the Servicing Office the necessary information for the analysis. To determine an amount for the delinquency workout agreement, a ratio of 41 percent of annual income will be used. After determining 41 percent of the borrower's annual income, subtract the annual amount for principal, interest, real estate taxes, and insurance, child support payments, and installments on consumer and medical debts which will require longer than 6 months to repay. The amount remaining will be used to establish a delinquency workout agreement. In situations where the balance will not pay off the delinquency within 24 months, or there is a negative balance, a delinquency workout agreement will not be established, unless the borrower firmly asserts that they can repay the delinquency within 24 months

### **2. Confirming the Agreement**

For borrowers who agree to pay delinquent amounts within 30 days, the reaffirmation agreement must be documented. At least 30 days before the moratorium is scheduled to expire, the borrower must provide financial information needed to process the re-amortization of the loan(s). Borrowers



who need more than 30 days to repay a delinquency must be sent a letter confirming the repayment agreement. Borrowers who require a formal delinquency workout agreement (any agreement that exceeds 60 days) will receive an adjusted billing statement that itemizes the additional amount to be paid.

### ***3. Late Fees on Delinquency Workout Agreements***

Late fees accrued during the term of the agreement will be waived for months in which the borrower pays according to the agreement.

### ***4. Borrower Failure to Pay***

If a borrower who's required to make payments under a delinquency workout agreement is more than 30 days past due, the agreement is automatically canceled. If the borrower's failure to comply with the terms of the agreement is the result of additional financial problems, additional servicing options may be considered. If the borrower is unwilling to comply with the agreement or if, even with all available servicing options, the account cannot be brought current, the loan should be liquidated.

### ***5. Bringing the Account Current Through Reamortization***

Borrowers who have been successfully paying the amounts due under a delinquency workout agreement may be offered the opportunity to have the outstanding balance reamortized over the remaining term of the loan. To be eligible for reamortization: (1) the remaining term of the delinquency workout agreement must be at least 12 months; and (2) the borrower must have been making full payments without incurring any late fees for at least 6 months.

As a condition of reamortization, annual-pay borrowers with monthly income must convert to a monthly payment schedule, and the borrower must agree to the establishment of an escrow account for taxes, insurance, and related costs. Annual-pay borrowers without monthly income will be encouraged to convert to a monthly payment schedule, but are not required to convert to a monthly schedule or establish an escrow.

## **5.3 USING PAYMENT ASSISTANCE AS A SPECIAL SERVICING ACTION [7 CFR 3550.204]**

Payment assistance is offered as part of a special servicing strategy to help prevent future delinquent payments by adjusting the monthly payment to an amount the borrower can afford.

However, providing payment assistance alone will not cure a delinquency. Therefore, payment assistance must be used in conjunction with either a delinquency workout agreement or a moratorium. Detailed instructions for processing payment assistance are provided in Chapter 4.

#### **A. Refinancing Loans to Permit Payment Assistance**

Payment assistance cannot be provided in conjunction with loans made before August 1, 1968, or with loans made on above-moderate or nonprogram terms. However, borrowers who are in danger of losing their homes due to circumstances beyond their control may be permitted to refinance their loans to enable them to obtain payment assistance. Before proposing that a loan be refinanced, the Servicer should consider whether other servicing actions can solve the problem without payment assistance. If not, the Servicer must consider whether the payment assistance that will be provided, plus any other available servicing actions, will be sufficient to remedy the delinquency and place the borrower in a position to remain current on the new loan. To do so, the Servicer should:

- Confirm that the borrower would be income-eligible for payment assistance following the procedures in Chapter 4; and
- Use LoanServ to estimate the borrower's monthly payments if the loan were refinanced.

If refinancing the loan appears feasible, the Servicing Office should request that the appropriate Field Office originate the new loan. No additional servicing actions are taken on the account until the Field Office makes a determination about refinancing the loan.

#### **B. Servicing Actions While the Request for Payment Subsidies Is Processed**

During the time that it takes to receive and verify income data and determine that the family is eligible for payment assistance, the account continues to accrue late fees.

### **5.4 PROTECTIVE ADVANCES [7 CFR 3550.206]**

The Agency may advance funds to pay for fees and services that are needed to protect the Government's interest in either program or nonprogram property. Protective advances are generally only considered when the Agency cannot provide a subsequent loan for such purpose to the borrower. This could occur because the borrower does not meet current eligibility requirements, a lack of funds, or an unwillingness of the borrower to cooperate. When the Servicing Office becomes aware that a borrower may need a subsequent loan or protective advance, they will refer the case to the Field Office, and cue the Field Office accordingly. The Agency recovers the



## Paragraph 5.4 Protective Advances [7 CFR 3550.206]

amounts advanced by charging the borrower's account. Amounts advanced are due with the next scheduled payment. If the borrower is unable to repay the advance in a lump sum, the Field Office may request that the Servicing Office schedule repayment consistent with the borrower's ability to pay or reamortize the loan.

### **A. Advances for Property Repairs**

Protective advances for property repairs are made only to protect the Government's interest in the security property and should be considered only if the repairs cannot be financed through a subsequent loan. Advances will bear interest at the promissory note rate of the loan against which they are charged. Advances for borrowers with multiple loans secured by the same property should be charged against the largest loan.

#### **1. *Determining the Need for Repairs***

The need for repairs may be identified by either the borrower, Field Office, or the Servicing Office. Field Offices are responsible for completing an inspection of the property, an environmental review, developing a description of the work required, preparing a cost estimate, and approving the protective advance.

#### **2. *Alternative Sources of Funding***

Before processing the advance, the Field Office must first determine whether it appears that the borrower qualifies for a subsequent loan. If a subsequent loan appears feasible, the Field Office will process a loan application immediately. If the need for a protective advance is so urgent or if it is clearly apparent that the borrower would not qualify for a loan, is uncooperative, or that a protective advance is more appropriate, the Field Office must document why alternatives were not feasible and why the repairs are needed to protect the Government's interest when processing an advance. Protective advances will be reported to the IRS as income to the vendor and IRS Form 1099 will be generated. In no case will the borrower or a RD employee be listed as the vendor.

### **B. Advances for Other Purposes**

In order to protect the Government's interest, protective advances also may be used for other purposes. These types of advances will be processed and approved by Field Offices or the Servicing Office, as appropriate. Field Staff will coordinate efforts with the Servicing Office for any loan that is still under the jurisdiction of the Servicing Office. Protective advances for other purposes include such items as:

- Paying off a prior lien holder who intends to foreclose in cases where the Agency is a junior lien holder.

- Paying taxes or insurance premiums; or
- Paying for local assessments.

## 5.5 MORATORIUMS [7 CFR 3550.207]

A moratorium is an agreement between the Agency and a program borrower to suspend the requirement for the borrower to make payments for up to a 2-year period. A moratorium is intended to help a borrower who is experiencing **temporary** financial difficulties avoid foreclosure. Before considering a moratorium, a borrower must first be considered for payment subsidy, or if currently receiving a payment subsidy, an increase in such assistance. A nonprogram borrower is not eligible for a moratorium.

When a borrower with a leveraged/participation loan is approved for a moratorium they should be informed that it is their responsibility to continue making payments on the leveraged/participation loan. If the borrower's loss or decrease in income prohibits them from paying the other mortgage payment consideration can be given to paying off the leveraged/participation lender.

### A. Eligibility

For a borrower to be eligible for a moratorium, all of the following conditions must be met:

- Due to circumstances beyond the borrower's control, the borrower is temporarily unable to continue to make scheduled payments because:
  - ◇ The borrowers repayment income fell by at least 20 percent within the past 12 months. The change in repayment income is based only on the income of parties to the note who are living in the household, or
  - ◇ The borrower must pay unexpected and unreimbursed expenses resulting from the illness, injury, or death of the borrower or a family member, or
  - ◇ The borrower must pay unexpected and unreimbursed expenses resulting from damage to the security property in cases where adequate hazard insurance was not available or was prohibitively expensive.



#### Multiple Moratoriums

A borrower may be eligible for more than 1 moratorium over the life of the loan. No waiting period between moratoriums is required **if** new circumstances qualify the borrower for a new moratorium at the end of a moratorium.

## Paragraph 5.5 Moratoriums [7 CFR 3550.207]

- The borrower occupies the dwelling, unless RHS determines that it is uninhabitable or the borrower may be temporarily absent, and
- The borrower's account is not currently accelerated, and
- The loan was written on program terms.

**B. Initiating the Request for a Moratorium**

Although some borrowers may be knowledgeable enough to request a moratorium, more typically the Servicing Office will recognize that a borrower is a candidate for a moratorium and propose it to the borrower. Regardless of which party initiates the discussion, the borrower must request the moratorium and provide financial information to enable the Servicing Office to determine whether the borrower's new financial circumstances support the request for a moratorium. The Servicer should carefully document the request. Moratoriums are not available to nonprogram borrowers.

**C. Evaluating and Acting on the Request**

A moratorium is not an appropriate servicing tool for borrowers whose circumstances have changed in such a way that it is unrealistic to anticipate recovery within the maximum moratorium period. Both the borrower's plans and the Servicer's judgment enter into this decision. To evaluate the situation, the Servicer must:

- Determine whether the borrower may be eligible for payment assistance or, if already on a payment subsidy, for an increase in such assistance.
- If it is determined that the borrower cannot make the scheduled payments, determine whether the cause is due to reasons beyond the borrower's control;

Conduct a financial analysis to determine whether, given the new circumstances, the borrower is unable to make the scheduled payment;

**Four Key Steps In Evaluating a Moratorium Request**

- Confirm the facts of the case.
- Determine whether a moratorium is the appropriate remedy.
- Determine if borrower is protected by the SCRA Act of 2003
- Determine an appropriate monitoring schedule.

- Determine whether there is reason to believe that the borrower's financial problems are temporary -- that is, can be sufficiently resolved within 2 years to enable the borrower to resume making scheduled payments; and
- If the borrower's request is approved, notify the borrower in writing; or
- If the borrower's request is rejected, notify the borrower and provide information about the appeal process described in Paragraph 1.9.
- If a leveraged/participation loan is involved, determine if the borrower can continue to make the other liholders loan payments;
- If the borrower cannot make the leveraged/participation loan payments determine if the loan should be paid off with a protective advance prior to granting a moratorium.

#### **D. Monitoring Borrower Accounts During the Moratorium**

Moratoriums are permitted only for as long as the borrower's circumstances prevent repayment of the loan. Borrowers are required to report changes in the circumstances on which the moratorium is based. For example, if a moratorium is granted because a borrower loses a job, the Agency must be notified when the borrower finds employment

Borrower eligibility for a continuation of the moratorium should be reviewed at least once every 6 months. The precise schedule should be worked out based on the borrower's individual situation. For borrowers who receive payment subsidy, one of the semiannual reviews should be conducted simultaneously with the annual income re-examination.

When the moratorium is linked to unexpected expenses, the borrower periodically must submit evidence to document that those debts are being paid. Acceptable forms of documentation include certifications from the payee, copies of paid receipts, or canceled checks or money orders. If a borrower will continue to make payments on a leveraged/participation loan, the Servicing Office must verify with the other lender that the payments are being made each month

#### **E. Cancellation of a Moratorium**

The Servicing Office should cancel the moratorium if:

- The borrower does not respond to a request for financial information;

## Paragraph 5.5 Moratoriums [7 CFR 3550.207]

- The Agency receives information indicating that the moratorium is no longer required; or
- The moratorium was granted due to unexpected and unreimbursed expenses, and the borrower cannot show that an amount at least equal to the deferred payments has been applied toward the expenses.

If a cancellation is required, the Servicing Office must notify the borrower. If a borrower provides the information necessary to justify continuance of the moratorium within 30 days of the notification, the Servicing Office should continue the moratorium.


## F. Resumption of Payments

At least 60 days before the moratorium is scheduled to expire, the Servicing Office should review the borrower's account to determine whether the borrower is able to resume making scheduled monthly payments. Unless current income data is available, the borrower must provide updated financial information.

### 1. *Reamortization*

When the moratorium expires or is cancelled, the loan will be re-amortized to include the amount deferred during the moratorium and the borrower will be required to escrow.

**SCRA OF 2003**



Original mortgage interest rate must be restored prior to reamortization for borrowers protected by the Act. Reduce mortgage interest rate to 6% upon completion of the reamortization if borrower is on active duty.

### 2. *Forgiving Interest*

If the new monthly payment, after consideration of the maximum amount of payment subsidy available to the borrower, exceeds the borrower's repayment ability, all or part of the interest that has accrued during the moratorium may be forgiven so that the new monthly payment optimizes both affordability to the borrower as well as the best interest of the Government.

### ***3. Borrowers Unable to Resume Payments***

If after the approved moratorium period, the borrower is unable to resume payments, the account must be liquidated, as described in Chapter 6.

## **5.6 THE LIQUIDATION RECOMMENDATION**

At any point during the special servicing process, it may become clear that the borrower will be unable to succeed and that liquidation is appropriate. The Servicer should discuss this issue openly with the borrower and encourage the borrower to consider voluntary liquidation.

After discussing the situation with the borrower, the Servicer should use the problem case report to recommend liquidation and submit it to a supervisor for approval. Chapter 6 describes the various methods of liquidation that are available. The problem case report should document that the Counselor has pursued all appropriate servicing actions and summarize the reasons for the liquidation recommendation.

## CHAPTER 6: LIQUIDATION AND ACQUISITION

### *[7 CFR 3550.211]*

The Servicer should offer all appropriate special servicing tools to help a borrower with financial problems bring the account current. However, if it is clear that a borrower cannot continue with the loan, the Servicer should analyze the feasibility of liquidation options and recommend the option that is in the Government's best interest, defined as the option which will result in the greatest net recovery. When the Servicer's liquidation recommendation is approved, the Servicing and Asset Management Office (Servicing Office) should take prompt action.

### 6.1 OVERVIEW OF LIQUIDATION OPTIONS

#### A. Voluntary Liquidation

##### 1. *Encouraging the Borrower to Sell*

Sale of security property is generally the most desirable option for both the Agency and a borrower who is unable to continue the loan. For the Agency, a sale to another party avoids the potential costs of liquidation, as well as costs related to owning and disposing of a property. For the borrower, it offers the best opportunity for being released from the debt without a major credit history blemish. A borrower may sell a property to a third party even after the account is accelerated. If a proposed sale will satisfy the debt in full, the account will continue to be handled by the Servicing Office. When it appears that the sale proceeds will not settle the debt in full, the Field Office will handle the sale. The Servicing Office will notify the Field Office of the sale, any relevant information, and provide a Debt Settlement Package to the local office.

If a borrower proposes to sell the property for an amount which may be insufficient to pay the Agency debt, prior liens, and authorized selling expenses, the Field Office may consent to the sale when it is determined to be in the best interest of the Agency. For states included in the REO/Foreclosure centralization, the Servicing Office may consent to the sale. In non-centralized states, the Field Office may consent to the



#### Authorized Selling Expenses

Authorized selling expenses are those which a seller customarily and legally pays to convey title and includes such items as a typical real estate commission, up to three points to enable the buyer to secure credit (but not to reduce the interest rate), real estate taxes, junior liens, deed preparation, abstract and title fees, termite and related inspections, title insurance, surveys, and deed and revenue stamps.

sale. The Agency may also advance authorized selling expenses to facilitate the sale. To determine if the proposed sale is in the Agency's best interest, a copy of the sales contract, appraisal, and sales expenses are needed. Another lender's appraisal may be used if it meets Agency appraisal guidelines.

Whether the short sale request is approved for less than the debt or if the request is denied, a Loan Approval Official should provide their decision in writing to the homeowner. Handbook Letter 115 provides sample language for letters that may be used.

At a minimum, the approval letter should include the approved sale price, amount of net proceeds due to the Agency and a Debt Settlement Package with instructions to return the completed package to the Servicing Office. The homeowner is to be made fully aware that while the Agency is agreeing to release the lien they are still responsible for any remaining debt, which can be settled through the debt settlement process.

The denial letter should state, at a minimum, that the Agency has reviewed the request for consent to sell the property for the proposed sale price and provide specific reasons why the Agency does not consent to the sale. The Field Office should be listed as the contact.

In cases where a junior lien exists, the State Director may approve settlement of a junior lien to effect sale of the property when it is determined to be in the Agency's best interest. Field staff will negotiate the lowest cost to have the junior lien released from the security property, bearing in mind the Agency only seeks to have the lien released (and not necessarily satisfied). The junior lienholder may still seek recovery from the debtor, if permitted by State law.

The Agency's objective is to minimize any potential loss to the Government and to the borrower. The Field Office may consent to a sale for as low as the market value of the property, minus the prior liens and authorized sales expenses. When the proposed sales price is less than the market value, a net recovery valuation is required. Both action is handled in the Field Office and the final decision to concur with the proposed sale lies with a Loan Approval Official.

**Example - Sale for Less Than Debt**

A borrower's debt is \$30,000, the sales price of the property is \$28,000, authorized sales expenses are \$3,000, and the market value is \$28,000. In this case, the Loan Approval Official may consent to the proposed sale since it will net the Agency \$25,000 (\$28,000 minus \$3,000 in authorized selling expenses). If the proposed sales price was less than the market value (\$28,000), a net recovery valuation would be required.



## Paragraph 6.1 Overview of Liquidation Options

When sales proceeds will not fully satisfy the debt, the Servicing Office will make the determination of whether the borrower will be released from personal liability. This determination is based upon a Debt Settlement Package completed by the borrower and forwarded to the Servicing Office for review and approval. A completed Debt Settlement Package is required to be submitted at or before loan closing for all sales for less than the debt, and sales proceeds must be submitted by certified or cashiers check. In cases where the borrower is not able or willing to complete the Debt Settlement Package, the Field Office may still release the mortgage when it is determined to be in the best interest of the Agency. This generally occurs when the borrower has moved out of the area or failure to close the loan will result in liquidation and the Agency receiving less than the anticipated net recovery value. The Debt Settlement Package, if available, and proceeds from the sale will be transmitted to the Cash Section of the Loan Administration Branch in the Servicing Office. *Form RD 3550-17* with the final payment coded "00" will be used to transmit the loan proceeds.

The Field Office will enter in GLOBAL/NOTES the date of the sale or assumption, purchase price, outstanding vouchers, and the date funds were submitted to the Servicing Office. On accounts which were accelerated, the Field Office will also update the FCL/INFO screens with third party information. When proceeds have been posted or the assumption processed, the Servicing Office will notify the Field Office of such action through Task #86, "Approved short sale, release mortgage/deed only," and will provide further guidance on release of the promissory note or debt settlement action, as appropriate.



### Debt Settlement

A Debt Settlement Package consists of:

- *Form RD 3550-20, "Application for Settlement of Indebtedness"*
- *Form RD 3550-21, "Payment Subsidy Renewal Certification"*
- Copies of the last two months bank statements for all accounts
- Verification of Income (last two pay stubs, benefit letter, etc.)
- Copy of most recent Federal Income Tax Return
- Copy of Net Recovery Worksheet, if applicable
- Estimated selling expenses
- Any other relevant information

The Servicing Office should provide the Field Office with a Debt Settlement Package or the Field Office may assemble the necessary information. For emergency releases on debt settlement cases, Field Offices may fax the above information to: Servicing Office, Direct Loss Mitigation Section, ATTN: QR Debt Settlement, in Servicing Office at (314) 457-4451 or (314) 457-4551. The borrower's telephone number must be provided. Nonemergency cases are sent to the aforementioned section in the Servicing Office.

## ***2. Deed in Lieu of Foreclosure***

After the account has been accelerated, the borrower can offer to convey the security property to the Agency. The Agency will accept the deed in lieu of foreclosure only if the Agency will realize a greater net recovery value than would be obtained if foreclosure proceedings continued. Such a decision must be approved by a supervisor. However, the borrower is not released from liability for any remaining debt unless the procedures for debt settlement outlined in Section 3 of Chapter 7 are followed.

## ***3. Borrowers in Bankruptcy***

If the Agency is offered title to a property by a Bankruptcy Court, the decision to accept the conveyance must be approved by a supervisor and the Office of General Counsel (OGC). The Agency generally will accept the conveyance if the Agency will acquire title free of all liens and encumbrances other than Agency loans, and the conveyance will enable the Agency to substantially recover the Agency debt. The Agency may pay any necessary and proper fees approved by the Bankruptcy Court in connection with the conveyance.

## **B. Foreclosure**

### ***1. Agency Foreclosure***



When the Servicing Office determines that liquidation is appropriate, the loan is accelerated. Between the time that the loan is accelerated and the time the foreclosure takes place, the borrower may offer to liquidate voluntarily.

### ***2. Foreclosure by Another Lien Holder***

When notified that a foreclosure action has been or will be initiated by another lien holder, the Servicing Office should develop a strategy that is expected to result in the greatest net recovery by the Government. This may be to join the action, make an offer for the property at the foreclosure sale, or to settle the debt of the other lien holder in exchange for an assignment of the note and mortgage.

In a situation where the Government did not protect its interest in a security property during a foreclosure by another lien holder and the Government has redemption rights, the Servicing Office Supervisor will determine whether to redeem the property depending on the estimated net recovery value.

## Paragraph 6.1 Overview of Liquidation Options

**C. Release of a Valueless Lien**

In liquidation cases, if a net recovery valuation indicates the Agency's lien is valueless (that is, there is no or a negative potential recovery), the lien may be released. This action generally occurs and is approved at the Field Office level, and when done, the Field Office will notify the Field Assistance Desk at the Servicing Office. This is necessary to ensure that taxes and insurance are no longer paid by the Agency, and a Debt Settlement Package is sent to the borrower by the Servicing Office.


**6.2 NET RECOVERY VALUE**

**Estimated net recovery value** represents the amount that the Agency could expect to recover from a property if it was liquidated after considering all costs associated with liquidating, holding, and selling the property. Attachment 6-A contains a net recovery value worksheet to aid in this calculation. **Actual net recovery value** is the amount the Agency in fact does recover from the sale of a property, after accounting for all costs.

**A. Establishing Market Value**

The market value of the property is the fundamental basis for establishing the estimated net recovery value. All calculations undertaken on the net recovery value worksheet provide additions or deductions from market value.

Depending upon the likely method of liquidation and at what point in the process the calculation is being made, market value may be based on an estimated value, on an appraisal, or on the actual sale price. Early in the process of determining which liquidation method should be followed, the Servicer may need to make a rough estimate of the market value based on any available information.

 <b>Calculation of Net Recovery Value</b>
Market value
(less) Costs
<u>(plus) Income</u>
Net recovery value

**B. Environmental Considerations**

The Servicer's estimate of market value must take into consideration potential environmental hazards that may pose a liability issue for the Agency and the presence of environmental resources for which the Agency will have an affirmative responsibility to take protective measures once it owns the property. Exhibit 6-1 provides a partial list of environmental factors for consideration.

In order to minimize Agency liability, the Agency must ensure, *prior* to acquiring property through foreclosure, that the property has been examined for potential contamination from hazardous substances, hazardous wastes, and petroleum products, including underground storage tanks. This should be accomplished by requesting that Field Staff complete the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)*. If the completed questionnaire raises any concerns it should be submitted to the State Environmental Coordinator for further evaluation and guidance.

The Agency also should examine the property prior to acquisition and consider any costs associated with environmental resources the Agency might be required to protect.

For additional information, refer to RD Instruction 1970.



Exhibit 6-1	
Environmentally Sensitive Land Uses and Resources	Extraordinary Circumstances
<ul style="list-style-type: none"> <li>• Historic properties</li> <li>• Federally listed threatened or endangered species, critical habitat, Federally proposed or candidate species</li> <li>• Wetlands</li> <li>• Floodplains</li> </ul>	<ul style="list-style-type: none"> <li>• Any violation of applicable Federal, state, or local statutory, regulatory, or permit requirements for environment, safety, and health.</li> <li>• Any proposal that is likely to cause uncontrolled or unpermitted releases of hazardous substances, pollutants, contaminants, or petroleum and natural gas products.</li> <li>• An adverse effect on the following environmental resources: <ul style="list-style-type: none"> <li>○ Historic properties;</li> <li>○ Federally listed threatened or endangered species, critical habitat, Federally proposed or candidate species;</li> <li>○ Wetlands;</li> <li>○ Floodplains;</li> <li>○ Areas having formal Federal or state designations such as wilderness areas, parks, or wildlife refuges; wild and scenic rivers; or marine sanctuaries;</li> <li>○ Special sources of water (such as sole source aquifers, wellhead protection areas, and other water sources that are vital in a region);</li> <li>○ Coastal barrier resources or, unless exempt, coastal zone management areas; and</li> <li>○ Coral reefs.</li> </ul> </li> <li>• The existence of controversy based on effects to the human environment brought to the Agency's attention by a Federal, tribal, state, or local government agency.</li> </ul>

## Paragraph 6.2 Net Recovery Value

It is important to note that development on Tribal land or dependent Indian communities may require additional coordination with the Tribe to determine if the proposal has an effect on the human environment or an adverse impact on cultural resources and the Section 106 review. In accordance with RD Instruction 1970-H, Exhibit B “when an applicant’s proposal is located on tribal lands, defined in 36 CFR § 800.16(x) as all lands within the exterior boundary of any Indian reservation and all dependent Indian communities, and that tribe has designated a Tribal Historic Preservation Officer (THPO) in accordance with Section 101(d)(2) of NHPA, the SHPO participates only under the conditions specified in 36 CFR § 800.2(c)(1)(ii). If the Indian tribe has not designated a THPO, then the SHPO participates in Section 106 review pursuant to 36 CFR § 800.2(c)(2)(i)(B).” Exhibit D of RD Instruction 1970-H provides guidance on working with Indian Tribes in the Section 106 review.

**C. Ordering An Appraisal**

Information about conducting appraisals is contained in Chapter 5, Section 5 of HB-1-3550. The point at which a formal appraisal is actually conducted will vary.

**1. *Valueless Lien***

If the Servicer’s estimate suggests that the lien may be valueless, an appraisal should be obtained immediately. If the appraisal indicates that the lien is in fact valueless, it should be released without incurring servicing costs.

**2. *Deed in Lieu of Foreclosure***

If, after acceleration, the borrower offers a deed in lieu of foreclosure, an appraisal should be obtained immediately so the Servicer can determine whether it is in the Government’s interest to accept the deed.

### **3. *Foreclosure***

If the property will be going to foreclosure, no appraisal should be obtained until shortly before the sale is scheduled to take place. In areas where the foreclosure process can be lengthy, the value of the property could change before the sale if it is conducted too far in advance.

### **D. Holding Period**

Nearly all costs and income used in the net recovery value calculation are affected by the holding period. For estimated net recovery value, the length of the holding period is estimated differently, depending on the likely method of disposition. The holding period should be estimated as the time between the date the net recovery worksheet is being filled out and the anticipated date for:

- Filing of the deed and the expiration of redemption rights (foreclosure);
- Filing the warranty deed (deed-in-lieu of foreclosure);
- Filing the release (release of valueless lien); or
- Payoff and release (debt settlement offer subsequent to acceleration).

The time for marketing and disposition, if acquired, should also be considered when estimating the holding period.

### **E. Deductions from Market Value**

Numerous costs associated with liquidation must be considered when determining the net recovery value, including the following costs.

- **Prior liens to be paid by the Agency.** In a case where a prior lien is involved, the amount required to repay the prior lien holder must be included in the calculation.
- **Junior liens to be paid by the Agency.** If the Agency pursues foreclosure, junior liens are not paid. However, in the case of a deed in lieu of foreclosure, it may be to the Agency's advantage to pay off a junior lien holder. The Servicing Office should conduct a title search to identify the position and the amount of each lien against the property.

## Paragraph 6.2 Net Recovery Value

- **Selling expenses to be paid by the Agency.** All of the transaction costs involved in selling the property including advertising, commissions for selling agents, required seller certifications, surveys, points, and closing costs paid by the Agency, whether on behalf of the borrower in a voluntary liquidation, or as an Agency expense for an Real Estate Owned (REO) sale, must be included in the calculation.
- **Holding costs.** During the time that the Agency owns the property, the monthly interest accrued is multiplied by the number of months in the holding period.
- **Depreciation during the holding period.** The property may depreciate in value while it is being held by the Agency.
- **Administrative costs.** The administrative burden associated with holding a property includes the cost of liquidation, such as attorney, filing, recordation, advertising, and document service fees that are customarily incurred in a foreclosure action.
- **Management costs.** During the period the Agency holds the property it will accrue costs related to cleaning, securing, and maintaining the property such as utilities and real estate taxes.

**F. Additions to Market Value**

Although most of the adjustments to market value involve deductions to reduce the recovery amount, there are a few factors that can increase the market value.

- **Appreciation during the holding period.** In markets that are strong, the property may appreciate while it is being held by the Agency.
- **Income during the holding period.** In general, the Agency does not lease properties. However, REO properties may be leased in limited circumstances, such as a property located in an area where keeping the property occupied could greatly reduce vandalism.

### 6.3 BASIC SECURITY LOSS

The basic security loss is the difference between the property's market value and the outstanding Agency debt on the property, including principal, subsidy subject to recapture, and other recoverable costs. Exhibit 6-2 provides the basic security loss formula.

It is important for the Servicer to consider the basic security loss in determining how to work with the borrower. For example, the debt settlement arrangements the Agency agrees to might be more lenient in the case of a borrower with a property that lost value through no fault of the borrower. More important, this information can be used for portfolio analysis to help the Agency originate loans more effectively in the future.

<b>Exhibit 6-2</b>	
<b>Calculation of Basic Security Loss</b>	
Gross Investment	
A. \$ _____	Principal
B. \$ _____	Subsidy Recapture
C. \$ _____	Recoverable Costs
Market Value (use current appraisal)	
Basic Security Loss	

### 6.4 DEED IN LIEU OF FORECLOSURE

A deed in lieu of foreclosure is a method of liquidation by which title to the security property is conveyed to the Agency by the borrower. The Agency must not consider a borrower's offer to convey the title to the security property until after the account is accelerated, and then only when it is in the best interest of the Government based upon the estimated net recovery value. After an account has been accelerated, a deed in lieu of foreclosure is processed and approved by Field Offices. In exceptional cases where a borrower offers to convey title to the property at a Field Office when the account has not been accelerated, the Field Office will immediately contact the Servicing Office to determine an appropriate course of action.

To process a deed in lieu of foreclosure, Field Offices will obtain the following items from the borrower: (1) a warranty deed; (2) *Form RD 1955-1, Offer to Convey Security*; and (3) copies of any leases, junior liens, or other documents affecting the title to the property. The borrower should be informed that the deed will not be recorded unless the conveyance is accepted.

Generally, borrowers will be required to satisfy liens and real estate taxes or assessments before conveyance is accepted. However, if the borrower is unwilling to do so, the Agency may elect to satisfy or settle these debts if it is in the best interest of the Government.

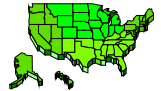


## Paragraph 6.4 Deed In Lieu Of Foreclosure

A deed in lieu of foreclosure does not automatically release the borrower from liability for any outstanding debt. The borrower's account will be credited with the actual net recovery value. If the actual net recovery value does not satisfy the debt, the remaining debt must be debt settled following the debt settlement procedures provided in Section 3 of Chapter 7.

The borrower should be reminded that under a deed in lieu of foreclosure:

- Foreclosure action will not be suspended while the offer for a deed in lieu of foreclosure is considered;
- All costs related to the conveyance paid by the Agency will be added to the debt;
- A credit equal to the actual net recovery value will be applied to the debt;
- If the borrower does not satisfy the debt, the borrower will not automatically be released from liability; and
- The borrower will be required to provide a title insurance policy or a final title opinion from an Agency-approved title company or attorney.



## 6.5 FORECLOSURE

State laws pertaining to acceleration and foreclosure will affect the procedures the Agency is required to follow. OGC should be consulted to ensure that appropriate procedures are followed.

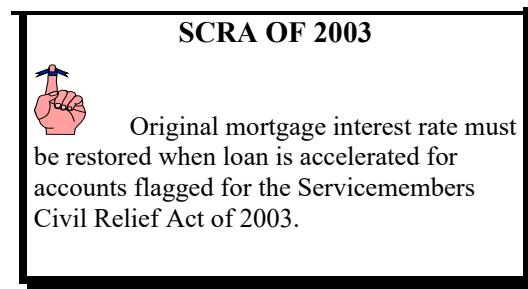
### A. Making the Acceleration Decision

The Servicing Office must decide whether to accelerate the account and begin the foreclosure process. The decision to accelerate involves numerous considerations, many of which will vary case-by-case. The following issues should always be considered.

#### 1. *OGC Concurrence*

OGC concurrence is needed before beginning the foreclosure process if:

- The foreclosure is based on a nonmonetary default;
- The borrower obtained the loan while a civilian and entered military service after the loan was closed; or



- The property also serves as security for a loan under another United States Department of Agriculture (USDA) Agency program such as the Farm Service Agency (FSA), since this may trigger liquidation of the other loan.

## **2. *Tribal Land***

If the security property is located on tribal allotted or trust land, the acceleration may be approved; however, liquidation may not proceed until after the State Director has offered, in writing, to transfer the account to an eligible tribal member, the tribe, or the Indian Housing Authority servicing the tribe or tribes. This offer is generally made after the account has been accelerated, the appeals process has been concluded and the case sent to the respective State office.

## **3. *Role of Other Lien Holders***

Depending upon the status of other liens on the security property, the Servicing Office may invite other lien holders to join in the foreclosure action or join in a foreclosure action initiated by another lien holder.

Assignment of promissory notes and security instruments is authorized where a junior lienholder is foreclosing its lien and is paying the Agency in full.

Recapture will be calculated if the junior lienholder provides the necessary information.

## **B. Acceleration**

### **1. *The Acceleration Notice***

If the Servicing Office determines that the appropriate approach to liquidation is foreclosure, the process begins with an acceleration notice. The acceleration notice demands full payment of the account including unpaid principal and interest, advances, and subsidy subject to recapture. It notifies the borrower of: (1) the reason for the acceleration; (2) the amount due; (3) the method of payment; (4) the opportunity for an informal discussion with the decision maker; and (5) the process for requesting an administrative appeal hearing. The notice gives the borrower 30 days to pay in full or request a hearing.

The notice must be sent to the borrower and any cosigners simultaneously by both regular mail and certified mail. If the property address is different from the address of the borrower, the notice should be sent to the property address as well.

**2. *Treatment of Payment Subsidy***

If a borrower is receiving payment subsidy, the payment subsidy agreement will not be canceled when the debt is accelerated, but the agreement will not be renewed when it expires unless the account is reinstated.

**3. *Special Servicing***

After a borrower's account has been accelerated, the borrower is no longer eligible for any of the special servicing actions described in Chapter 5.

**4. *Assignment of Security Instruments***

Assignment of promissory notes and security instruments is authorized when an account has been accelerated, all appeals have been exhausted, the case has been accepted by OGC for foreclosure, and the Agency is being paid at least the net recovery value of the security property.

**5. *Offers to Pay***

Field Offices will refer offers to cure the default to the Servicing Office. The borrower is permitted to cure the default and retain the loan under the following conditions:

- The Agency is required by State law to reinstate the loan; or
- The Agency is required by a decision from the National Appeals Division (NAD) to reinstate the loan; or
- The borrower has not cured the account within the last two years to prevent foreclosure.

The Deputy Administrator of the Servicing and Asset Management Office has the authority to grant a waiver to the two-year limitation for allowing borrowers to cure the default and avoid foreclosure if it is in the government's best interest. Field Office employees may recommend a waiver to the two-year limitation. When a proposal is made to waive the two-year limitation, a cure and financial statement must be completed to include wage or other income statements and a profile credit report to demonstrate repayment ability (41 percent Total Debt Ratio). In addition, the borrower must agree to establish and fund an

escrow account, and agree to cure the default within 30 days of the date of the offer (which must be at least two weeks prior to the scheduled foreclosure sale date). In States with judicial foreclosures, the offer may only be accepted until the time the case has been referred to the United States Attorney for foreclosure. Field Offices will submit the request to waive the two-year limitation through their State Office for submission to the Servicing Office, Attention: Acceleration Unit. In the submission to the Servicing Office, State Offices will indicate the borrower's total debt ratio and why the waiver is being requested. Field Offices will maintain the supporting documentation in the borrower's case file.

When an offer is made to accept less than the full amount to cure the default, a cure and financial statement must be completed. If RHS accepts the offer the account will be reamortized if the borrower is unable to pay the remaining delinquency within 30 days of reinstating the account.

Funds submitted by a borrower to a Field Office should be sent to the lockbox on a RD Form 3550-17, "*Funds Transmittal Report*."

### **C. Review of the Acceleration Decision**

Several remedies are available to borrowers who believe their accounts should not have been accelerated. These include an informal review at the Servicing Office, mediation or dispute resolution, and a formal appeal with the NAD. Paragraph 1.9 describes the appeal and review process in detail.

### **D. Initiating Legal Proceedings**

Field Offices should continue the foreclosure process 30 days after the acceleration notice is sent if the borrower does not request an informal review or appeal the acceleration decision, or as soon as NAD upholds the Agency's decision to foreclose. Because foreclosure law differs from State to State, the Servicing Office should consult with OGC for guidance, as necessary, regarding the specific processing procedures for each State.

The Agency will only seek a deficiency judgment (in those States where available) when foreclosure is initiated and the Agency determines the borrower has or will have the assets from which a deficiency judgment could be recovered. Deficiency judgments will never be sought in the following situations: (1) acceleration is due to an unpaid recapture amount; (2) the borrower was granted a moratorium at any time during the course of the loan and faithfully tried to meet the loan obligations; (3) State law does not permit a personal deficiency; (4) in nonjudicial foreclosure States, the United States Attorney will not accept a referral for the deficiency; or (5) the Agency has determined after consultation with OGC, that it is not cost effective to seek a deficiency on a particular case.

## Paragraph 6.5 Foreclosure

Throughout the time required for legal proceedings to conclude, the Servicer should encourage the borrower to liquidate voluntarily and may consider using the debt settlement options described in Section 3 of Chapter 7.

### **E. The Foreclosure Sale**

Once legal proceedings have concluded, the property will be sold at a foreclosure sale. To complete the foreclosure process, Field Offices must determine how much to bid and enter that bid at the sale.

#### **1. Establishing a Bid Amount**

The Agency's bid will be the lesser of the Agency's gross investment or the estimated net recovery value of the security property.

Gross investment is the sum of:

- ***The unpaid balance***, defined as:
  - ◇ In States with judicial foreclosure, the judgment account established as a result of the foreclosure judgment.
  - ◇ In States with nonjudicial foreclosure, the borrower's account balance reflecting secured loans and advances.
- ***All outstanding advances and fees charged to the borrower's account.***
- ***Total subsidy received.***

#### **2. Bidding at the Foreclosure Sale**

Procedures for bidding at a sale will vary by locality and a local presence may be required. If the Agency is the highest bidder, the property will become REO property, which will be managed and disposed of by the Field Office. If the amount received through the foreclosure sale is less than the borrower's outstanding debt, the Servicing Office will follow the debt settlement procedures outlined in Section 3 of Chapter 7. Note: RHS must lease or sell program and nonprogram inventory properties to public agencies and nonprofits to provide transitional housing and to provide turnkey housing for tenants of such transitional housing and for eligible families.

**ATTACHMENT 6-A**  
**NET RECOVERY VALUE WORKSHEET**

<b>I. BACKGROUND</b>	
(1) Case Number:	(2) Borrower Name/ID
(3) Proposed Liquidation Option:	(4) Calculation Date:
(5) Estimated Holding Period: <sup>1</sup>	
<b>II. CALCULATION OF NET RECOVERY VALUE</b>	
(6) Market Value (use current appraisal)	(6)
(7) Deductions from Market Value	
A. Prior liens to be paid by the Agency	\$ _____
B. Junior liens to be paid by Agency (N/A for foreclosures)	\$ _____
C. Selling expenses to be paid by Agency <sup>2</sup>	\$ _____
D. Holding costs <sup>3</sup>	\$ _____
E. Depreciation During Holding Period	\$ _____
F. Administrative Costs <sup>4</sup>	\$ _____
G. Management Costs <sup>5</sup>	\$ _____
H. Total Reductions (sum of items 7A through 7G)	\$ _____
(8) Additions to Present Market Value	
A. Appreciation during holding period	\$ _____
B. Income during holding period	\$ _____
C. Total Additions (sum of items 8A and 8B)	\$ _____
(9) NET RECOVERY VALUE (6 <u>minus</u> Item 7H <u>plus</u> Item 8C)	

<sup>1</sup> To calculate holding period:

- For release of valueless lien, use number of months from calculation to filing the release;
- For refinancing, use number of months from calculation to closing of new loan and payoff;
- For sales, use number of months from calculation to closing of loan or transfer and assumption;
- For deed-in-lieu of foreclosure, use number of months from calculation to filing warranty deed;
- For debt settlement offer subsequent to acceleration, use number of months from calculation to payoff and release;

- For foreclosures, use number of months from calculation to filing of deed and expiration of redemption rights; and
- Add the time for marketing and disposition, if acquired.

<sup>2</sup> Selling expenses: advertising, commissions for selling agents, required seller certifications, surveys, points, and closing costs to be paid by the Agency.

<sup>3</sup> Holding costs: monthly interest accrual multiplied by number of months in the holding period.

<sup>4</sup> Administrative costs: costs of liquidation, including attorney, filing, recordation, advertising, and document service fees that are customarily incurred in a foreclosure action.

<sup>5</sup> Management Costs: cost of cleaning, securing, and maintaining the property during the holding period, including utilities, real estate taxes, and other assessments accruing for custodial or REO properties.

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## CHAPTER 7: SPECIAL COLLECTIONS

### 7.1 INTRODUCTION

Although most borrowers fulfill their obligations, special collection efforts are sometimes required. This chapter describes the procedures for recovering unauthorized assistance; collecting debts owed the Agency due through administrative, salary and IRS offsets; and debt settlement.

It is the Agency's policy to collect unauthorized assistance, whether the assistance was received as a result of error or deception, unless any applicable Statute of Limitations has expired. Even if the error was made by Agency staff, the borrower is responsible for repaying the unauthorized amount. The Agency will provide assistance to help borrowers who received unauthorized assistance based on an error. Section 1 of this chapter provides instructions for identifying, investigating, and correcting instances of unauthorized assistance.

In the case of unauthorized assistance or any other debt owed the Agency, amounts owed to the Agency may be collected by offsetting payments due a borrower from Federal agencies including Internal Revenue Service (IRS) tax refunds and Federal employee salary and retirement payments. Section 2 of this chapter provides instructions for obtaining offsets of debt from these sources.

When all other collection attempts have failed, the Agency may elect to accept a portion of the remaining debt to settle and close the account. Debt settlement procedures are provided in Section 3.

### SECTION 1: UNAUTHORIZED ASSISTANCE [7 CFR 3550.164]

### 7.2 OVERVIEW OF UNAUTHORIZED ASSISTANCE

The process used to collect unauthorized assistance differs depending upon the form of unauthorized assistance and whether it was received based on false information or an error.

***Inaccurate information*** includes incorrect information inadvertently provided, used, or omitted without the intent to obtain benefits for which the borrower was not eligible. The error may be caused by the borrower, a third party, or the Agency; the source of the error is irrelevant. The Statute of Limitations for collecting unauthorized assistance as a result of inaccurate information is 6 years.



***False information*** includes information that: (1) the borrower knew was incorrect or should have known was incorrect; and (2) was provided or omitted for the purpose of obtaining assistance for which the borrower was not eligible. If both false and inaccurate information was provided or omitted, the account is serviced as if the unauthorized assistance is solely the result of false information. A borrower is held accountable for false information provided by a third party if the borrower knew or should have known that the information provided was incorrect. The Statute of Limitations for collecting unauthorized assistance as a result of false information is 10 years.

### **A. Three Types of Unauthorized Assistance**

#### ***1. Unauthorized Loan***

Loans made to unqualified loan borrowers, written at the wrong interest rate, or made for an ineligible purpose are considered unauthorized assistance. Borrowers are not considered to have obtained unauthorized assistance if, due to inaccurate information, they obtained a loan despite inadequate payment ability, or received a program loan when private credit would have been available.

#### ***2. Unauthorized Subsidy***

Subsidy received by a borrower for which they were not eligible. The Agency only seeks collection of the unauthorized assistance if the amount received is equal to or greater than \$550, in which case the borrower must repay the full amount of unauthorized subsidy received.

Unauthorized assistance will not be pursued when an individual who is eligible for a same rates and terms assumption under HB-1-3550, Paragraph 13.14 B. has been occupying the security property, receiving subsidy based on their household income, and executes a same rates and terms assumption. As these cases are identified, the Unauthorized Assistance Unit will notify the individuals occupying the security property in writing that unauthorized assistance will be pursued unless an assumption agreement is signed within 90 days. A task will be sent to the Field Office informing them of the unauthorized assistance and a request to have the individuals execute a same rates and terms assumption. If the assumption is not executed within 90 days and the Field Office has not requested an extension to complete the processing of the assumption, collection of the unauthorized assistance will be pursued.

## Paragraph 7.2 Overview of Unauthorized Assistance

**3. *Unauthorized Grant***

Grants made to unqualified borrowers, or for an ineligible purpose, are considered unauthorized assistance.

**B. Consequences for borrowers****1. *Assistance Based on False Information***

Borrowers who obtained unauthorized assistance based on false information must pay off the loan and repay the subsidy within 30 days of the expiration of all appeal rights. A borrower who received a loan without being eligible, or the loan was approved for unauthorized purposes, must repay the outstanding loan balance.

A borrower who received unauthorized subsidy must repay the unauthorized amount in a lump sum. If the unauthorized subsidy is repaid within the required time frame, the loan may be continued. The borrower also may continue to receive payment subsidy for the authorized amount.

**2. *Assistance Based on Inaccurate Information***

Borrowers who obtained unauthorized assistance based on inaccurate information also are required to correct the situation within 30 days of the expiration of all appeal rights. However, the Agency may permit the borrower to retain the loan, with some adjustments, and may assist borrowers who cannot repay delinquent amounts in a lump sum.

- **Loan to over-income borrowers.** If a Section 502 borrower's income was above the moderate-income level at loan approval or closing, the borrower must refinance with private credit, or the loan must be converted to a nonprogram loan. If a Section 504 borrower's income was above the very low-income level at loan approval or closing, the loan must be converted to a Section 502 loan.
- **Loan to ineligible borrowers.** If a borrower was not eligible for a loan, the Agency cannot continue the loan and must require that it be repaid within 30 days.

- **Loan to other borrowers.** The loan can be continued on existing terms if the loan was approved for unauthorized purposes, or the borrower's income was incorrect, but the borrower still qualified as income-eligible.
- **Loan at wrong interest rate.** If the wrong interest rate was used on the promissory note, the account must be adjusted using the correct interest rate.
- **Subsidy.** If a borrower received unauthorized subsidy based on inaccurate information, the borrower must repay the unauthorized amount.



#### Loans Made at the Wrong Interest Rates

If a loan was made at the wrong interest rate, but the borrower was granted subsidy at the correct interest rate, the unauthorized assistance is zero for the period of the subsidy agreement. The promissory note must be corrected to reflect the appropriate interest rate.

### 3. *Unauthorized Grants*

Borrowers who received an unauthorized Section 504 grant should correct the situation within 30 days of the expiration of all appeal rights, regardless of whether it was received based on false or inaccurate information. The grant borrower must repay it in a lump sum or execute a promissory note agreeing to convert the grant to a Section 504 loan to be repaid over time, unless the borrower does not have repayment ability.

If a borrower is unable to repay the unauthorized grant in a lump sum, the Servicing and Asset Management Office (Servicing Office) should evaluate the borrower's current financial situation. If the borrower has repayment ability and agrees to repay the unauthorized assistance, the Servicing Office must execute *Form RD 1940-16, Promissory Note*. If the borrower has repayment ability but refuses to repay, the Servicing Office should document the information and seek a judgment on the account.



#### Best Practice

For grant of \$7,500, seek the best lien obtainable to secure repayment.



### 7.3 IDENTIFYING AND INVESTIGATING CASES

The Agency may identify instances of unauthorized assistance through file reviews conducted by the Servicing Office, referrals made by a Field Office or private citizen, or audits conducted by the Office of the Inspector General (OIG) of the United States Department of Agriculture. Suspected cases of unauthorized assistance must be investigated to determine whether unauthorized assistance was actually received.



#### **Suspension or Debarment**

The Servicing Office Servicers should recommend suspension or debarment when false information has been provided by the applicant. The National Office will decide whether to accept or reject the recommendation. The ultimate decision is made by an Administrative Law Judge.

If the case does not involve false information, the Servicing Office must conduct the investigation and document all actions and findings. Any case of unauthorized assistance that may be the result of false information must be referred to OIG. OIG also becomes involved in cases discovered during OIG audits. Whenever OIG is involved, all the Servicing Office actions are deferred until the OIG investigation is completed, or OIG declines to handle the case and refers it to the Servicing Office. If OIG chooses to handle a case, no further the Servicing Office involvement is necessary, unless OIG requests assistance.



In the investigation of cases involving false information, OIG or the Servicing Office must determine whether the borrower was aware of or should have been aware of false information submitted by a third party. Borrowers will not be penalized for false information submitted by a third party if they were not aware of the submission. In such a case, the account is serviced as if the unauthorized assistance is the result of inaccurate information.

OIG requires reports on the results of the investigation into any audit cases, regardless of whether the case is handled by OIG or the Agency. Cases involving grants or pending liquidation are not closed until the account is paid in full, otherwise satisfied, or liquidation is completed.

## **7.4 NOTIFICATION AND APPEALS AND ADMINISTRATIVE COST**

### **A. Notify Borrower**

The Servicing Office must notify the borrower of the determination that unauthorized assistance has been received, specifying in detail the reasons the assistance was found to be unauthorized, and the amount to be repaid. The borrower has 30 days to consult with the Servicing Office or to dispute the claim.

### **B. Borrower Consultation**

The borrower should contact the Servicing Office if he or she wishes to review the claim with the Agency. During the consultation, the Servicing Office should outline the reasons the assistance is believed to be unauthorized and document the borrower's responses. If the borrower requests additional time to assemble documentation, the Servicing Office may grant an extension that is long enough to gather such information. The number of days granted for the extension must be documented so that the notice of determination is not sent before the extension has elapsed.



### **C. Notice of Determination**

At the end of the 30-day consultation period and after any extension period has elapsed, the Servicing Office should notify the borrower of the final amount of assistance determined to be unauthorized, where to send the payment, servicing actions to be taken by the Agency, and the borrower's appeal rights. Servicing actions to recover unauthorized assistance cannot proceed until the 30-day period allowed to request an appeal has elapsed and any appeal that is filed has been concluded.

### **D. Administrative Cost**

Borrowers who are contractually obligated will be assessed a \$300 administrative cost plus any additional third party costs if the borrower fails to repay unauthorized assistance or enter into an Agency approved repayment plan to repay the lump sum amount within 30 days after the borrower's appeal expiration date or final appeal determination date.

## **7.5 DETERMINING THE AMOUNT DUE**


### **A. Determine Correct Interest Rate**

If the loan was made at the wrong interest rate, the Servicing Office must determine the rate that should have been used at the time the loan was made.

## Paragraph 7.5 Determining the Amount Due

- For borrowers who were income-eligible at loan approval and closing, the Servicing Office should use the Agency interest rate in effect at the time of loan approval or closing, whichever is lower.
- For borrowers who were not income-eligible for a Section 502 loan at loan approval or closing, the Servicing Office should use the nonprogram interest rate in effect at the time of loan approval. Appendix 6 contains a list of historical nonprogram interest rates.
- For borrowers who were not income-eligible for a Section 504 loan or grant, the Servicing Office should use the program or nonprogram interest rate that would have been applicable at the time the loan or grant was made.

#### **B. Determine Correct Subsidy Amount**



**Consequences if a loan account adjustment results in delinquency:**

In the case of false information:

- Borrower must repay in a lump sum; or
- Servicing Office accelerates loan.

In the case of inaccurate information:

- Borrower may repay in a lump sum; or
- Borrower may consent to reamortizing the account; or
- Servicing Office accelerates loan.

The amount of subsidy borrowers were eligible to receive will be calculated based on the amount they were eligible for at the time the unauthorized assistance began, even if their eligibility has changed over time.

#### **C. Reverse and Reapply Procedures**

For unauthorized assistance resulting from payment subsidy, a fee may be established in accordance with Paragraph 7.6 B.2. For all other types of unauthorized assistance, borrower accounts must be adjusted retroactively to establish the amount of unauthorized assistance. This adjustment or fee amount calculation involves determining the amount paid by the borrower since the unauthorized assistance began and applying that amount to the monthly installments that should have been charged, as illustrated in Exhibit 7-1. This may create an account delinquency in the amount of the unauthorized assistance that must be repaid.


<b>Exhibit 7-1</b>		
<b>Reverse and Reapply Procedures</b>		
Mr. Smith received a loan in January 1996. An incorrect interest rate was used to calculate Mr. Smith's monthly payment and the error was not identified until April 1996. Due to the error, Mr. Smith was making \$400 payments but should have been making \$450 payments. The following illustrates how his monthly payments were applied to his account at the incorrect rate and the application of payments at the correct rate after the account adjustments were made.		
<b>Month</b>	<b>Incorrect Rate</b>	<b>Correct Rate</b>
January	400	450
February	400	450
March	400	450
April	400	250
<b>TOTAL</b>	<b>1,600</b>	<b>1,600</b>
Mr. Smith's account is now \$200 past due.		

## 7.6 SERVICING ACTIONS

### A. Assistance to Borrowers

The Agency offers no assistance to loan borrowers who obtained unauthorized assistance based on false information. If the borrower is unable or unwilling to make the required payment within 30 days of the expiration of all appeal rights, the loan will be accelerated.

If a borrower obtained unauthorized assistance based on inaccurate information and is unable to repay the amount due in a lump sum, the Agency will assist the borrower by reamortizing the loan to include the delinquent amount. If the borrower fails to authorize reamortization within 30 days of the expiration of all appeal rights, the loan will be accelerated. Any lump sum payments received after the account is accelerated will be handled in accordance with Paragraph 6.5 B.5.

<b>SCRA OF 2003</b>	
	Original mortgage interest rate must be restored when loan is accelerated for borrowers protected by the Act.

## Paragraph 7.6 Servicing Actions

**B. Processing Changes to the Account****1. Change in Interest Rate**

Any time an interest rate must be changed, *Form RD 1940-16* must be amended and the borrower must initial the change. Based upon State law, and with the advice of the Office of General Counsel (OGC), the real estate mortgage or deed of trust may also need to be amended. If a borrower fails to execute *Form RD 1940-16* or other required documents within 30 days, the Servicing Office should obtain advice from OGC and accelerate the account.

**2. Change in Subsidy**

If the current subsidy agreement is incorrect, the Servicing Office must reverify the borrower's income, following the procedures discussed in Chapter 4, unless the required information has been gathered during the course of the unauthorized assistance investigation. The Servicing Office should send *Form RD 3550-21* to the borrower. If the borrower fails to provide the required information within 30 days, the installment at the promissory note interest rate will be due.

The amount of unauthorized assistance will be established as a fee on the account. The fee will be placed on the primary loan. The fee will be due and payable within 30 days. If a lump sum payment is made, it will be applied against the fee.

**3. Reamortization**

If a borrower received unauthorized assistance based on inaccurate information and is unable to repay the unauthorized amount within 30 days, the account can be reamortized to include the unauthorized amount using *Form RD 3550-18*, *if the borrower occupies the property*. If the borrower fails to sign *Form RD 3550-18* within 30 days, the account will be accelerated. Escrow will be required at the time of reamortization if the borrower is delinquent on real estate taxes and insurance or does not have insurance.

**C. Reactivating Satisfied Accounts**

If a former borrower with a satisfied account is found to have received unauthorized subsidy, the account must be reopened so that the necessary account adjustments can be made. The Servicing Office should attempt to contact the former borrower using the last known address and phone number to inform them of the unauthorized subsidy and to request repayment. If the borrower agrees to repay, he or she should execute *Form RD 1940-16*. The new *Form RD 1940-16* should be written at the interest rate that had been used for the initial loan. The term should be as short as feasible, given the former borrower's ability to pay, but generally not more than 5 years. If the real estate mortgage or deed of trust had not been released, OGC should be consulted about any changes in the documents necessary to secure repayment.



If the borrower fails to repay the unauthorized subsidy, the Servicing Office should attempt to obtain financial information about the borrower. If the borrower has assets, the Servicing Office should seek a judgment to secure repayment. If financial information is not available or the borrower cannot be located, the Servicing Office should debt settle the unauthorized subsidy as described in Section 3 of this chapter.

If the Real Estate mortgage or Deed of Trust has been released and the amount of unauthorized assistance is less than **\$550**, the unauthorized assistance will not be pursued.

## SECTION 2: OFFSETS [7 CFR 3550.210]

### 7.7 OVERVIEW OF OFFSETS

Any money that is or may become payable to an Agency borrower or debtor from the United States may be subject to offsets for the collection of a debt owed to the Agency. This section discusses three types of offsets.



Through an **administrative offset**, the Agency may collect money, such as retirement benefits or a Farm Service Agency contract payment, that is or may become payable to a borrower from a Federal agency. Administrative offsets must be conducted in accordance with the procedures in 7 CFR Part 3, Subpart B.

**Salary offsets** must be conducted in accordance with 7 CFR Part 3, Subpart C. The Agency may use a salary offset to collect a debt owed from a borrower's pay if the borrower works for a Federal agency, the United States Postal Service, the Postal Rate Commission, or is a member of the United States Armed Forces or military reserve, or any other persons covered in 7 CFR Part 3, Subpart C.



#### Applicability to Debtors

Offsets may be used to collect debts owed by present borrowers and former borrowers (debtors). For simplicity, the term "borrower" is used rather than stating borrower or debtor each time a reference is made.

The Agency may offset a borrower's Federal tax refunds to collect a debt owed. **IRS offsets** must be conducted in accordance with the provisions of 31 U.S.C. 3720A and 31 CFR 285.2.

Administrative and salary offset may be used simultaneously to cure a debt. Although the IRS offset is the tool most commonly used by the Agency, it can only be used if the debt cannot be obtained through administrative or salary offset and cannot be used in conjunction with the other two types of offset.

### 7.8 ANNUAL REVIEW OF DELINQUENT ACCOUNTS

At least once a year, delinquent accounts should be screened to identify borrowers eligible for offset. Offsets will not be considered unless the account is delinquent by more than 2 monthly payments and the delinquent amount is at least \$25. Offsets are not permitted when any of the circumstances listed below exist.

- The account is accelerated and collection of the debt through offset would jeopardize foreclosure litigation or reinstate the borrower's account. The Servicing Office should consult with OGC for guidance on pending foreclosure cases;
- The account is under the jurisdiction of a bankruptcy account or has been discharged in bankruptcy;
- The borrower received the loan before entering full time active duty in the military service and is still on active duty;
- The account is current under an approved adjustment, moratorium, or delinquency workout agreement, or the account has a suspend code that indicates a problem with the account; or
- The statute of limitations has expired.

## 7.9 SALARY AND ADMINISTRATIVE OFFSETS

If a borrower has salary or other income that can be offset, the Servicing Office must determine whether the offset is appropriate and, if an administrative or salary offset will not be pursued, document the reasons. If the Servicing Office plans to collect a debt through an administrative or salary offset, the borrower must be notified within 15 days of the determination.



### A. Amount of Offsets

Payments effected by administrative offset are collected in a lump sum. If the borrower has multiple Agency loans, any amounts collected are applied based on the advantage to the Agency.

For salary offsets, a borrower's disposable pay, after taxes, is offset 15 percent each pay period. Disposable pay includes basic, special, incentive, retired, retainer, or other authorized pay. The dollar amount offset from a borrower's pay may change if income increases or decreases. The borrower may volunteer to have a larger amount deducted by submitting to the Servicing Office *Handbook Letter 103(3550), Agreement to Increase Salary Offset*. If the borrower has multiple Agency loans, amounts collected are applied to the accounts based on the advantage to the Agency.

## Paragraph 7.9 Salary and Administrative Offsets

**B. Notifying the Borrower**

*Handbook Letter 104(3550)*, *Notification of Salary Offset* should be used to notify the borrower of a salary offset, and *Handbook Letter 105(3550)*, *Notification of Administrative Offset* should be used to notify the borrower of an administrative offset. The notification letter must be sent by both regular and certified mail with a return receipt requested. The letter should state the nature and amount of the debt, the intended date of collection, the facts giving rise to the determination, and an explanation of the borrower's rights.

**Time Frames**

An offset must not take effect until 30 days after the borrower receives notice of the Agency's intent to use offset. Time frames begin once the borrower signs for the certified mail. If the certified mail receipt is not signed, the time frame begins on the date of nondelivery for salary offset and 10 days after the regular mail was sent for administrative offset.

The Agency is not required to provide notification before effecting an administrative offset if providing the notice would substantially affect the Government's ability to collect the debt. However, if the borrower was not previously notified, the borrower should be notified as soon as possible using *Handbook Letter 105(3550)*.

**C. Borrower Response and Appeals**

Borrowers may avoid having their salaries or other payments offset by paying the delinquency within 30 days. If the account has been accelerated the full amount owed must be paid. If the account has not been accelerated, the borrower must make a payment sufficient to bring the account current.

Borrowers have the right to obtain copies of their records, provide evidence against the claim, have a consultation with the Servicing Office, and appeal the decision. Borrowers must make all requests in writing. The Servicing Office should send a letter to advise the borrower of the decision for all requests made, unless the borrower's request was for copies of documents only. If the borrower's request is denied, the letter should state the reasons for the denial and the borrower's appeal rights. All decisions should be documented in LoanServ.

**Requests for Records**

Borrower requests for copies of their records should be met as quickly as possible to enable the borrower to review documents, provide evidence to the Servicing Office, or to file a petition. Copying costs may be charged to the borrower's account.



**1. Consultation with the Servicing Office and NAD Appeals**

A borrower who has any questions concerning the determination of the offset may consult with the Servicing Office. As a result of the consultation, the borrower may request that the Servicing Office review additional documentation to refute of the determination. Borrowers must state in the request the reasons for the review. If the borrower needs additional time to assemble documentation, an extension may be granted for the amount of time the Servicer believes will be needed to gather such information. All reviews are based on written evidence, unless otherwise agreed upon by the Agency and borrower. Payments are not offset until the borrower is sent a letter about the Agency's decision.

The borrower may appeal a Servicing Office adverse decision to the National Appeals Division (NAD) following the procedures described in Paragraph 1.9. If a borrower appeals to NAD, action on the offset is suspended until NAD has made a determination.

**2. Delinquency Workout Agreement**

If a borrower requests a delinquency workout agreement, the offer should be accepted if the amount offered is not less than the Agency would obtain from an offset. Extreme hardship or unfairness to the borrower due to the offset may be a consideration in the decision. If a borrower is exempted from offset because of extreme hardship or unfairness, the Servicing Office and the borrower must agree on a delinquency workout agreement, and the debt must have adequate security. Any decision to reject an offer for payment in lieu of a salary offset must be based on an analysis of the borrower's financial situation.

**3. Debt Settlement**

A debt settlement offer in lieu of offset may be considered only if the account has already been accelerated or the delinquency is owed by a former borrower with an inactive account. If a borrower requests debt settlement, the borrower should be informed of the application procedures for debt settlement, but action on the offset should not be delayed. Debt settlement procedures are provided in Section 3 of this chapter.

**4. Petitioning for a Salary Offset Hearing or Administrative Offset Appeal**

Borrowers who wish to request a hearing or appeal conducted by an Administrative Law Judge or other official not under the control of the Secretary of Agriculture must submit a petition to the Servicing Office within 30 days of the notification of salary and administrative offset. The borrower must state in the petition the reasons supporting the request and sign it. Petitions filed late are only accepted if the delay was beyond the borrower's control.

## Paragraph 7.9 Salary and Administrative Offsets

The Servicing Office may choose to provide a borrower who has requested a salary offset hearing the opportunity for a review of file documents in lieu of a salary offset hearing, if the matter can be solved more efficiently in this manner. The borrower must be notified of the acceptance or non-acceptance of a petition and the time and place of the hearing, if applicable. Accepted petitions stay the collection of the debt.

Final decisions should outline the facts of the case and provide a repayment schedule, if applicable. Decisions are made within 60 days of the request for a salary offset hearing and 30 days of the hearing for administrative offset.

**D. Processing Offsets**

Paying agencies must be provided written certification that the debtor owes the Agency a debt. The certification outlines the basis for the offset, amount, due date, and a confirmation that the Agency abided by the regulations for offsets. If proper certification is not provided to the paying agency, the request will be returned to the Servicing Office. Once the Servicing Office receives notice from the paying agency that the offset has been effected, the Servicing Office should credit the borrower's account in LoanServ for the amount offset.

**1. Administrative Offset**

To request an administrative offset, the Servicing Office should send *Handbook Letter 106(3550), Request for Administrative Offset* to the appropriate Federal agency. The Servicing Office must cancel administrative offset requests by written notification to the paying agency once the borrower's account is brought current or otherwise satisfied. An agency may decline an administrative offset request if the offset would substantially interfere with or defeat the purposes of a program.

Paying agencies should be notified as soon as practical of debtors eligible for administrative offset so that the paying agency can flag the debtor's account. Early identification can help alleviate problems with collecting the debt under the statute of limitations. If at least 1 year has elapsed since the original administrative offset was requested from the paying agency, the debtor may offer a repayment plan in lieu of the offset.

## **2. Salary Offset**

To request a salary offset, the Servicing Office should submit *Handbook Letter 107(3550), Request for Salary Offset* to the paying agency and attach *Handbook Letter 103(3550)* if the borrower has agreed to an offset of more than 15 percent of the borrower's salary. The Servicing Office must notify the paying agency by letter of the cancellation once the borrower's account is brought current or otherwise satisfied.

Generally, the paying agency will contact the Servicing Office if an employee is resigning or retiring before the debt is complete. However, if the Servicing Office becomes aware of the resignation or retirement, they should contact the paying agency immediately to secure repayment of the debt. The Servicing Office should inform the paying agency of the remaining amount of debt owed by the borrower and request the borrower's final salary payment and lump-sum leave to liquidate the debt. If the delinquency will not be resolved, the Servicing Office should instruct the paying agency to put a hold on the borrower's retirement funds in order to offset the remaining debt and should submit a claim to the next paying agency. If the borrower changes employers and salary offset is still a viable option, the Servicing Office should submit a claim to the next paying agency. In this situation, the Agency is not required to provide the borrower with additional notification.

## **7.10 IRS OFFSET**

Since most borrowers pay taxes to the IRS, offsetting tax refunds is an effective tool for collecting amounts owed from a large number of borrowers and is the type of offset used most frequently by the Agency. However, since taxes are refunded only once a year and borrowers must receive at least a 60-day notice before affecting an offset, the Agency must adhere strictly to IRS deadlines. Borrowers who are in debt both prior to and post acceleration may be offset.

### **A. Amount of the Offset**

Whenever possible, the Servicing Office should collect the amount equal to the debt. If this is not possible, the Servicing Office should collect the maximum amount of taxes and request an IRS offset again the following year. If an Agency borrower has multiple debts, the payment should be applied in the order the debts are accrued.

## Paragraph 7.10 IRS Offset

**B. Processing**

Each year, IRS provides the Servicing Office with a schedule for submitting preliminary and final lists of borrowers eligible for IRS offset. After LoanServ screens borrower's accounts, the Servicing Office should submit to IRS a preliminary list of the borrowers eligible for offset.


**Reporting Delinquencies  
to a Credit Bureau**

It is especially important to report delinquencies to a credit bureau when requesting an IRS offset because the IRS will not offset a borrower's tax refund if the borrower has not been reported to a credit bureau.

Borrowers should be notified of the upcoming IRS offset using *Handbook Letter 108(3550), Notification of IRS Offset*. Borrowers have 60 days from the date of the letter to provide the Servicing Office with evidence against the determination in writing or to pay the delinquency. If the borrower provides documentation, the Servicing Office should determine whether offset will be exercised and send *Handbook Letter 109(3550), Confirmation of IRS Offset* advising the borrower of the decision.

If the documentation provided by the borrower demonstrates that the offset should not be used or should be for a lower amount, or if the borrower pays the amount owed, the Servicing Office should amend the list provided to IRS to reflect the changes. The Servicing Office must submit a final list of the borrowers eligible for offset to the IRS in accordance with the schedule provided by the IRS. Any revisions to the final list can only consist of removing borrowers from the list entirely or reducing the amount to be offset. Since an IRS offset cannot be canceled after the final request has been made, offset amounts that should not have been taken must be refunded to the borrower.

IRS notifies the borrower after his or her tax refunds have been offset. The Servicing Office will credit the borrower's account for the amount of the offset, less the IRS processing costs.

**7.11 REFUNDS**

Offsets received by the Agency in excess of the debt must be returned to the borrower. For administrative offsets only, the refund will include interest on the overpayment calculated at the 90-day treasury bill rate (Exhibit B of RD Instruction 440.1) within 45 days of determining that an overpayment was received.





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### SECTION 3: DEBT SETTLEMENT

Debt settlement should be pursued when all other attempts to collect outstanding debt have failed. If the outstanding debt is secured, debt settlement cannot be pursued until the loan is accelerated or fully matured. If the outstanding debt is unsecured, debt settlement may be pursued at any time, whether or not it is due and payable. Settlement may be requested by the debtor or initiated by the Agency. Debt settlement, when complete, closes the debtor's account.

Debt settlement may take one of the following forms.

- **Compromise.** An agreement that permits the debtor to retain the security property and be released from further liability upon receipt of a specified lump sum that is less than the total amount due. In all instances a reasonable compromise offer is the most expedient and cost-effective method of settling the remaining balance on a debt.
- **Adjustment.** An agreement to release a debtor from liability, generally upon receipt of an initial lump sum and the promise of additional periodic payments over a period up to 5 years. The debtor is not permitted to retain the security property, except in cases of valueless liens.
- **Charge-off.** An action taken by the Agency when a compromise or adjustment cannot be negotiated, but the debtor is not to be released from liability.
- **Cancellation.** An action taken by the Agency to cease collection activities and release the debtor from personal liability for any remaining amounts owed.

*Form RD 3550-20, Application for Settlement of Indebtedness*, is used to process all four forms of debt settlement. However, the Servicing Office may enter into a verbal agreement for a compromise offer which will be documented on LoanServ and confirmed by letter within 5 days to the borrower. The verbal agreement for the compromise should generally require payment within 30 days. Adjustment offers must always be documented on *Form RD 3550-20*. In addition, when the agency cancels debt without application, the basis for cancelling the debt will be documented on LoanServ in lieu of a RD 3550-20.

#### 7.12 COMPROMISE AND ADJUSTMENT OF DEBT [7 CFR 3550.253]

The Agency may agree to a compromise or adjustment for less than the debt owed and cancel the remaining debt. The debtor may request a compromise or adjustment by completing *Form RD 3550-20*. No payment should be accepted until an agreement has been approved; any payment submitted with *Form RD 3550-20* must be returned to the debtor.

Before accepting a compromise or adjustment offer, the Agency must establish that the offer represents the maximum amount the debtor is able to pay based on available financial information as described in Paragraph 7.16. The Agency will not agree to a compromise or an adjustment if there is doubt about a debtor's ability to pay that reduced amount.

#### **A. Compromise**

A compromise involves the acceptance of a lump-sum payment of less than the total amount owed and cancellation of the remaining debt. A debtor may retain the security property under a compromise offer if the compromise payment is at least equal to the net recovery value of the property and it is in the best interest of the Government.

#### **B. Adjustment**

An adjustment provides for payment of an initial lump sum representing the maximum amount the debtor can afford to pay and a new schedule of regular payments over the shortest period the debtor can afford, but no longer than 5 years. If the adjustment offer is for less than the full outstanding debt, any remaining balance is canceled once all payments under the adjustment agreement have been made. The debtor is not permitted to retain the security property, except in the case of a valueless lien.

When an adjustment offer is approved, the Servicing Office must establish an adjustment account, send regular billing statements, and archive any account balance in excess of the adjustment offer. In the event of a default on the agreement, the entire debt should be reinstated. The archived account balances should not be written off and reported to the IRS until the adjustment offer has been fulfilled or the entire remaining debt is canceled because the debtor has defaulted on the adjustment agreement.

A debtor whose adjustment account becomes past due should be contacted as soon as a payment is missed to determine their circumstances and to aggressively seek collection. Any account under an adjustment agreement that becomes past due should immediately be referred for offset, as described in Section 2 of this chapter.

Based on an analysis of the debtor's present circumstances, the Servicing Office may decide to modify the adjustment agreement. The Servicer may approve only one amendment to an adjustment agreement. Any further amendments must receive prior authorization from the next-level supervisor. If the adjustment agreement is modified, it must be documented on *Form RD 3550-20*, or in LoanServ by the Servicing Office and confirmed by letter to the borrower.

## Paragraph 7.12 Compromise and Adjustment of Debt [7 CFR 3550.253]

If the debtor is unable or unwilling to repay the debt, the Servicing Office must notify the debtor, in writing, that the adjustment agreement is canceled and inform the debtor of all available appeal rights. If an adjustment agreement is canceled, payments made by the debtor prior to the cancellation are retained by the Agency.

**7.13 RECALL TREASURY DEBT**

A debt is recalled from Treasury when the Agency has determined that it is in the best interest of the Government to end collection efforts that were used to resolve a Direct Single Family Housing debt remaining after the liquidation of the secured property. This determination is pursuant to the Debt Collection Improvement Act, - 31 U.S.C. 3711(a)(3) and USDA regulation 7 CFR 3.20; as well as, 31 CFR 903.3(a) which identifies the circumstances under which a debt may be terminated.

The Agency will evaluate if a substantial amount of debt is being collected by Treasury by reviewing both the amount of the debt owed (outstanding) and the amount collected regardless of the amount of the debt owed. Annual reviews of a three year collection history will be conducted to determine if:

- Treasury collected at least 30% of the outstanding balance initially due during the past three year period **or**
- Treasury collected more than \$3,600 during the past three years.

If a substantial amount of unsecured debt has not been collected by Treasury during the past three years, the debt may be recalled by the Agency. Once debts are recalled from Treasury, the Agency shall cancel the accounts without further analysis. The Agency issues IRS Form 1099-C (Cancellation of Debt) to borrowers whose debts have been cancelled.

**7.14 CHARGE-OFF OF DEBT**

A debt is charged off when a compromise or adjustment cannot be negotiated with a debtor, but available information indicates that the debtor is able to repay some part of the debt now or in the future. The Servicer should use *Form RD 3550-20* to charge off a debt.

A charge-off does not release the debtor from liability. Debtors whose debts have been charged off will be referred to Treasury for collection. If the Department of Treasury determines the debt is uncollectible and returns to the account to the Agency, the Agency will cancel the debt under paragraph 7.15. An account that has been charged off can be settled through a compromise, adjustment, or cancellation at any time. The debtor is not permitted to retain the security property, except in the case of a valueless lien or when the total debt against the secured property is \$7,500 or less.

## **7.15 CANCELLATION OF DEBT**

Debt will be canceled only if other means of debt settlement cannot be used, there is no security remaining, and the available information indicates that the debtor is unable to repay any part of the debt and has no prospects of doing so in the future. If the security is remaining, cancellation may be approved when the total debt against the secured property is less than \$7,500 and the account has been accelerated. Form RD 3550-20 is used to cancel a debt. If a cancellation is approved based on a review of the borrowers account without the submission of Form RD 3550-20, the decision will be documented in LoanServ without use of the RD Form.

### **A. Application from Debtor**

Upon application by the debtor, the debt may be canceled when there is no deficiency judgment or the debtor is unable to pay any part of the debt and has no reasonable prospects of doing so in the future.

## Paragraph 7.15 Cancellation of Debt

**B. No Application from Debtor**

Without an application from the debtor, the debt may be canceled in any of the circumstances listed below.

- OGC has provided a written opinion indicating that the claim is not legally enforceable.
- The debt has been serviced by the Department of Treasury and returned to the Agency as uncollectible unless it can be documented that further monies can be collected (for example, if a debtor is due to receive an inheritance at a specific point in time). .
- The debtor is deceased, and there are no other known assets from which collection could be made if: (1) a final settlement has been made and confirmed by the probate court, and the Agency has received all the funds to which it is entitled; or (2) a final settlement has not been made and confirmed by the probate court, but there are no assets from which there is reasonable prospect of recovery.
- The debtor has been discharged from the debt through bankruptcy. Such debtors are not personally liable for the debt, and no attempt should be made to collect. However, if debts were discharged, but the debtor executed a new promise to pay prior to the discharge that was properly affirmed by the court, the debtor is liable for the debt and cancellation would not be appropriate.
- A judgment has been obtained, the Department of Justice (DOJ) file is closed, and:
  - ◊ The debtor has no known assets or future debt-paying ability, has disappeared and cannot be found without undue expense, and there is no existing security for the debt; or
  - ◊ Three years have elapsed since any collections were made on the judgment and the debtor has no equity in the subject property.
- A property sold at a foreclosure sale does not generate sufficient proceeds to satisfy the outstanding debt, deficiency judgment was obtained, and OGC has advised that no further collection efforts may be pursued.

- Based on a review of the debtor's case file and other available information, the debtor is unable to pay any part of the debt and has no reasonable prospects of doing so in the future. The decision will be thoroughly documented in the LoanServ system.

## 7.16 NEGOTIATING A SETTLEMENT

Settlements must be negotiated consistently to avoid disparate treatment. If a living debtor is unable to act, an offer of debt settlement may be made by a party having legal authority to act for the debtor.



### A. Assessing the Debtor's Financial Condition

The Servicing Office must assess the financial condition of the debtor before negotiating a settlement. Only the financial situation of signatories to the note and any cosigners should be considered, except in common property States. The Servicer should consider the following factors in evaluating offers:



- Prior liens against the security;
- Value of the existing security, as determined by a current appraisal;
- Debtor's equity in assets not pledged as security for the Agency debt;
- Debtor's total present income and probable income over the next 5 years, including any possible inheritances; and
- Amount of other debt.

This information can be obtained from *Form RD 3550-20* which includes a section on household expenses and provides a formula by which the amount of income available for debt payments can be established. *Form RD 3550-20* may be completed either by the debtor, by the Servicing Office (in the absence of the debtor), or as a joint effort between the Servicing Office and the debtor.

Once *Form RD 3550-20* has been completed, the Servicing Office should send a letter requesting that the debtor submit additional information within 30 days, so that their financial situation can be verified. The Servicing Office should review the following information as part of the financial assessment:

- Verification of income such as paystubs or copies of Social Security checks;

## Paragraph 7.16 Negotiating A Settlement

- \* Debtors' expense verifications such as medical expenses;
- \* Tax returns and bank statements;
- \* County records, such as personal property tax rolls, to determine what other assets the debtor has or may have recently disposed of; and
- \* Department of Labor wage information, where available.

Some of this information may already be available if there has been a recent subsidy renewal. If additional verifications are needed, they should be conducted in accordance with the policies described in Chapter 4. Any costs involved in obtaining the needed financial information are charged to the debtor's account. Credit reports will only be obtained if there is reason to believe the debtor has not provided complete and accurate financial information.

- \* If a compromise, adjustment, or cancellation agreement is to be reached with one of several joint debtors because the other parties will not or cannot join the application, the Servicer must document the reasons the other parties are not included on *Form RD 3550-20* in order to justify settlement with those joint debtors. Joint debtors can not be included on the application if they are deceased, discharged in bankruptcy, or have disappeared.



## B. Special Case Debtors

### 1. *Deceased Debtors*

An offer to settle the debt of a deceased debtor may be made by a duly-appointed executor or administrator. Claims against estates are to be settled based on the value of the security property and the expected value of the estate after paying expenses that have priority over Agency claims, such as the cost of administration, allowances of minor children and/or surviving spouse, allowable funeral expenses, and dower or curtesy rights.

### 2. *Debtors Who Have Disappeared*

Before charging off or cancelling the debt of a debtor who has disappeared, reasonable efforts must be made to locate the debtor. Such efforts generally include contact with Post Offices, motor vehicle licensing authorities, telephone or city directories, utility companies, local, State, and other Federal Government agencies (such as Health and Human Services and the Department of Labor), known relatives and friends, former neighbors and employers, the children's schools, skip-tracing agencies, and the Social Security Administration. Efforts to locate the debtor must be thoroughly documented.





**3. *Settlement Where Debtor Owes More Than One Type of Agency Loan*  
[7 CFR 3550.252(c)]**

A loan on a property should not be settled while other USDA Agency (such as FSA) loans on the same security property remain active, unless settlement is in the best interest of the Government.

**7.17 PROCESSING DEBT SETTLEMENTS**

**A. Escrow and Unapplied Funds [7 CFR 3550.252(h)]**

Escrow disbursements continue until debt settlement is complete or the Agency no longer has a security interest in the property. All remaining funds held in escrow or unapplied when the debt is settled will be applied against the debt.

**B. Approved Settlements**

Once a settlement has been approved, the Servicing Office must take the following actions.

- \* Execute *Form RD 3550-20*.
- \* Notify the debtor, in writing, that a settlement offer has been approved. The notification should outline the specific terms and conditions of the settlement and *Form RD 3550-20* should be attached.
- \* In the case of a cancellation that has not been requested by the debtor, notify the debtor that the debt has been canceled.
- \* In the case of a compromise, adjustment, or cancellation, cancel the offset by notifying the paying agencies that have been contacted for offset.

### **C. Rejected Settlements**

When a settlement offer is rejected, the Servicing Office must document the reasons for rejection on *Form RD 3550-20* and execute the form. The debtor must be notified, in writing, of the reasons that his or her settlement offer has been rejected and must be informed of their appeal rights. The original form should be sent to the Field Office for filing in the debtor's case file and a copy should be attached to the debtor's settlement rejection letter.

### **D. Notify the IRS and Credit Agencies [7 CFR 3550.252(e)]**

In accordance with the requirements of the IRS, the Servicing Office must report to the IRS debts that have been settled. *IRS Form 1099-C, Cancellation of Debt* is used to report any debt (principal balance and any administrative costs) settled through cancellation, compromise, or adjustment. After reporting the debt to the IRS, no further efforts to collect the debt should be made. Credit reporting agencies also must be notified of debt settlement actions.

## **7.18 DISPOSITION OF PROMISSORY NOTES AND RELEASE OF SECURITY INSTRUMENTS**

When the debt is satisfied through any of the debt settlement mechanisms, the Field Office must generate the appropriate satisfaction and/or release letter.

If the debtor requested the settlement, the Field Office should indicate on the note the method by which it was satisfied and return it to the debtor, along with the satisfaction and/or release letter and the mortgage.

If the debtor did not request settlement and the Agency chooses to cancel the debt, the satisfaction letter should be sent to the Field Office and retained in the debtor's case file. In cases of cancellation or chargeoff, the note will not be returned to the debtor.

## GLOSSARY

**Acceleration.** Demand for immediate repayment of the entire balance of a debt if the security instruments are breached.

**Actual net recovery value.** The amount the Agency in fact does recover from the sale of a property after accounting for all costs.

**Adequate housing.** A dwelling that provides complete plumbing and adequate heating; is structurally sound; is not overcrowded; and does not contain health or safety hazards.

**Adjusted income.** Used to determine whether an applicant is income-eligible. Adjusted income is based on annual income and provides for deductions to account for varying household circumstances and expenses.

**Adjustment.** An agreement to release a debtor from liability generally upon receipt of an initial lump sum representing the maximum amount the debtor can afford to pay and periodic additional payments over a period of up to 5 years.

**Administrator.** The official of the Rural Housing Service within the Rural Development mission area (or official of its successor agency) delegated authority by the Secretary of the U.S. Department of Agriculture to administer the Agency and its programs.

**Adverse decision.** An administrative decision made by an officer, employee or committee of the Agency that has a negative impact on the applicant or borrower.

**Affordable Housing Product.** Any form of participating funds which have limited restrictions and repayment terms. These can include subordinate liens, grants, silent mortgages, forgivable loans and community land trusts.

**Agency.** The Rural Housing Service within the Rural Development mission area of the U.S. Department of Agriculture or its successor agency, which administers Section 502 loans and Section 504 loans and grants.

**Allowable excess costs.** The cost of the appraisal fee, tax service fee, homeownership education fee, and initial contribution to the escrow account. These costs can be financed even if they cause the total loan amount to exceed the area loan limit or the property's market value.

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

**Annual Income.** Used to determine an applicant's eligibility for assistance. All amounts, monetary or not, of the applicant's household not specifically excluded by regulations, and amounts derived from assets any members of the family have access to.

**Applicant.** An adult member of the household who will be responsible for repayment of the loan.

**Assumption.** The procedure whereby the transferee becomes liable for all or part of the debt of the transferor. An assumption may be at the same rates and terms or at new rates and terms, depending on the circumstances.

**Best mortgage obtainable.** In cases when the borrower is delinquent and the loan is unsecured, the Agency will attempt to obtain the best security position possible to secure repayment of the delinquency.

**Borrower.** A recipient who is indebted under the Section 502 or 504 programs.

**Cancellation.** A decision to cease collection activities and release the debtor from personal liability for any remaining amounts owed.

**Case File.** A file established for each application to contain all documents used for loan origination.

**Servicing and Asset Management Office (Servicing Office).** The Agency branch located in St. Louis, Missouri that is responsible for servicing Section 502 and 504 loans.

**Closing costs.** Various fees required to conclude a real estate transaction.

**Compromise.** An agreement to release a debtor from liability upon receipt of a specified lump sum that is less than the total amount due.

**Cosigner.** An individual or entity that joins in the execution of a promissory note to compensate for any deficiency in the applicant's repayment ability. The cosigner becomes jointly liable to comply with the terms of the promissory note in the event of the borrower's default, but is not entitled to any interest in the security or borrower rights.

**Cross-collateralized loan.** A situation in which a single property secures both Agency and Farm Service Agency (FSA) loans.

**Custodial property.** Borrower-owned real property that serves as security for a loan that has been taken into possession by the Agency to protect Government's interest.

**Daily simple interest.** A method of establishing borrower payments based on daily interest charged on the outstanding principal balance of the loan. Principal is reduced by the amount of payment in excess of the accrued interest.

**Debt instrument.** A collective term encompassing obligating documents for a loan, including any applicable promissory note, assumption agreement, or a grant agreement.

**Debt settlement.** Actions undertaken to collect at least a portion of debt owed to the Agency in conjunction with a voluntary liquidation, forced liquidation, or after the debt is fully matured. Debt settlement, when complete, closes the account.

**Dedicated Loan Origination and Servicing System (DLOS).** The overall automated system used by the Agency for originating and servicing loans, which includes UniFi and MortgageServ. It is designed to expedite loan making, standardize information collection and record keeping, and facilitate communication between the Field Office and Servicing Office.

**Deed in lieu of foreclosure.** A method of liquidation by which title to the security property is conveyed to the Agency by the borrower.

**Deferred mortgage payments.** A subsidy available to eligible, very low-income borrowers of up to 25 percent of their principal and interest payments at 1 percent for up to 15 years. The deferred amounts are subject to recapture on sale or nonoccupancy.

**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.

**Deficiency judgment.** A personal judgment against a debtor for the amount remaining due after foreclosure.

**Delinquency workout agreement.** An agreement establishing a new repayment plan for a borrower who has delinquent Agency debt.

**Disability (individual with a).** Any person who has a physical or mental impairment that substantially limits one or more major life activities, has a record of such an impairment, or is regarded as having such an impairment.

**Do Not Pay portal.** The Department of Treasury's DNP portal was announced through a Presidential Memorandum dated June 18, 2010. At a minimum and before payment and award, the Presidential Memorandum and the Improper Payments Elimination and Recovery Improvement Act of 2012 requires a check of the following five databases: 1) Social Security Administration's Death Master File, 2) General Services Administration's Excluded Parties List System, 3) Department of the Treasury's Debt Check Database of the Department of the Treasury, 4) Department of Housing and Urban Development's Credit Alert System, and 5) Department of Health and Human Services, Office of the Inspector General's List of Excluded Individuals/Entities. The DNP portal allows users to check the above databases required by the law using a single-entry point web-based application.

**Due Diligence.** The process of inquiring into the environmental condition of real estate in the context of a real estate transaction to determine the presence of contamination from hazardous substances, hazardous wastes, and petroleum products, and what impact such contamination may have on the market value of the property.

**Easement.** The legal right to use land, or a portion of land, owned by another for a limited purpose.

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

- A. A person who is the head, spouse, or sole member of a family and who is 62 years of age or older, or who is disabled, and is an applicant or borrower; or
- B. 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
- C. In the case of a family where the deceased borrower or spouse was at least 62 years old or disabled, surviving household members shall continue to be classified as an elderly family for the purpose of determining adjusted income, even though the surviving members may not meet the definition of elderly family on their own, provided:
  - 1. They occupied the dwelling with the deceased family member at the time of the death;
  - 2. If one of the surviving family members is the spouse of the deceased family member, the family shall be classified as an elderly family only until the remarriage of the surviving spouse; and
  - 3. At the time of the death of the deceased family member, the dwelling was financed under title V of the Housing Act of 1949.

**Environmental review.** An analysis of the potential for environmental impacts from a proposed action by the Agency and an examination of alternatives to avoid or minimize adverse impacts on the environment.

**Equivalent interest rate (EIR).** The interest rate charged by the Agency to program borrowers who receive payment assistance via method 1. The interest rate varies according to the borrower's income.

**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.

**Estimated net recovery value.** The amount that the Agency could expect to recover from a property if it was liquidated after considering all costs associated with liquidating, holding, and selling the property.

**False information.** Information that the recipient knew was incorrect or should have known was incorrect that was provided or omitted for the purposes of obtaining assistance for which the recipient was not eligible.

**Fee simple ownership.** A form of ownership under which the owner has absolute title to a piece of property.

**Field Office.** An Agency office that originates loans.

**Floor payment.** A minimum amount that the borrower must pay for Principal, Interest, Taxes, and Insurance (PITI) when payment assistance method 1 is used. The payment amount is determined by the borrower's adjusted income, and its relation to the applicable adjusted median income in the area in which the security property is located.

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

**Hazard.** A condition of the property that jeopardizes the health or safety of the occupants or members of the community, that does not make it unfit for habitation (see also the definition of major hazard).

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

**Housing Act of 1949, as amended.** The Act which provides the authority for the direct single family housing programs. It is codified at 42 U.S.C. 1471, et seq.

**HUD.** The U.S. Department of Housing and Urban Development.

**HUD high cost area.** An area defined by HUD as having high housing costs.

**Inaccurate information.** Incorrect information inadvertently provided, used, or omitted without intent to obtain benefits for which the applicant was not eligible.

**Indian reservation.** All land located within the limits of any Indian reservation under the jurisdiction of the United States notwithstanding the issuance of any patent and including rights-of-way running through the reservation; trust or restricted land located within the boundaries of a former reservation of a Federally recognized Indian tribe in the State of Oklahoma; or all Indian allotments, the titles to which have not been extinguished if such allotments are subject to the jurisdiction of a Federally recognized Indian tribe.

**Interest credit.** A payment subsidy available to certain eligible Section 502 borrowers that reduces the effective interest rate of the loan. Borrowers receiving interest credit will continue to receive it on all current and future loans for as long as they remain eligible for and continue to receive a subsidy. Borrowers who cease to be eligible for interest credit can never receive interest credit again, but may receive payment assistance method 2 if they again qualify for a payment subsidy.

**Junior lien.** A security instrument or a judgment against the security property to which the Agency debt instrument is superior.

**Legal alien.** For the purposes of these programs, legal alien refers to any person lawfully admitted to the country who meets the criteria in Section 214 of the Housing and Community Development Act of 1980, as amended, 42 U.S.C. 1436a.

**Leveraged loan.** An affordable housing product loan or grant to an Agency borrower property, closed simultaneously with an RHS loan. Affordable leveraged loans are characterized by long term (not less than 30 years), amortized payments with a note interest rate equal to or less than 3 percent.

**Liquidation.** A forced sale or voluntary disposition of the security property to obtain funds to repay outstanding debt. The proceeds from the sale are given to leinholders in order of priority, with any remaining funds returned to the borrower.

**Live-in aide.** A person who lives with an elderly person 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.

**Loan Approval Official.** An Agency employee who has the authority to approve loans. Unless otherwise indicated, each State Director may determine which approval actions may be made by the Loan Approval Official, and which must come to the State Office for approval.

**Loan docket.** The legal documents and forms developed during loan origination that must be provided to Servicing Office for servicing purposes.

**Loan Originator.** An Agency employee who works with the loan applicant, conducts the basic underwriting analysis, and makes the loan approval or credit denial recommendation to the Loan Approval Official.

**Loan-to-Value (LTV) Ratio.** LTV ratio is the relationship between the amount to be financed and the market value of the security property.

**Lockbox.** The service that receives and processes borrower payments.



**Loss draft.** A payment from an insurance company to a borrower to cover the borrower's adjusted losses due to damages covered under the insurance policy.

**Low income.** An adjusted income developed in consultation with HUD under 42 U.S.C. 1437a(b)(2)(D)

**Major hazard.** A condition so severe that it makes the property unfit for habitation. (See also the definition of hazard.)

**Market value.** The value of the property as determined by a current appraisal; the Agency may authorize the use of a Broker's Price Opinion (BPO) or similar instrument to determine market value in limited servicing situations.

**Mineral lease.** A granting of rights to a third party to mine, drill or otherwise access oil, gas or other valuable natural resources on a property.

**Minor.** Any individual under 18 years of age, except that a recipient or spouse may never be considered a minor.

**Moderate income.** An adjusted income that does not exceed the moderate income limit for the guaranteed single family housing loan program authorized by Section 502(h) of the Housing Act of 1949, as amended

**Modest housing.** A property that is considered modest for the area, with a market value that does not exceed the applicable area loan limit as established by RHS in accordance with §3550.63. In addition, the property must not be designed for income producing activities nor have an in ground swimming pool.

**Moratorium.** A period of up to two years during which scheduled payments for principal, interest and deposits to the escrow account are not required, but are subject to repayment at a later date.

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

**MortgageServ.** The mainframe-based computer application that is used by the Field Office to electronically communicate with, and transmit information to SO, and by SO to service and track a borrower's loan.

**National Appeals Division (NAD).** The organization within the United States Department of Agriculture that is responsible for the Department's administrative appeals procedures which must be followed by participants who desire to appeal an adverse decision made by the Agency.

**National Office.** The headquarters of the Agency located in Washington, DC where the Administrator's office and the national policy-making staff are located.

**Net family assets.** The value of assets are available to a household that could be used towards housing costs. Net family assets are considered in the calculation of annual income and are used to determine whether the household must make additional cash contributions to improve or purchase the property.

**Net recovery value.** The market value of the security property minus anticipated expenses of liquidation, acquisition, and sale as determined by the Agency.

**Nonprogram interest rate.** The interest rate offered by the Agency for loans made on nonprogram terms.

**Nonprogram property.** Property that does not meet the program's requirements.

**Nonprogram terms.** Credit terms available from the Agency when the applicant or property is not program-eligible.

**Note only loan.** See "unsecured loan."

**Note rate.** See "promissory note rate."

**Offset.** Deductions to pay a debt owed to the Agency from a borrower's retirement benefits, salary, income tax refund, or payments from other Federal agencies to the borrower. Deductions from retirement benefits and salary generally apply only to current and former Federal employees.

**Partial release of security.** An action by the Agency under which it releases a portion of the security property from the security instrument.

**Participant.** For the purpose of reviews and appeals, a participant is any individual or entity who has applied for or whose right to participate in or receive a payment, loan, or other benefit is affected by an Agency decision.

**Payment assistance.** A payment subsidy available to eligible Section 502 borrowers that reduces the effective interest rate of a loan.

**Payment moratorium.** A period of up to 2 years during which scheduled payments for principal, interest and deposits to the escrow account are not required, but are subject to repayment at a later date.

**Payment subsidy.** A general term for subsidies which reduce the borrower's scheduled payment. It refers to either payment assistance method 1 or 2, or interest credit.

**Person with a disability.** Any person who has a physical or mental impairment that substantially limits on 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 paid by the borrower for principal, interest, taxes, and insurance, divided by repayment income.

**Principal reduction attributable to subsidy (PRAS).** Accelerated principal reduction that may occur when a borrower receives a reduced interest rate through interest credit assistance.

**Prior lien.** A security instrument or a judgment against the security property that is superior to the Agency's debt instrument.

**Program-eligible applicant.** Any applicant meeting the eligibility requirements of the Section 502 or Section 504 programs.

**Program-eligible property.** A property eligible to be financed under the Section 502 or Section 504 programs.

**Program terms.** Credit terms that are available only to program-eligible applicants for program-eligible properties.

**Promissory note rate.** The unsubsidized interest rate offered by the Agency for loans made on program terms.

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

**Protective advances.** Costs incurred by the Agency to protect the security interest of the Government that are charged to the borrower's account.

**Real Estate Owned (REO).** Property for which the Agency holds title (formerly known by the Agency as "inventory property").

**Real estate taxes.** Taxes and the annual portion of assessments estimated to be due and payable on the property, reduced by any available tax exemption.

**Reamortization.** The establishment of a new, revised schedule of equal monthly payments of principal and interest over the remaining term of a mortgage loan.

**Recapture amount.** An amount of subsidy to be repaid by the borrower upon disposition or nonoccupancy of the property.

**Recipient.** An individual who has received an Agency loan or grant.

**Refinancing with private credit.** An Agency requirement under which program borrowers who appear to qualify for private credit must seek such credit (formerly known by the Agency as “graduation”).

**Repayment income.** Used to determine whether an applicant has the ability to make monthly loan payments. Repayment income is based only on the income attributable to parties to the note and includes some income sources excluded for the purpose of adjusted income.

**Rural area.** The definition of “rural area” is found in section 520 of the Housing Act of 1949, as amended.

**Scheduled payment.** The monthly or annual installment on a promissory note plus escrow (if required), as modified by any payment subsidy agreement, delinquency workout agreement, other documented agreements between the Agency and the borrower, or protective advances.

**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 satisfy the debt (see also “unsecured loan”).

**Security instrument.** The written instrument that legally records the Agency’s security interest in the property.

**Security property.** All the property that serves as collateral for an Agency loan.

**Servicing and Asset Management Office (Servicing Office).** The Agency branch located in St. Louis, Missouri that is responsible for servicing Section 502 and 504 loans.

**Special Flood Hazard Area (SFHA).** An area having special flood, mudslide and/or flood related erosion hazards as shown on Federal Emergency Management Agency (FEMA) floodplain maps.

**State Director.** The highest Agency decision making official at the State level.

**State Supplement.** Additional guidance provided by the State Director when State, local or tribal laws affect how Agency requirements are implemented in a particular State.

**Subordination.** Moving a lien position to a lower priority.

**Subsequent loans.** Additional Agency credit that is extended to an existing program borrower.

**Subsidy.** Interest credit, payment assistance method 1, payment assistance method 2, or deferred mortgage assistance received by a borrower under the Section 502 program.

**Subsidy repayment agreement.** An agreement under which a borrower agrees to repay to the Agency any subsidy received under the Section 502 program upon disposition or nonoccupancy of the security property.

**Supervised funds.** Funds deposited in an Agency supervised bank account on behalf of a borrower.

**Tax service.** A contractor hired by the Agency to secure tax information about borrower properties.

**Temporarily absent.** A person is considered temporarily absent from a household for reasons such as seasonal or migratory employment, military callup, hospitalization.

**Total debt ratio.** The amount paid by the borrower for principal, interest, taxes, and insurance and any recurring monthly debt, divided by repayment income.

**Tribal allotted land.** Tribal land allotted to individual tribal members which is held in trust.

**Tribe.** Any Federally-recognized tribe, band, pueblo, group, community, or nation of Indians or Alaska natives.

**Trust land.** Land held in trust by the United States on behalf of an Indian tribe.

**Unauthorized assistance.** Any loan, payment subsidy, deferred mortgage payment, or grant for which there was no regulatory authorization or for which the recipient was not eligible.

**UniFi.** A personal computer-based application located in each Field Office that is used by Loan Originators. It retains applicant information, calculates maximum loan amounts, and generates loan approval and closing forms.

**United States (U.S.) citizen.** An individual who resides as a U.S. 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 Marinas, the Federated States of Micronesia, the Republic of Palau, or the Republic of the Marshall Islands.

**USDA.** The United States Department of Agriculture.

**Unsecured loan.** A loan, also known as a “note only loan,” evidenced only by the borrower’s promissory note (see also “secured loan”).

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

**Very low income.** An adjusted income limit developed in consultation with HUD under 42 U.S.C. 1437a(b)(2)(D).

**Veterans preference.** A preference extended to any person applying for a loan or grant under the Section 502 or Section 504 programs who was honorably discharged or released on conditions other than dishonorable conduct from the active forces of the United States Army, Navy, Air Force, Marine Corps, or Coast Guard and who served in active duty during one of the following periods:

- A. April 6, 1917 through March 31, 1921;
- B. December 7, 1941 through December 31, 1946;
- C. June 27, 1950 through January 31, 1955;
- D. A period of more than 180 days, any part of which occurred after January 31, 1955, but on or before May 7, 1975; or
- E. During the period beginning August 2, 1990, and ending the date prescribed by Presidential Proclamation or law.

The ***family*** of a service person who died in service during any of the periods listed above is also extended the preference.

Appendix 1

7 CFR PART 3550 - DIRECT SINGLE FAMILY HOUSING LOANS AND GRANTS

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## 7 CFR PART 3550 - DIRECT SINGLE FAMILY HOUSING LOANS AND GRANTS

### Subpart A - General

#### § 3550.1 Applicability.

This part sets forth policies for the direct single family housing loan programs operated by the Rural Housing Service (RHS) of the U.S. Department of Agriculture (USDA). It addresses the requirements of sections 502 and 504 of the Housing Act of 1949, as amended, and includes policies regarding both loan and grant origination and servicing. Procedures for implementing these regulations can be found in program handbooks, available in any Rural Development office. Any provision on the expenditure of funds under this part is contingent upon the availability of funds.

#### § 3550.2 Purpose.

The purpose of the direct RHS single family housing loan programs is to provide low- and very low-income people who will live in rural areas with an opportunity to own adequate but modest, decent, safe, and sanitary dwellings and related facilities. The section 502 program offers persons who do not currently own adequate housing, and who cannot obtain other credit, the opportunity to acquire, build, rehabilitate, improve, or relocate dwellings in rural areas. The section 504 program offers loans to very low-income homeowners who cannot obtain other credit to repair or rehabilitate their properties. The section 504 program also offers grants to homeowners age 62 or older who cannot obtain a loan to correct health and safety hazards or to make the unit accessible to household members with disabilities.

#### § 3550.3 Civil rights.

RHS will administer its programs fairly, and in accordance with both the letter and the spirit of all equal opportunity and fair housing legislation and applicable executive orders. Loans, grants, 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, physical or mental disability, receipt of income from public assistance, 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), Executive Order 11246, and Executive Order 11063, as amended by Executive Order 12259, as applicable. The civil rights compliance requirements for RHS are in 7 CFR part 1901, subpart E. The nondiscrimination requirements also originate from the Equal Credit Opportunity Act (ECOA), 15 USC 1601 as amended and its Regulation B, 12 CFR 202, as amended.

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### § 3550.4 Reviews and appeals.

Whenever RHS makes a decision that is adverse to a participant, RHS will provide the participant with written notice of such adverse decision and the participant's rights to a USDA National Appeals Division hearing in accordance with 7 CFR part 11. Any adverse decision, whether appealable or non-appealable may be reviewed by the next-level RHS supervisor.

### § 3550.5 Environmental requirements.

(a) Policy. RHS will consider environmental quality as equal with economic, social, and other relevant factors in program development and decision-making processes. RHS will take into account potential environmental impacts of proposed projects by working with RHS applicants, other federal agencies, 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. Processing or servicing actions taken under this part must comply with the environmental review requirements in accordance with 7 CFR part 1970, and 7 CFR part 1924, which addresses lead-based paint.

### § 3550.6 State law or state supplement.

State and local laws and regulations, and the laws of federally recognized Indian tribes, may affect RHS implementation of certain provisions of this regulation, for example, with respect to the treatment of liens, construction, or environmental policies. Supplemental guidance may be issued in the case of any conflict or significant differences.

### § 3550.7 Demonstration programs.

From time to time, RHS may authorize limited demonstration programs. The purpose of these demonstration programs is to test new approaches to offering housing under the statutory authority granted to the Secretary. Therefore, such demonstration programs may not be consistent with some of the provisions contained in this part. However, any program requirements that are statutory will remain in effect. Demonstration programs will be clearly identified as such.

### § 3550.8 Exception authority.

An RHS official may request, and the Administrator or designee may make, an exception to any requirement or provision of this part or address any omission of this part that is consistent with the applicable statute if 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.

§ 3550.9 Conflict of interest.

(a) Objective. It is the objective of RHS to maintain the highest standards of honesty, integrity, and impartiality by employees. To reduce the potential for employee conflict of interest, all processing, approval, servicing, or review activity will be conducted in accordance with 7 CFR part 1900, subpart D by RHS employees who:

- (1) Are not themselves the applicant or borrower;
- (2) Are not members of the family or close known relatives of the applicant or borrower;
- (3) Do not have an immediate working relationship with the applicant or borrower, the employee related to the applicant or borrower, or the employee who would normally conduct the activity; or
- (4) Do not have a business or close personal association with the applicant or borrower.

(b) Applicant or borrower responsibility. The applicant or borrower must disclose any known relationship or association with an RHS employee when such information is requested.

(c) RHS employee responsibility. An RHS employee must disclose any known relationship or association with a recipient, regardless of whether the relationship or association is known to others. RHS employees or members of their families may not purchase a Real Estate Owned (REO) property, security property from a borrower, or security property at a foreclosure sale. Loan closing agents who have been involved with a particular property, as well as members of their families, are also precluded from purchasing such properties.

§ 3550.10 Definitions.

Acceleration. Demand for immediate repayment of the entire balance of a debt if the security instruments are breached.

Adjusted income. Used to determine whether an applicant is income-eligible. Adjusted income provides for deductions to account for varying household circumstances and expenses. See § 3550.54 for a complete description of adjusted income.

Adjustment. An agreement to release a debtor from liability generally upon receipt of an initial lump sum representing the maximum amount the debtor can afford to pay and periodic additional payments over a period of up to 5 years.

Agency-approved intermediary. An affordable housing nonprofit, public agency, or State Housing Finance Agency approved by RHS to perform quality assurance reviews on packages prepared by Agency-certified loan application packagers through their qualified employers. See § 3550.75 for further details.

Agency-certified loan application packager. An individual certified by RHS under this subpart to package section 502 loan applications while employed (either as an employee or as an independent contractor) by a qualified employer. See § 3550.75 for further details.

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.

Applicant. An adult member of the household who will be responsible for repayment of the loan.

Assumption. The procedure whereby the transferee becomes liable for all or part of the debt of the transferor.

Borrower. A recipient who is indebted under the section 502 or 504 programs.

Cancellation. A decision to cease collection activities and release the debtor from personal liability for any remaining amounts owed.

Compromise. An agreement to release a debtor from liability upon receipt of a specified lump sum that is less than the total amount due.

Conditional commitment. A determination that a proposed dwelling will qualify as a program-eligible property. The conditional commitment does not reserve funds, nor does it ensure that a program-eligible applicant will be available to buy the dwelling.

Cosigner. An individual or an entity that joins in the execution of a promissory note to compensate for any deficiency in the applicant's repayment ability. The cosigner becomes jointly liable to comply with the terms of the promissory note in the event of the borrower's default, but is not entitled to any interest in the security or borrower rights.

Cross-collateralized loan. A situation in which a single property secures both RHS and Farm Service Agency loans.

Custodial property. Borrower-owned real property that serves as security for a loan that has been taken into possession by the Agency to protect the Government's interest.

Daily simple interest. A method of establishing borrower payments based on daily interest charged on the outstanding principal balance of the loan. Principal is reduced by the amount of payment in excess of the accrued interest.

## § 3550.10 (Con.)

Dealer-contractor. A person, firm, partnership, or corporation in the business of selling and servicing manufactured homes and developing sites for manufactured homes. A person, firm, partnership, or corporation not capable of providing the complete service is not eligible to be a dealer-contractor.

Debt instrument. A collective term encompassing obligating documents for a loan, including any applicable promissory note, assumption agreement, or grant agreement.

Deferred mortgage payments. A subsidy available to eligible, very low-income borrowers of up to 25 percent of their principal and interest payments at 1 percent for up to 15 years. The deferred amounts are subject to recapture on sale or nonoccupancy.

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.

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

- (1) A person who is the head, spouse, or sole member of a family 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 1 of whom is age 62 or older, or disabled, and who is an applicant or borrower; or
- (3) In the case of a family where the deceased borrower or spouse was at least 62 years old or disabled, the surviving household member shall continue to be classified as an elderly family for the purpose of determining adjusted income, even though the surviving members may not meet the definition of elderly family on their own, *provided*:
  - (i) They occupied the dwelling with the deceased family member at the time of the death;
  - (ii) If one of the surviving family members is the spouse of the deceased family member, the family shall be classified as an elderly family only until the remarriage of the surviving spouse; and
  - (iii) At the time of the death of the deceased family member, the dwelling was financed under title V of the Housing Act of 1949, as amended.

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 or unit. A dwelling that has either been previously owner-occupied or has been completed for more than 1 year as evidenced by an occupancy permit, certificate of occupancy or similar document issued by the local authority.

False information. Information that the recipient knew was incorrect or should have known was incorrect that was provided or omitted for the purposes of obtaining assistance for which the recipient was not eligible.

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

Hazard. A condition of the property that jeopardizes the health or safety of the occupants or members of the community, that does not make it unfit for habitation. (See also the definition of major hazard in this section.)

Household. All persons expected to be living in the dwelling, except for live-in aids, foster children, and foster adults.

Housing Act of 1949, as amended. The Act which provides the authority for the direct single family housing programs. It is codified at 42 U.S.C. 1471, et seq.

HUD. The U.S. Department of Housing and Urban Development.

Inaccurate information. Incorrect information inadvertently provided, used, or omitted without the intent to obtain benefits for which the recipient was not eligible.

Indian reservation. All land located within the limits of any Indian reservation under the jurisdiction of the United States notwithstanding the issuance of any patent and including rights-of-way running through the reservation; trust or restricted land located within the boundaries of a former reservation of a federally recognized Indian tribe in the State of Oklahoma; or all Indian allotments, the titles to which have not been extinguished, if such allotments are subject to the jurisdiction of a federally recognized Indian tribe.

Interest credit. A payment subsidy available to certain eligible section 502 borrowers that reduces the effective interest rate of a loan (see § 3550.68(d)). Borrowers receiving interest credit will continue to receive it on all current and future loans for as long as they remain eligible for and continue to receive a subsidy. Borrowers who cease to be eligible for interest credit can never receive interest credit again, but may receive payment assistance if they again qualify for a payment subsidy.

Junior lien. A security instrument or a judgment against the security property to which the RHS debt instrument is superior.

Legal alien. For the purposes of this part, legal alien refers to any person lawfully admitted to the country who meets the criteria in section 214 of the Housing and Community Development Act of 1980, 42 U.S.C. 1436a.

Leveraged loan. An affordable housing product loan or grant to an Agency borrower property, closed simultaneously with an RHS loan. Affordable leveraged loans are characterized by long term (not less than 30 years), amortized payments with a note interest rate equal to or less than 3 percent.

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 limit developed in consultation with HUD under 42 U.S.C. 1437a(b)(2)(D).

Major hazard. A condition so severe that it makes the property unfit for habitation. (See also the definition of hazard in this section.)

Manufactured home. A structure that is built to Federally Manufactured Home Construction and Safety Standards and RHS Thermal Performance Standards. It is transportable in 1 or more sections, which in the traveling mode is 10-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, RHS may authorize the use of a Broker's Price Opinion or similar instrument to determine market value in limited servicing situations.

Mobile home. A manufactured unit often referred to as a "trailer," designed to be used as a dwelling, but built prior to the enactment of the Housing and Community Development Act of 1980 (Pub. L. 96-399) enacted October 8, 1980.

Moderate income. An adjusted income that does not exceed the moderate income limit for the guaranteed single family housing loan program authorized by Section 502(h) of the Housing Act of 1949, as amended.

Modest housing. A property that is considered modest for the area, with a market value that does not exceed the applicable maximum loan limit as established by RHS in accordance with §3550.63. In addition, the property must not be designed for income producing activities nor have an in-ground swimming pool.

Modular or panelized home. Housing, constructed of one or more factory-built sections or panels, which, when completed, meets or exceeds the requirements of the recognized development standards (model building codes) for site built housing, and which is designed to be permanently connected to a site-built foundation.

Moratorium. A period of up to 2 years during which scheduled payments are not required, but are subject to repayment at a later date.

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

National average area loan limit. Across the nation, the average area loan limit as specified in § 3550.63 (a). The national average is considered when determining the maximum packaging fee permitted under the certified loan application packaging process under the section 502 program.

Net family assets. The value of assets available to a household that could be used towards housing costs. Net family assets are considered in the calculation of annual income and are used to determine whether the household must make additional cash contributions to improve or purchase the property.

Net recovery value. The market value of the security property minus anticipated expenses of liquidation, acquisition, and sale as determined by RHS.

New dwelling or unit. A dwelling that is to be constructed, or a dwelling that is less than 1 year old as evidenced by an occupancy permit, certificate of occupancy or similar document issued by the local authority and has never been occupied.

Nonprogram (NP) interest rate. The interest rate offered by RHS for loans made on NP terms.

NP property. Property that does not meet the program eligibility requirements outlined in §§ 3550.56 and 3550.57.

NP terms. Credit terms available from RHS when the applicant or property is not program-eligible.

Offset. Deductions to pay a debt owed to RHS from a borrower's retirement benefits, salary, income tax refund, or payments from other federal agencies to the borrower. Deductions from retirement benefits and salary generally apply only to current and former federal employees.

Participant. For the purpose of reviews and appeals, a participant is any individual or entity who has applied for, or whose right to participate in or receive a payment, loan, or other benefit is affected by an RHS decision.



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Payment assistance. A payment subsidy available to eligible section 502 borrowers that reduces the effective interest rate of a loan (see § 3550.68(c)). Borrowers eligible for a payment subsidy receive payment assistance unless they are currently eligible for and receive interest credit. There are two methods of payment assistance. Payment Assistance Method 1 is found at §3550.68(c)(2). Payment Assistance Method 2 is found at §3550.68(c)(1).

Payment subsidy. A general term for subsidies which reduce the borrower's scheduled payment. It refers to either payment assistance or interest credit.

Person with 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 paid by the borrower for principal, interest, taxes, and insurance (PITI), divided by repayment income.

Principal reduction attributed to subsidy (PRAS). Accelerated principal reduction that can occur when a borrower receives a reduced interest rate through a payment subsidy.

Prior lien. A security instrument or a judgment against the security property that is superior to the RHS debt instrument.

Program-eligible applicant. Any applicant meeting the eligibility requirements described in §3550.53.

Program-eligible property. A property eligible to be financed under this part, as determined by the criteria listed in §§3550.56 through 3550.59.

Program terms. Credit terms that are available only to program-eligible applicants for program-eligible properties.

Property. The land, dwelling, and related facilities for which the applicant will use RHS assistance.

Protective advances. Costs incurred by the Agency to protect the security interest of the Government that are charged to the borrower's account.

Qualified employer. An affordable housing nonprofit organization, public agency, tribal housing authority, or State Housing Finance Agency that meets the requirements outlined in § 3550.75 (b)(2) and is involved in the certified loan application packaging process under the section 502 program.

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Real estate taxes. Taxes and the annual portion of assessments estimated to be due and payable on the property, reduced by any available tax exemption.

Recapture amount. An amount of subsidy to be repaid by the borrower upon disposition or nonoccupancy of the property.

Recipient. Any applicant, borrower, or grant recipient who applies for or receives assistance under the section 502 or 504 programs.

REO. The acronym for “Real Estate Owned.” It refers to property for which RHS holds title.

Repayment income. Used to determine whether an applicant has the ability to make monthly loan payments. Repayment income includes amounts excluded for the purpose of determining adjusted income. See § 3550.54 for a complete description.

RHS. The Rural Housing Service of the U.S. Department of Agriculture, or its successor agency, formerly the Rural Housing and Community Development Service (RHCDs), a successor agency to the Farmers Home Administration (FmHA).

RHS employee. Any employee of RHS, or any employee of the Rural Development mission area who carries out grant or loan origination or servicing functions for the section 502 or 504 programs.

RHS interest rate. The unsubsidized interest rate offered by RHS for loans made on program terms.

Rural area: An area defined in section 520 of the Housing Act of 1949, as amended.

Rural Development. A mission area within USDA which includes RHS, Rural Utilities Service (RUS), and Rural Business-Cooperative Service (RBS).

Scheduled payment. The monthly or annual installment on a promissory note plus escrow (if required), as modified by any payment subsidy agreement, delinquency workout agreement, other documented agreements between RHS and the borrower, or protective advances.

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 satisfy the debt.

Security property. All the property that serves as collateral for an RHS loan.

Subsidy. Interest credit, payment assistance, or deferred mortgage assistance received by a borrower under the section 502 or 504 programs.

Total debt ratio. The amount paid by the borrower for PITI and any recurring monthly debt, divided by repayment income.

Unauthorized assistance. Any loan, payment subsidy, deferred mortgage payment, or grant for which there was no regulatory authorization or for which the recipient was not eligible.

U.S. 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.

Unsecured loan. A loan evidenced only by the borrower's promissory note.

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

Very low income. An adjusted income limit developed in consultation with HUD under 42 U.S.C. 1437a(b)(2)(D)..

Veterans preference. A preference extended to any person applying for a loan or grant 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 serviceperson, or the family of a deceased serviceperson who died in service before the termination of such war or such period or era. The applicable timeframes 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.

§ 3550.11 State Director Assessment of Homeowner Education.

(a) State Director's will make an assessment of the availability of certified homeowner education in their respective states and maintain an annually updated listing of providers and their reasonable costs.

(b)The order of preference for homeowner education formats is as follows:

- (1) Classroom; one-on-one counseling; or interactive video conference.
- (2) If none of the formats in paragraph (b)(1) of this section is reasonably available; as determined under §3550.53, then the applicant may use interactive home-study or interactive telephone counseling of at least four hours duration.

§ 3550.11 (b) (Con.)

(3) If none of the formats in paragraphs (b)(1) and (b)(2) of this section is reasonably available as determined under § 3550.53, then the applicant may use on-line counseling to meet the homeownership education requirement.

(c) Homeownership education must include a letter or certificate of completion and be provided by homeownership education counselors that are certified by any of the following:

- (1) The Department of Housing and Urban Development (HUD);
- (2) NeighborWorks America (NWA);
- (3) The National Federation of Housing Counselors (NFHC) ;
- (4) National American Indian Housing Council (NAIHC); or
- (5) The State Housing Finance Agency or other qualified organization approved by the State Director.

(d) The provider will issue a letter or certificate of completion to document that the borrower has satisfactory knowledge of these minimum topics:

- (1) Preparing for homeownership (evaluate readiness to go from rental to homeownership),
- (2) Budgeting (pre and post-purchase),
- (3) Credit counseling,
- (4) Shopping for a home,
- (5) Lender differences (predatory lending),
- (6) Obtaining a mortgage (mortgage process, different types of mortgages),
- (7) Loan closing (closing process, documentation, closing costs),
- (8) Post-occupancy counseling (delinquency and foreclosure prevention),
- (9) Life as a homeowner (homeowner warranties, maintenance and repairs).

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(e) The provider may tailor the homeownership education training to the needs of the borrower to ensure satisfactory knowledge of the topics listed in paragraph (d) of this section.

§§ 3550.12 - 3550.49 [Reserved]

§ 3550.50 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0172. Public reporting burden for this collection of information is estimated to vary from 5 minutes to 3 hours per response, with an average of 1 1/2 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. You are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Subpart B - Section 502 Origination

§ 3550.51 Program objectives.

Section 502 of the Housing Act of 1949, as amended authorizes the Rural Housing Service (RHS) to provide financing to help low- and very low-income persons who cannot obtain credit from other sources obtain adequate housing in rural areas. Resources for the section 502 program are limited, and therefore, applicants are required to use section 502 funds in conjunction with funding or financing from other sources, if feasible. Sections 3550.52 through 3550.73 set forth the requirements for originating loans on program terms. Section 3550.74 describes the differences for originating loans on nonprogram (NP) terms.

§ 3550.52 Loan purposes.

Section 502 funds may be used to buy, build, rehabilitate, improve, or relocate an eligible dwelling and provide related facilities for use by the borrower as a permanent residence. In limited circumstances section 502 funds may be used to refinance existing debt.

(a) Purchases from existing RHS borrowers. To purchase a property currently financed by an RHS loan, the new borrower must assume the existing RHS indebtedness. Section 502 funds may be used to provide additional financing or make repairs. Loan funds also may be used to permit a remaining borrower to purchase the equity of a departing co-borrower.

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(b) Refinancing non-RHS loans. Debt from an existing non-RHS loan may be refinanced if the existing debt is secured by a lien against the property, RHS will have a first lien position on the security property after refinancing, and:

(1) In the case of loans for existing dwellings, if:

(i) Due to circumstances beyond the applicant's control, the applicant is in danger of losing the property, the debt is over \$5,000 and the debt was incurred for eligible program purposes prior to loan application or was a protective advance made by the mortgagee for items covered by the loan to be refinanced, including accrued interest, insurance premiums, real estate tax advances, or preliminary foreclosure costs; or

(ii) If a loan of \$5,000 or more is necessary for repairs to correct major deficiencies and make the dwelling decent, safe and sanitary and refinancing is necessary for the borrower to show repayment ability, regardless of the delinquency.

(2) In the case of loans for a building site without a dwelling, 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) The RHS loan will include funds to construct an appropriate dwelling on the site for the applicant's use.

(3) Debts incurred after the date of RHS loan application but before closing may be refinanced if the costs are incurred for eligible loan purposes and any construction work conforms to the standards specified in this part.

(c) Refinancing RHS debt. Under limited circumstances, an existing RHS loan may be refinanced in accordance with § 3550.204 to allow the borrower to receive payment assistance.

(d) Eligible costs. Improvements financed with loan funds must be on land which, after closing, is part of the security property. In addition to acquisition, construction, repairs, or the cost of relocating a dwelling, loan funds may be used to pay for:

(1) Reasonable expenses related to obtaining the loan, including legal, architectural and engineering, technical, title clearance, and loan closing fees; and appraisal, surveying, environmental, tax monitoring, and other technical services; and personal liability insurance fees for Mutual Self-Help borrowers.

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- (2) The cost of providing 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 liable and which are not paid from other funds.
- (4) Reasonable and customary lender charges and fees if the RHS loan is being made in combination with a leveraged loan.
- (5) 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.
- (6) Packaging fees resulting from the certified loan application packaging process outlined in § 3550.75. The fee may not exceed two percent of the national average area loan limit as determined by the Agency and may be limited further at the Agency's discretion. Nominal packaging fees not resulting from the certified loan application process are an eligible cost provided the fee is no more than \$350; the loan application packager is a nonprofit, tax exempt partner that received an exception to all or part of the requirements outlined in § 3550.75 from the applicable Rural Development State Director; and the packager gathers and submits the information needed for the Agency to determine if the applicant is preliminarily eligible along with a fully completed and signed uniform residential loan application.
- (7) Purchasing and installing essential equipment in the dwelling, including ranges, refrigerators, washers or dryers, if these items are normally sold with dwellings in the area and if the purchase of these items is not the primary purpose of the loans.
- (8) Purchasing and installing approved energy savings measures and approved furnaces and space heaters that use fuel that is commonly used, economical, and dependably available.
- (9) Providing site preparation, including grading, foundation plantings, seeding or sodding, trees, walks, yard fences, and driveways to a building site.
- (10) Reasonable fees for homeownership education as determined by the State Director under §3550.11 of this subpart. Such fees may be added to the loan amount in excess of the area loan limit and appraised value of the house.



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(e) Loan restrictions. Loan funds may not be used to:

- (1) Purchase an existing manufactured home, or for any other purposes prohibited in § 3550.73(b).
- (2) Purchase or improve income-producing land or buildings to be used principally for income-producing purposes.
- (2) Pay fees, commissions, or charges to for-profit entities related to loan packaging or referral of prospective applicants to RHS.

§ 3550.53 Eligibility requirements.

(a) Income eligibility. At the time of loan approval, the household's adjusted income must not exceed the applicable low-income limit for the area, and at closing, must not exceed the applicable moderate-income limit for the area (see § 3550.54).

(b) Citizenship status. The applicant must be a United States citizen or a noncitizen who qualifies as a legal alien as defined in § 3550.10.

(c) Primary residence. Applicants must agree to and have the ability to occupy the dwelling on a permanent basis.

- (1) Because of the probability of transfer, loans will not be approved for military personnel on active duty unless the applicant will be discharged within a reasonable period of time.
- (2) Because of the probability of moves after graduation, loans will not be approved for a full-time student unless the applicant intends to make the home a permanent residence and there are reasonable prospects that employment will be available in the area after graduation.
- (3) If the home is being constructed or renovated an adult member of the household must be available to make inspections and authorize progress payments as the dwelling is being constructed.

(d) Eligibility of current homeowners. Current homeowners are not eligible for initial loans except as follows:

(1) Current homeowners may receive RHS loan funds to:

- (i) refinance an existing loan under the conditions outlined in § 3550.52(b);
- (ii) purchase a new dwelling if the current dwelling is deficient housing as defined in § 3550.10; or
- (iii) make necessary repairs to the property which is financed with an affordable non-RHS loan.

(2) Current homeowners with an RHS loan may receive a subsequent loan.

(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. Applications from applicants who have been suspended or debarred from participation in federal programs will be handled in accordance with 2 CFR parts 180 and 417.

(g) Repayment ability. Repayment ability means applicants must demonstrate adequate and dependably available income. The determination of income dependability will include consideration of the applicant's past history of annual income.

(1) A very low-income applicant is considered to have 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) A low-income applicant is considered to have repayment ability when the monthly amount required for payment of PITI does not exceed 33 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 repayment income.

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(3) Repayment ratios may exceed the percentages specified in paragraphs (h)(1) and (h)(2) of this section if the applicant has demonstrated an ability to meet higher debt obligations, or if RHS determines, based on other compensating factors, that the household has a higher repayment ability.

(4) If an applicant does not meet the repayment ability requirements, the applicant can have another party join the application as a cosigner.

(5) If an applicant does not meet the repayment ability requirements, the applicant can have other household members join the application.

(h) Credit qualifications. Applicants must be unable to secure the necessary credit from other sources on terms and conditions that the applicant could reasonably be expected to fulfill. Applicants must have a credit history that indicates reasonable ability and willingness to meet debt obligations. An applicant with an outstanding judgment obtained by the United States in a federal court, other than the United States Tax Court, is not eligible for a loan or grant from RHS.

(1) Indicators of unacceptable credit include:

(i) Payments on any account where the amount of the delinquency exceeded one installment for more than 30 days within the last 12 months.

(ii) Payments on any account which was delinquent for more than 30 days on two or more occasions within a 12-month period.

(iii) A foreclosure which has been completed within the last 36 months.

(iv) An outstanding Internal Revenue Service tax lien or any other outstanding tax liens with no satisfactory arrangement for payment.

(v) 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.

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(vi) Two or more rent payments paid 30 or more days late within the last 2 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 if the RHS loan will reduce shelter costs significantly and contribute to an improved repayment ability.

(vii) 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.

(viii) Non-agency debts written off within the last 36 months unless paid in full at least 12 months ago.

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

(x) Delinquency on a federal debt.

(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.

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

(3) When an application is rejected because of unacceptable credit, the applicant will be informed of the reason and source of information.

(i) Homeownership education. Applicants who are first-time homebuyers must agree to provide documentation, in the form of a completion certificate or letter from the provider, that a homeownership education course from a certified provider under § 3550.11 has been successfully completed as defined by the provider prior to loan closing. Requests for exceptions to the homeowner education requirement will be reviewed and granted on an individual case-by-case basis. The State Director may grant an exception the homeownership education requirement for individuals in geographic areas within the State where the State Director verifies that certified homeownership education is not reasonably available in the local area in any of the formats listed in § 3550.11(b). Whether such homeownership education is reasonably available will be determined based on factors including, but not limited to: distance, travel time, geographic obstacles, and cost. On a case-by-case basis, the State Director also may grant an exception, provided the applicant borrower documents a special need, such as a disability, that would unduly impede completing a homeownership course in a reasonably available format.

§ 3550.54 Calculation of income and assets.

(a) Repayment income. Repayment income is the annual amount of income from all sources that are expected to be received by those household members who are parties to the promissory note, except for any student financial aid received by these household members for tuition, fees, books, equipment, materials, and transportation. Repayment income is used to determine the household's ability to repay a loan.

(b) Annual income. Annual income is the income of all household members from all sources except those listed in (b)(1) through (b)(12) of this section:

- (1) earned income of persons under the age of 18 unless they are a borrower 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 section 501(b)(5) of the Housing Act of 1949, as amended,
- (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 section 501(b)(5) of the Housing Act of 1949, as amended,
- (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 for section 502 and 504 and the amount of payment subsidy for which the household qualifies under section 502. 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) For each household 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 determined pursuant to section 501(b)(5) of the Housing Act of 1949, as amended.

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

(i) enable a family member to 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 earned by the family member enabled to work.

(3) Expenses related to the care of household members with disabilities that:

(i) enable a family member to work,

(ii) are not reimbursed from insurance or another source, and

(iii) are in excess of three percent of the household's annual income.

(4) For any elderly family, a deduction in the amount determined pursuant to section 501(b)(5) of the Housing Act of 1949, as amended.

(5) For elderly households 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 three 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. Net family assets also are considered in determining whether a down payment is required.

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(1) Net family assets include, but are not limited to:

- (i) equity in real property or other capital investments, 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 without retiring or terminating employment,
- (v) lump sum receipts such as lottery winnings, capital gains, inheritances, and
- (vi) personal property held as an investment.

(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);
- (vi) the value of an irrevocable trust fund or any other trust over which no member of the household has control;
- (vii) cash value of life insurance policies;
- (viii) the value of tax advantaged college savings plans (529 plan, Coverdell Educations Savings Account, etc.);
- (ix) the value of tax advantaged health or medical savings or spending accounts; and
- (x) other amounts deemed by the Agency not to constitute net family assets.

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§ 3550.55 Applications.

(a) Application submissions. All persons applying for RHS loans must file a complete written application in a format specified by RHS. Applications will be accepted even when funds are not available.

(b) Application processing.

(1) Incomplete applications will be returned to the applicant specifying in writing the additional information that is needed to make the application complete.

(2) An applicant may voluntarily withdraw an application at any time.

(3) RHS may periodically request in writing that applicants reconfirm their interest in obtaining a loan. RHS may withdraw the application of any applicant who does not respond within the specified timeframe.

(4) Applicants who are eligible will be notified in writing. If additional information becomes available that indicates that the original eligibility determination may have been incorrect, or that circumstances have changed, RHS may reconsider the application and the applicant may be required to submit additional information.

(5) Applicants who are ineligible will be notified in writing and provided with the specific reasons for the rejection.

(c) Selection for processing. When funding is not sufficient to serve all program-eligible applicants, applications will be selected for processing using the funding priorities specified in this paragraph. Within priority categories, applications will be processed in the order that the completed applications are received. In the case of applications with equivalent priority status that are received on the same day, preference will be extended to applicants qualifying for a veterans preference. After selection for processing, loans are funded on a first-come, first-served basis.



§ 3550.55 (c) (Con.)

- (1) First priority will be given to existing customers who request subsequent loans to correct health and safety hazards.
  - (2) Second priority will be given to loans related to the sale of an REO property or the transfer of an existing RHS financed property.
  - (3) Third priority will be given to applicants facing housing related hardships including applicants who have been living in deficient housing for more than 6 months, current homeowners in danger of losing a property through foreclosure, and other circumstances determined by RHS on a case-by-case basis to constitute a hardship.
  - (4) Fourth priority will be given to applicants seeking, loans for the construction of dwellings in an RHS-approved Mutual Self-Help project or loans that will leverage funding or financing from other sources.
  - (5) Applications from applicants who do not qualify for priority consideration in paragraphs (c)(1), (2), (3), or (4) of this section will be selected for processing after all applications with priority status have been processed. The Administrator may temporarily reclassify applications received through the certified loan application packaging process as fourth priority when determined appropriate.
- (d) Applicant timeframe. RHS will specify a reasonable timeframe within which eligible applicants selected for processing must provide the information needed to underwrite the loan.

§ 3550.56 Site requirements.

- (a) Rural areas. Loans may be made only in rural areas designated by RHS. If an area designation is changed to non-rural:
- (1) New conditional commitments will be made and existing conditional commitments will be honored only in conjunction with an applicant for a section 502 loan who applied for assistance before the area designation changed.

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§ 3550.56 (a)(Con.)

(2) REO property sales and transfers with assumption may be processed.

(3) Subsequent loans may be made either in conjunction with a transfer with assumption of an RHS loan or to repair properties that have RHS loans.

(b) Site standards. Sites must be developed in accordance with 7 CFR part 1924, subpart C and any applicable standards imposed by a State or local government.

(1) The site must not be large enough to subdivide into more than one site under existing local zoning ordinances,

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

(3) The value of the site must not exceed 30 percent of the “as improved” market value of the property. The State Director may waive the 30 percent requirement in high cost areas where other lenders permit a higher percentage.

§ 3550.57 Dwelling requirements.

(a) Modest dwelling. The property must be one that is considered modest for the area, must not be designed for income providing purposes, must not have an in-ground swimming pool or have a market value in excess of the applicable maximum loan limit, in accordance with §3550.63, unless RHS authorizes an exception under this paragraph. An exception may be granted on a case-by-case basis to accommodate the specific needs of an applicant, such as to serve exceptionally large households or to provide reasonable accommodation for a household member with a disability. Any additional loan amount approved must not exceed the amount required to address the specific need.

(b) New dwellings. Construction must meet the requirements in 7 CFR part 1924, subpart A.

(c) Existing dwellings. Existing dwellings must be structurally sound; functionally adequate; in good repair, or to be placed in good repair with loan funds; have adequate electrical, heating, plumbing, water, and wastewater disposal systems; and be free of termites and other wood damaging pests and organisms.

§ 3550.58 Ownership requirements.

After the loan is closed, the borrower must have an acceptable 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. A written lease is required. To be acceptable, a leasehold interest must have an unexpired term that is at least 150 percent of the term of the mortgage, unless the loan is guaranteed, in which case the unexpired term of the lease must be at least 2 years longer than the loan term. In no case may the unexpired term be less than 25 years.
- (c) Life estate interest. To be acceptable a life estate interest must provide the borrower with rights of present possession, control, and beneficial use of the property. Generally, persons with any remainder interests must be signatories to the mortgage. All of the remainder interests need not be included in the mortgage to the extent that one or more of the persons holding remainder interests are not legally competent (and there is no representative who can legally consent to the mortgage), cannot be located, or if the remainder interests are divided among such a large number of people that it is not practical to obtain the signatures of all of the remainder interests. In such cases, the loan may not exceed the value of the property interests owned by the persons executing the mortgage.
- (d) Undivided interest. All legally competent co-owners will be required to sign the mortgage. When one or more of the co-owners are not legally competent (and there is no representative who can legally consent to the mortgage), cannot be located, or the ownership interests are divided among so large a number of co-owners that it is not practical for all of their interests to be mortgaged, their interests not exceeding 50 percent may be excluded from the security requirements. In such cases, the loan may not exceed the value of the property interests owned by the persons executing the mortgage.
- (e) Possessory rights. Acceptable forms of ownership include possessory rights on an American Indian reservation or State-owned land and the interest of an American Indian in land held in severalty under trust patents or deeds containing restrictions against alienation, provided that land in trust or restricted status will remain in trust or restricted status.

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### § 3550.59 Security requirements.

Before approving any loan, RHS will impose requirements to secure its interests.

(a) Adequate security. A loan will be considered adequately secured only when all of the following requirements are met:

(1) RHS obtains at closing a mortgage on all ownership interests in the security property or the requirements of § 3550.58 are satisfied.

(2) No liens prior to the RHS mortgage exist at the time of closing and no junior liens are likely to be taken immediately subsequent to or at the time of closing, unless the other liens are taken as part of a leveraging strategy or the RHS loan is essential for repairs and the senior lien secures an affordable non-RHS loan. Liens junior to the RHS lien may be allowed at loan closing if the junior lien will not interfere with the purpose or repayment of the RHS loan. When the junior lien involves a grant or a forgivable affordable housing product, the total debt may exceed the market value by the amount of the forgivable loan or grant up to 5 percent.

(3) The provisions of 7 CFR part 1927, subpart B regarding title clearance and the use of legal services have been followed.

(4) Existing and proposed property improvements are totally on the site and do not encroach on adjoining property.

(b) Guaranteed payment. Mortgage insurance guaranteeing payment from a Government agency or Indian tribe is adequate security.

### § 3550.60 Escrow account.

RHS may require that customers deposit into an escrow account amounts necessary to ensure that the account will contain sufficient funds to pay real estate taxes, hazard and flood insurance premiums, and other related costs when they are due in accordance with the Real Estate Settlement and Procedures Act (RESPA) of 1974 (12 U.S.C. 2601, et seq.) and section 501(e) of the Housing Act of 1949, as amended.

§ 3550.61 Insurance.

(a) Borrower responsibility. Any borrower with a secured indebtedness in excess of \$15,000 at the time of loan approval must furnish and continually maintain hazard insurance on the security property, with companies, in amounts, and on terms and conditions acceptable to RHS including a "loss payable clause" payable to RHS to protect the Government's interest.

(b) Amount. The borrower is required to insure the dwelling and any other essential buildings in an amount equal to the insurable value of the dwelling and other essential buildings. However, in cases where the borrower's outstanding secured indebtedness is less than the insurable value of the dwelling and other essential buildings, the borrower may elect a lower coverage provided it is not less than the outstanding secured indebtedness. If the borrower fails, or is unable, to insure the secured property, RHS will force place insurance and charge the cost to the borrower's account. Force place insurance only provides insurance coverage to the Agency and does not provide any direct coverage or benefit to the borrower. The amount of the lender-placed coverage generally will be the property's last known insured value.

(c) Flood insurance. Flood insurance must be obtained and maintained for the life of the loan for all property located in a Special Flood Hazard Area (SFHA) as determined by the Federal Emergency Management Agency (FEMA). RHS actions will be consistent with 7 CFR part 1806, subpart B which addressed flood insurance requirements. If flood insurance through FEMA's National Flood Insurance Program is not available in an SFHA, the property is not eligible for federal financial assistance.

(d) Losses.

(1) Loss deductible clauses for required insurance coverage may not exceed the generally accepted minimums based on current industry standards and local market conditions.

(2) Customers must immediately notify RHS of any loss or damage to insured property and collect the amount of the loss from the insurance company.

(3) Depending on the amount of the loss, RHS may require that loss payments be supervised. All repairs and replacements done by or under the direction of the borrower, or by contract, will be planned, performed, inspected, and paid for in accordance with 7 CFR part 1924, subpart A.

(4) When insurance funds remain after all repairs, replacements, and other authorized disbursements have been made, the funds will be applied in the following order:

(i) Prior liens, including delinquent property taxes.

(ii) Past-due amounts.

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(iii) Protective advances due.

(iv) Released to the customer if the RHS debt is adequately secured.

(5) If a loss occurs when insurance is not in force, the borrower is responsible for making the needed repairs or replacements and ensuring that the insurance is reinstated on the property.

(6) If the borrower is not financially able to make the repairs, RHS may take one of the following actions:

(i) Make a subsequent loan for repairs.

(ii) Subordinate the RHS lien to permit the borrower to obtain funds for needed repairs from another source.

(iii) Permit the borrower to obtain funds secured by a junior lien from another source.

(iv) Make a protective advance to protect the Government's interest.

(v) Accelerate the account.

§ 3550.62 Appraisals.

(a) Requirement. An appraisal is required when the debt to be secured exceeds \$15,000 or whenever RHS determines that it is necessary to establish the adequacy of the security. Appraisals must be made in accordance with the Uniform Standards of Professional Appraisal Practices. When other real estate is taken as additional security, it will be appraised if it represents a substantial portion of the security for the loan.

(b) Fees. RHS will charge a fee for each loan application that requires an appraisal, except the appraisal fee is not required on appraisals done for subsequent loans needed to make minimal, essential repairs or in cases where another party provides an appraisal which is acceptable to RHS. Fees collected in connection with a dwelling constructed under an approved conditional commitment will be paid to the contractor at closing to offset the cost of the real estate appraisal that is included in the conditional commitment fee.

§ 3550.63 Maximum loan limit.

Total secured indebtedness must not exceed the area loan limit or market value limitations specified in paragraphs (a) or (b) of this section, whichever is lower. Any loan amount for the RHS appraisal, tax monitoring fee, and the charge to establish an escrow account for taxes and insurance will not be subject to the limitations specified below. This section does not apply to loans on NP terms.

## § 3550.63 (Con.)

(a) Area loan limit. (1) The area loan limit is the maximum value of the property RHS will finance in a given locality. This limit is based on a percentage(s) of the applicable local HUD section 203(b) limit. The percentage(s) will be determined by the Agency and published in the program handbook. The area loan limits will be reviewed at least annually and posted to the Agency website.

(2) The maximum loan limit calculated under paragraph (a)(1) will be reduced in the following situations:

(i) When the applicant owns the site or is purchasing the site at a sales price below market value, the market value of the lot will be deducted from the maximum loan limit, and

(ii) When an applicant is receiving a housing grant or other form of affordable housing assistance for purposes other than closing costs, the amount(s) of such grants and affordable housing assistance will be deducted from the maximum loan limit.

(3) The maximum loan limit for self-help housing will be calculated by adding the total of the market value of the lot (including reasonable and typical costs of site development), the cost of construction, and the value of sweat equity. The total of these three factors cannot exceed the limit established in paragraph (a)(1) of this section.

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(b) Market value limitation.

- (1) The market value limitation is 100 percent of market value for existing housing and for new dwellings for which RHS will receive adequate documentation of construction quality and the source of such documentation is acceptable to RHS.
- (2) The market value limitation is 90 percent of market value for new dwellings for which adequate documentation of construction quality is not available.
- (3) The market value limitation can be increased by:
  - (i) Up to one percent, if RHS makes a subsequent loan for closing costs only, in conjunction with the sale of an REO property or an assumption.
  - (ii) The amount necessary to make a subsequent loan for repairs necessary to protect the Government's interest, and reasonable closing costs.
  - (iii) The amount necessary to refinance an existing borrower's RHS loans, plus closing costs associated with the new loan.

§ 3550.64 Down payment.

Elderly families must use any net family assets in excess of \$20,000 towards a down payment on the property. Non-elderly families must use net family assets in excess of \$15,000 towards a down payment on the property. Applicants may contribute assets in addition to the required down payment to further reduce the amount to be financed.

§ 3550.65 [Reserved]

§ 3550.66 Interest rate.

Loans will be written using the applicable RHS interest rate in effect at loan approval or loan closing, whichever is lower. Information about current interest rates is available in any Rural Development office.

§ 3550.67 Repayment period.

Loans will be scheduled for repayment over a period that does not exceed the expected useful life of the property as a dwelling. The loan repayment period will not exceed:

- (a) Thirty-three years in all cases except as noted in paragraphs (b), (c), and (d) of this section.



## § 3550.67 (Con.)

## (b) Thirty-eight years:

(1) For initial loans, or subsequent loans made in conjunction with an assumption, if the applicant's adjusted income does not exceed 60 percent of the area adjusted median income and the longer term is necessary to show repayment ability.

(2) For subsequent loans not made in conjunction with an assumption if the applicant's initial loan was for a period of 38 years, the applicant's adjusted income at the time the subsequent loan is approved does not exceed 60 percent of area adjusted median income, and the longer terms is necessary to show repayment ability.

(c) Ten years for loans not exceeding \$2,500.

(d) Thirty years for manufactured homes.

§ 3550.68 Payment subsidies.

RHS administers three types of payment subsidies: interest credit, payment assistance method 1 and payment assistance method 2. Payment subsidies are subject to recapture when the borrower transfers title or ceases to occupy the property.

(a) Eligibility for payment subsidy.

(1) Applicants or borrowers who receive loans on program terms are eligible to receive payment subsidy if they personally occupy the property and have adjusted income at or below the applicable moderate-income limit.

(2) Payment subsidy may be granted for initial loans or subsequent loans made in conjunction with an assumption only if the term of the loan is at least 25 years or more.

(3) Payment subsidy may be granted for subsequent loans not made in conjunction with an assumption if the initial loan was for a term of 25 years or more.

(b) Determining type of payment subsidy.

(1) A borrower currently receiving interest credit will continue to receive it for the initial loan and for any subsequent loan for as long as the borrower is eligible for and remains on interest credit.

(2) If a borrower receiving payment assistance using payment assistance method 1 receives a subsequent loan, payment assistance method 2 will be used to calculate the subsidy for the initial loan and subsequent loan. .

(3) A borrower who has never received payment subsidy, or who has stopped receiving interest credit or payment assistance method 1, and at a later date again qualifies for a payment subsidy, will receive payment assistance method 2.

(4) A borrower may not opt to change payment assistance methods.

(c) Calculation of payment assistance. Regardless of the method used, payment assistance may not exceed the amount necessary if the loan were amortized at an interest rate of 1 percent.

(1) Payment Assistance Method 2. The amount of payment assistance granted is the lesser of the difference between:

(i) The annualized promissory note installments for the combined RHS loan and eligible leveraged loans plus the cost of taxes and insurance less 24 percent of the borrower's adjusted income, or

(ii) The annualized promissory note installments for the RHS loan less the amount the borrower would pay if the loan were amortized at an interest rate of 1 percent.

(2) Payment Assistance Method 1. The amount of payment assistance granted is the difference between the installment due on the promissory note and the greater of the payment amortized at the equivalent interest rate or the payment calculated based on the required floor payment. In leveraging situations, the equivalent interest rate will be used.

(i) The floor payment, which is defined as a minimum percentage of adjusted income that the borrower must pay for PITI: 22 percent for very low-income borrowers, 24 percent for low-income borrowers with adjusted income below 65 percent of area adjusted median, and 26 percent for low-income borrowers with adjusted incomes between 65 and 80 percent of area adjusted median; or

(ii) The annualized note rate installment and the payment at the equivalent interest rate, which is determined by a comparison of the borrower's adjusted income to the adjusted median income for the area in which the security property is located. The following chart is used to determine the equivalent interest rate.

## § 3550.68 (c)(2) (Con.)

## PERCENTAGE OF MEDIAN INCOME AND THE EQUIVALENT INTEREST RATE

When the applicant's adjusted income is:

Equal to	BUT	THEN the equivalent
or more than:	less than:	interest rate is*
00 %	50.01 of adjusted median income	1 %
50.01 %	55 of adjusted median income	2 %
55 %	60 of adjusted median income	3 %
60 %	65 of adjusted median income	4 %
65 %	70 of adjusted median income	5 %
70 %	75 of adjusted median income	6 %
75 %	80.01 of adjusted median income	6.5%
80.01 %	90 of adjusted median income	7.5 %
90 %	100 of adjusted median income	8.5 %
100 %	110 % of adjusted median income	9 %
110 %	or more than adjusted median income	9.5 %

\* Or note rate, whichever is less; in no case will the equivalent interest rate be less than one percent.

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(d) Calculation of interest credit. The amount of interest credit granted is the difference between the sum of the annual installments due at the promissory note interest rate and the greater of:

- (1) Twenty percent of the borrower's adjusted income less the cost of real estate taxes and insurance, or
- (2) The amount the borrower would pay if the loan were amortized at an interest rate of one percent.

(e) Annual review. The borrower's income will be reviewed annually to determine whether the borrower is eligible for continued payment subsidy. The borrower must notify RHS whenever an adult member of the household changes or obtains employment, there is a change in household composition, or if income increases by at least 10 percent so that RHS can determine whether a review of the borrower's circumstances is required.

§ 3550.69 Deferred mortgage payments.

For qualified borrowers, RHS may defer up to 25 percent of the monthly principal and interest payment at 1 percent for up to 15 years. This assistance may be granted only at initial loan closing and is reviewed annually. Deferred mortgage payments are subject to recapture when the borrower transfers title or ceases to occupy the property.

(a) Eligibility. In order to qualify for deferred mortgage payments, all of the following must be true:

- (1) The applicant's adjusted income at the time of initial loan approval does not exceed the applicable very low-income limits.
- (2) The loan term is 38 years, or 30 years for a manufactured home.
- (3) The applicant's payments for principal and interest, calculated at a one percent interest rate for the maximum allowable term, plus estimated costs for taxes and insurance exceeds:
  - (i) For applicants receiving payment assistance, 29 percent of the applicant's repayment income by more than \$10 per month, or
  - (ii) For applicants receiving interest credit, 20 percent of adjusted income by more than \$10 per month.

## § 3550.69 (Con.)

(b) Amount and terms.

(1) The amount of the mortgage payment to be deferred will be the difference between the applicant's payment for principal and interest, calculated at one percent interest for the maximum allowable term, plus estimated costs for taxes and insurance and:

(i) For applicants receiving payment assistance, 29 percent of the applicant's repayment income.

(ii) For applicants receiving interest credit, 20 percent of adjusted income.

(2) Deferred mortgage payment agreements will be effective for a 12-month period.

(3) Deferred mortgage assistance may be continued for up to 15 years after loan closing. Once a borrower becomes ineligible for deferred mortgage assistance, the borrower can never again receive deferred mortgage assistance.

(c) Annual review. The borrower's income, taxes, and insurance will be reviewed annually to determine eligibility for continued deferred mortgage assistance. The borrower must notify RHS whenever an adult member of the household changes or obtains employment or if income increases by at least 10 percent so that RHS can determine whether a review of the borrower's circumstances is required.

§ 3550.70 Conditional commitments.

A conditional commitment is a determination by RHS that a dwelling offered for sale will be acceptable for purchase by a qualified RHS loan applicant if it is built or rehabilitated in accordance with RHS-approved plans, specifications, and regulations and priced within the lesser of the property's appraised value or the applicable maximum loan limit. The conditional commitment does not reserve funds, does not guarantee funding, and does not ensure that an eligible loan applicant will be available to buy the dwelling.

(a) Eligibility. To be eligible to request a conditional commitment, the builder, dealer-contractor, or seller must:

(1) Have an adequate ownership interest in the property, as defined in § 3550.58, prior to the beginning of any planned construction;

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- (2) Have the experience and ability to complete any proposed work in a competent and professional manner;
- (3) Have the legal capacity to enter into the required agreements;
- (4) Be financially responsible and have the ability to finance or obtain financing for any proposed construction or rehabilitation; and
- (5) Comply with the requirements of 7 CFR part 1901, subpart E and all applicable laws, regulations, and Executive Orders relating to equal opportunity. Anyone who receives 5 or more conditional commitments during a 12-month period must obtain RHS approval of an affirmative marketing plan.

(b) Limitations. Conditional commitments for new or substantially rehabilitated dwellings will not be issued after construction has started. RHS may limit the total number of conditional commitments issued in any locality based on market demand.

(c) Commitment period. A conditional commitment will be valid for 12 months from the date of issuance. The commitment may be extended for up to an additional 6 months if there are unexpected delays in construction caused by such factors as bad weather, materials shortages, or marketing difficulties. Conditional commitments may be canceled if construction does not begin within 60 days after the commitment is issued.

(d) Conditional commitments involving packaging of applications. A conditional commitment may be made to a seller, builder, or dealer-contractor who packages an RHS loan application for a prospective purchaser. In cases where the dwelling is to be constructed for sale to a specific eligible applicant, all of the following conditions must be met:

- (1) The conditional commitment will not be approved until the applicant's loan has been approved;
- (2) Construction will not begin until loan funds are obligated for the loan. Exceptions may be made when it appears likely that funding will be forthcoming and as long as the RHS lien priority is not jeopardized. The sales agreement must indicate that the loan has been approved but not funded and must provide that if the loan is not closed within 90 days of the date of approval, the contractor may terminate the sales agreement and sell the property to another party. If the sales agreement is terminated, the conditional commitment will be honored for another eligible loan applicant for the remaining period of the commitment; and
- (3) The RHS loan will be closed only after the dwelling is constructed or the required rehabilitation completed and final inspection has been made.

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(e) Fees. An application for a conditional commitment must include payment of the conditional commitment fee. The fee will be refunded if for any reason preliminary inspection of the property or investigation of the conditional commitment applicant indicates that a conditional commitment will not be issued. Application fees will not be refunded for any property on which the required appraisal has been made.

(f) Failure of conditional commitment applicant or dwelling to qualify. The conditional commitment applicant will be informed if the conditional commitment is denied. Conditional commitments will be canceled if the property does not meet program requirements.

(g) Changes in plans, specifications, or commitment price. The holder of the conditional commitment must request approval for changes in plans, specifications, and commitment price. RHS may approve the changes if the following requirements are met:

- (1) The property price does not exceed the maximum loan limit and increases in costs are due to factors beyond the control of the commitment holder, and
- (2) The requested changes are justifiable and appropriate.

(h) Builder's warranty. The builder or seller, as appropriate, must execute either an RHS-approved "Builder's Warranty," or provide a 10-year insured warranty when construction is completed or the loan is closed.

§ 3550.71 Special requirements for condominiums.

RHS loans may be made for condominium units under the following conditions:

(a) The unit is in a project approved or accepted by U.S. Department of Housing and Urban Development (HUD), the Federal National Mortgage Association (Fannie Mae), or the Federal Home Loan Mortgage Corporation (Freddie Mac).

(b) The condominium project complies with the requirements of the condominium enabling statute and all other applicable laws. Any right of first refusal in the condominium documents will not impair the rights of RHS to:

- (1) Foreclose or take title to a condominium unit pursuant to the remedies in the mortgage;
- (2) Accept a deed in lieu of foreclosure in the event of default by a mortgagor; and
- (3) Sell or lease a unit acquired by RHS.

(c) If RHS obtains title to a condominium unit pursuant to the remedies in its mortgage or through foreclosure, RHS will not be liable for more than 6 months of the unit's unpaid regularly budgeted dues or charges accrued before acquisition of the title to the unit by RHS. The homeowners association's lien priority may include costs of collecting unpaid dues.

(d) In case of condemnation or substantial loss to the units or common elements of the condominium project, unless at least two-thirds of the first mortgagees or unit owners of the individual condominium units have given their consent, the homeowners association may not:

(1) By act or omission seek to abandon or terminate the condominium project;

(2) Change the pro rata interest or obligations of any condominium unit in order to levy assessments or charges, allocate distribution of hazard insurance proceeds or condemnation awards, or determine the pro rata share of ownership of each condominium unit in the common elements;

(3) Partition or subdivide any condominium unit;

(4) Seek to abandon, partition, subdivide, encumber, sell, or transfer the common elements by act or omission (the granting of easements for public utilities or other public purposes consistent with the intended use of the common elements by the condominium project is not a transfer within the meaning of this clause); or

(5) Use hazard insurance proceeds for losses to any condominium property (whether units or common elements) for other than the repair, replacement, or reconstruction of the condominium property.

(e) All taxes, assessments, and charges that may become liens prior to the first mortgage under local law relate only to the individual condominium units and not to the condominium project as a whole.

(f) No provision of the condominium documents gives a condominium unit owner or any other party priority over any rights of RHS as first or second mortgagee of the condominium unit pursuant to its mortgage in the case of a payment to the unit owner of insurance proceeds or condemnation awards for losses to or taking of condominium units or common elements.

(g) If the condominium project is on a leasehold the underlying lease provides adequate security of tenure as described in § 3550.58(b).



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(h) At least 70 percent of the units have been sold. Multiple purchases of condominium units by one owner are counted as one sale when determining if the sales requirement has been met.

(i) No more than 15 percent of the unit owners are more than 1 month delinquent in payment of homeowners association dues or assessments at the time the RHS loan is closed.

§ 3550.72 Community land trusts.

Eligible dwellings located on land owned by a community land trust may be financed if:

(a) The loan meets all the requirements of this subpart, and

(b) Any restrictions, imposed by the community land trust on the property or applicant are:

(1) Reviewed and accepted by RHS before loan closing, and

(2) Automatically and permanently terminated upon foreclosure or acceptance by RHS of a deed in lieu of foreclosure.

§ 3550.73 Manufactured homes.

With the exception of the restrictions and additional requirements contained in this section, section 502 loans on manufactured homes are subject to the same conditions as all other section 502 loans.

(a) Eligible costs. In addition to the eligible costs described in § 3550.52(d), RHS may finance the following activities related to manufactured homes when a real estate mortgage covers both the unit and the site:

(1) Purchase of an eligible unit, transportation, and set-up costs, and purchase of an eligible site if not already owned by the applicant.

(2) Site development work in accordance with 7 CFR part 1924, subpart A.

(3) Subsequent loans in conjunction with an assumption or sale of an REO property, or

(4) Subsequent loans for repairs of units financed under section 502.

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(b) Loan restrictions. In addition to the loan restrictions described in § 3550.52(e), RHS may not use loan funds to finance:

- (1) An existing unit and site unless it is already financed with a section 502 loan or is an RHS REO property.
- (2) The purchase of a site without also financing the unit.
- (3) Alteration or remodeling of the unit when the initial loan is made.
- (4) Furniture, including movable articles of personal property such as drapes, beds, bedding, chairs, sofas, divans, lamps, tables, televisions, radios, stereo sets, and other similar items of personal property. Furniture does not include wall-to-wall carpeting, refrigerators, ovens, ranges, washing machines, clothes dryers, heating or cooling equipment, or other similar items.

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

(d) Loan term. The maximum term of a loan on a manufactured home is 30 years.

(e) Construction and development. Unit construction, site development and set-up must conform to the Federal Manufactured Home Construction and Safety Standards (FMHCSS) and 7 CFR part 1924, subpart A. Development under the Mutual Self-Help and borrower construction methods is not permitted for manufactured homes.

(f) Contract requirements. The dealer-contractor must sign a construction contract, as specified in 7 CFR § 1924.6 which will cover both the unit and site development work. The use of multi-contracts is prohibited. A dealer-contractor may use subcontractors if the dealer-contractor is solely responsible for all work under the contract. Payment for all work will be in accordance with 7 CFR part 1924, subpart A, except no payment will be made for materials or property stored on site (e.g., payment for a unit will be made only after it is permanently attached to the foundation).

(g) Lien release requirements. All persons furnishing materials or labor in connection with the contract except the manufacturer of the unit must sign a Release by Claimants document, as specified in 7 CFR part 1924, subpart A. The manufacturer of the unit must furnish an executed manufacturer's certificate of origin to verify that the unit is free and clear of all legal encumbrances.

## § 3550.73 (Con.)

(h) Warranty requirements. The dealer-contractor must provide a warranty in accordance with the provisions of 7 CFR § 1924.12. The warranty must identify the unit by serial number. The dealer-contractor must certify that the unit substantially complies with the plans and specifications and 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 dealer-contractor will also furnish the applicant with a copy of all manufacturer's warranties.

§ 3550.74 Nonprogram loans.

NP terms may be extended to applicants who do not qualify for program credit, or for properties that do not qualify as program properties, when it is in the best interest of the Government. NP loans are originated and serviced according to the requirements for program loans except as indicated in this section.

(a) Purpose. NP terms may be offered to expedite:

- (1) Sale of an REO property.
- (2) Assumption of an existing program loan on new rates and terms. If additional funds are required to purchase the property, the applicant must obtain them from another source.
- (3) Conversion of a program loan that has received unauthorized assistance.
- (4) Continuation of a loan on a portion of a security property when the remainder is being transferred and the RHS debt is not paid in full.

(b) Terms.

(1) Rate and term:

- (i) For an applicant who intends to occupy the property, the term will not exceed 30 years.
- (ii) For other applicants, the term will not exceed 10 years. If more favorable terms are necessary to facilitate the sale, the loan may be amortized over a period of up to 20 years with payment in full due not later than 10 years from the date of closing.

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(iii) An applicant with a NP loan under paragraph (b)(1)(i) of this section who wishes to retain the property and purchase a new property with RHS credit must purchase the second property according to the terms of paragraph (b)(1)(ii) of this section, even if the new property will serve as the applicant's principal residence.

(2) NP loans are written at the NP interest rate in effect at the time of loan approval.

(3) NP borrowers are not eligible for payment assistance or a moratorium.

(c) Additional requirements.

(1) NP applicants other than public bodies and nonprofit organizations must pay a nonrefundable application fee.

(2) NP applicants must make a down payment based upon the purchase price and whether the applicant intends to personally occupy the property or use it for other purposes.

(3) NP applicants cannot finance loan closing costs or escrow, tax service, or appraisal fees.

(d) Reduced restrictions.

(1) NP applicants need not be unable to obtain other credit in order to receive a NP loan and are not required to refinance with private credit when they are able to do so.

(2) NP applicants are not required to occupy the property.

(3) NP applicants are not subject to leasing restrictions.

(e) Waiver of costs. When the purpose of the loan is the conversion of a program loan that has received unauthorized assistance or continuation of a loan on a portion of a security property when the remainder is being transferred, the application fee, appraisal fee, and down payment may be waived.

§ 3550.75 Certified loan application packaging process.

Persons interested in applying for a section 502 loan may, but are not required to, submit an application through the certified loan application packaging process.

(a) General. The certified loan application packaging process involves individuals who have been designated as an Agency-certified loan application packager, their qualified employers, and, if required by the State Director, Agency-approved intermediaries.

## § 3550.75 (Con.)

(b) Process requirements. To package section 502 loan applications under this process, each of the following conditions must be met:

(1) Agency-certified loan application packager. An individual who wishes to acquire RHS certification as a loan application packager must meet all of the following conditions:

- (i) Have at least one year of affordable housing loan origination and/or affordable housing counseling experience;
- (ii) Be employed (either as an employee or as an independent contractor) by a qualified employer as outlined in paragraph (b)(2) of this section;
- (iii) Complete an Agency-approved loan application packaging course and successfully pass the corresponding test as specified in paragraph (c) of this section; and
- (iv) Submit applications to the Agency via an intermediary if determined necessary by a State Director.

(2) Qualified employer. Individuals who have been designated as an Agency-certified loan application packager must be employed (either as an employee or as an independent contractor) by a qualified employer. To be considered a qualified employer, the packager's employer must meet each of the conditions specified in paragraphs (b)(2)(i) through (v) of this section. Tribal housing authorities and the States' Housing Finance Agencies are eligible and are exempt from the conditions specified in paragraphs (b)(2)(i) through (ii) of this section.

- (i) Be a nonprofit organization or public agency in good standing in the State(s) of its operation.
- (ii) Be tax exempt under the Internal Revenue Code and be engaged in affordable housing per their regulations, articles of incorporation, or bylaws.
- (iii) Notify the Agency and the applicant if they or their Agency-certified packager(s) are the developer, builder, seller of, or have any other such financial interest in the property for which the application package is submitted. The Agency may disallow a particular qualified employer and/or Agency-certified packager from receiving part or all of a packaging fee if the Agency determines that the financial interest is improper or the qualified employer or Agency-certified packager has a history of improperly using its position when there has been a financial interest in the property.

(iv) Prepare an affirmative fair housing marketing plan for Agency approval as outlined in RD Instruction 1901-E (or in any superseding guidance provided in the impending RD Instruction 1940-D).

(v) Submit applications to the Agency via an intermediary if determined necessary by a State Director.

(3) Agency-approved intermediaries. To become an Agency-approved intermediary, an interested party must apply and demonstrate to the Agency's satisfaction that they meet each of the conditions specified below. The States' Housing Finance Agencies, however, are exempt from the conditions specified in paragraphs (b)(3)(i) through (v). After the initial application process, the Agency may require intermediaries to periodically demonstrate that they still meet the following criteria.

(i) Be a Section 501 (c)(3) nonprofit organization or public agency in good standing in the State(s) of its operation with the capacity to serve multiple qualified employers and their Agency-certified loan application packagers throughout an entire State or preferably throughout entire States and with the capacity to perform quality assurance reviews on a large volume of packaged loan applications within an acceptable period of time as determined by the Agency;

(ii) Be engaged in affordable housing in accordance with their regulations, articles of incorporation, or bylaws;

(iii) Be financially viable and demonstrate positive operating performance as evidenced by an independent audit paid for by the applicant seeking to be an intermediary;

(iv) Have at least five years of verifiable experience with the Agency's direct single family housing loan programs;

(v) Demonstrate that their quality assurance staff has experience with packaging, originating, or underwriting affordable housing loans.

(vi) Develop and implement quality control procedures designed to prevent submission of incomplete or ineligible application packages to the Agency;

(vii) Ensure that their quality assurance staff complete an Agency-approved loan application packaging course and successfully pass the corresponding test;

(viii) Not be the developer, builder, seller of, or have any other such financial interest in the property for which the application package is submitted; and

(ix) Provide supplemental training, technical assistance, and support to certified loan application packagers and qualified employers to promote quality standards and accountability; and to address areas for improvement and any changes in program guidance.

(c) Loan application packaging courses. Prospective loan application packagers must successfully complete an Agency-approved course that covers the material identified in paragraph (c)(1) of this section. Prospective intermediaries must also successfully complete an Agency-approved course as specified in paragraph (c)(2) of this section.

(1) Loan application packagers. At a minimum, the certification course for individuals who wish to become Agency-certified loan application packagers will provide:

(i) An in-depth review of the section 502 direct single family housing loan program and the regulations and laws that govern the program (including civil rights lending laws such as the Equal Credit Opportunity Act, Fair Housing Act, and Section 504 of the Rehabilitation Act of 1973);

(ii) A detailed discussion on the program's application process and borrower/property eligibility requirements;

(iii) An examination of the Agency's loan underwriting process which includes the use of payment subsidies; and

(iv) The roles and responsibilities of a loan application packager and the Agency staff.

(2) Intermediaries. The required course for an intermediary's quality assurance staff will cover the components described in paragraph (c)(1) of this section and other information relevant to undertaking quality assurance, technical assistance, and training functions in support of the qualified employers and their Agency-certified loan application packagers.

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(3) Non-Agency trainers. Prior to offering the required course to packagers and intermediaries, non-Agency trainers must obtain approval from designated Agency staff. Non-Agency trainers, who will generally be limited to housing nonprofit organizations but may in rare cases include public bodies such as public universities, must provide proof of relevant experience and resources for delivery; present evidence that their individual trainers are competent and knowledgeable on all subject areas; submit course materials for Agency review; agree to maintain attendance records, test results, and updated course materials; and bear the cost of providing the training though a reasonable tuition fee may be charged the course participants. The course content, schedule, and tuition must be approved by RHS and a designated Agency staff member will typically participate in each training session to ensure accuracy of the program information and to serve as a program resource. A list of eligible non-Agency trainers, which is subject to change based on non-Agency trainers' performance, will be published by the Agency.

(d) Confidentiality. The Agency-certified loan application packager, qualified employer, Agency-approved intermediary and their agents must safeguard each applicant's personal and financial information.

(e) Retaining designation. The Agency will meet with the Agency-certified loan application packager, their qualified employer, and Agency-approved intermediary (if applicable) at least annually to maintain open lines of communication; discuss their packaging activities; identify and resolve deficiencies in the packaging process; and stipulate any training requirements for retaining designation (including but not limited to civil rights refresher training).

(f) Revocation. The designation as an Agency-certified loan application packager or Agency-approved intermediary is subject to revocation by the Agency under any of the following conditions:

- (1) The rate of submitted packaged loan applications that receive RHS approval is below the acceptable limit as determined by the Agency;
- (2) The rate of submitted packaged loan applications from very low-income applicants is below the acceptable level as determined by the Agency;
- (3) Violation of applicable regulations, statutes and other guidance; or
- (4) No viable packaged loan applications are submitted to the Agency in any consecutive 12-month period.

§§ 3550.76 - 3550.99 [Reserved]



§ 3550.100 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0172. Public reporting burden for this collection of information is estimated to vary from 5 minutes to 3 hours per response, with an average of 1 1/2 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. You are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Subpart C - Section 504 Origination and Section 306C Water and Waste Disposal Grants

§ 3550.101 Program objectives.

This subpart sets forth policies for administering loans and grants under section 504(a) of title V of the Housing Act of 1949, as amended. Section 504 loans and grants are intended to help very low-income owner-occupants in rural areas repair their properties. This subpart also covers Water and Waste Disposal grants to individuals authorized by Section 306C(b) of the Consolidated Farm and Rural Development Act, (7 U.S.C. 1926c).

§ 3550.102 Grant and loan purposes.

(a) Grant funds. Grant funds may be used only to pay costs for repairs and improvements that will remove identified health and safety hazards or to repair or remodel dwellings to make them accessible and useable for household members with disabilities. Unused grant funds must be returned to the Rural Housing Service (RHS).

(b) Loan funds. Loan funds may be used to make general repairs and improvements to properties or to remove health and safety hazards, as long as the dwelling remains modest in size and design.

(c) Eligibility of mobile and manufactured homes. Repairs necessary to remove health and safety hazards may be made to mobile or manufactured homes provided:

- (1) The applicant owns the home and site and has occupied the home prior to filing an application with RHS, and
- (2) The mobile or manufactured home is on a permanent foundation or will be put on a permanent foundation with section 504 funds.

(d) Eligible costs. In addition to construction costs to make necessary repairs and improvements, loan and grant funds may be used for:

- (1) Reasonable expenses related to obtaining the loan or grant, including legal, architectural and engineering, title clearance, and loan closing fees; and appraisal, surveying, environmental, tax monitoring, and other technical services.
- (2) The cost of providing 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 installation costs for utilities such as water, sewer, electricity, and gas for which the borrower is liable and which are not paid from other funds.
- (4) 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) Fees to public and private nonprofit organizations that are tax exempt under the Internal Revenue Code for the development and packaging of applications.

(e) Restrictions on uses of loan or grant funds. Section 504 funds may not be used to:

- (1) Assist in the construction of a new dwelling.
- (2) Make repairs to a dwelling in such poor condition that when the repairs are completed, the dwelling will continue to have major hazards.
- (3) Move a mobile home or manufactured home from one site to another.
- (4) Pay for off-site improvements except for the necessary installation and assessment costs for utilities.
- (5) Refinance any debt or obligation of the applicant incurred before the date of application, except for the installation and assessment costs of utilities.
- (6) Pay fees, commission, or charges to for-profit entities related to loan packaging or referral of prospective applicants to RHS.

§ 3550.103 Eligibility requirements.

To be eligible, applicants must meet the following requirements:

(a) Owner-occupant. Applicants must own, as described in § 3550.107, and occupy the dwelling.

(b) Age (grant only). To be eligible for grant assistance, an applicant must be 62 years of age or older at the time of application.

(c) Income eligibility. At the time of loan or grant approval, the household's adjusted income must not exceed the applicable very low-income limit. Section 3550.54 provides a detailed discussion of the calculation of adjusted income.

(d) Citizenship status. The applicant must be a U.S. citizen or a non-citizen who qualifies as a legal alien, as defined in § 3550.10.

(e) Need and use of personal resources. Applicants must be unable to obtain financial assistance at reasonable terms and conditions from non-RHS credit or grant sources and lack the personal resources to meet their needs. In cases where the household is experiencing medical expenses in excess of three percent of the household's income, this requirement may be waived or modified. Elderly families must use any net family assets in excess of \$20,000 to reduce their section 504 request. Non-elderly families must use any net family assets in excess of \$15,000 to reduce their section 504 request. Applicants may contribute assets in excess of the aforementioned amounts to further reduce their request for assistance. The definition of assets for this purpose is net family assets as described in § 3550.54 of subpart B of this part, less the value of the dwelling and a minimum adequate site.

(f) Legal capacity. The applicant 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.

(g) Suspension or debarment. Applications from applicants who have been suspended or debarred from participation in federal programs will be handled in accordance with FmHA Instruction 1940-M (available in any Rural Development office).

(h) Repayment ability (loans only). Applicants must demonstrate adequate repayment ability as supported by a budget.

(1) If an applicant does not meet the repayment ability requirements, the applicant can have another party join the application as a cosigner.

(2) If an applicant does not meet the repayment ability requirements, the applicant can have other household members join the application.

(i) Credit qualifications. Applicants must be unable to secure the necessary credit from other sources under terms and conditions that the applicant could reasonably be expected to fulfill. Loan applicants must have a credit history that indicates reasonable ability and willingness to meet debt obligations. An applicant with an outstanding judgment obtained by the United States in a federal court, other than the United States Tax Court is not eligible for a loan or grant from RHS.

(1) Indicators of unacceptable credit include:

(i) Payments on any account where the amount of the delinquency exceeded one installment for more than 30 days within the last 12 months.

(ii) Payments on any account which was delinquent for more than 30 days on two or more occasions within a 12-month period.

(iii) Loss of security due to a foreclosure if the foreclosure has been completed within the last 36 months.

(iv) An outstanding Internal Revenue Service tax lien or any other outstanding tax liens with no satisfactory arrangement for payment.

(v) 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 by paragraphs (i)(2)(i) and (i)(2)(ii) of this section.

(vi) 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.

(vii) Non-agency debts written off within the last 36 months or paid in full at least 12 months ago.

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

(ix) Delinquency on a federal debt.

(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.

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

(3) When an application is rejected because of unacceptable credit, the applicant will be informed of the reason and source of information.

§ 3550.104 Applications.

(a) Application submissions. All persons applying for section 504 loans or grants must file a complete written application in a format specified by RHS. Applications will be accepted even when funds are not available.

(b) Application processing.

(1) Incomplete applications will be returned to the applicant specifying in writing the additional information that is needed to make the application complete.

(2) An applicant may voluntarily withdraw an application at any time.

(3) RHS may periodically request in writing that applicants reconfirm their interest in obtaining a loan or grant. RHS may withdraw the application of any applicant who does not respond within the specified timeframe.

(4) Applicants who are eligible will be notified in writing. If additional information becomes available that indicates that the original eligibility determination may have been in error or that circumstances have changed, RHS may reconsider the application and the applicant may be required to submit additional information.

(5) Applicants who are ineligible will be notified in writing and provided with the specific reasons for the rejection.

(c) Processing priorities. When funding is not sufficient to serve all eligible applicants, applications for assistance to remove health and safety hazards will receive priority for funding. In the case of applications with equivalent priority status that are received on the same day, preference will be extended to applicants qualifying for a veterans preference. After selection for processing, requests for assistance are funded on a first-come, first-served basis.

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### § 3550.105 Site requirements.

- (a) Rural areas. Loans may be made only in rural areas designated by RHS. If an area designation is changed to nonrural an existing RHS borrower may receive 504 assistance.
- (b) Not subdividable. The site must not be large enough to subdivide into more than one site under existing local zoning ordinances.

### § 3550.106 Dwelling requirements.

- (a) Modest dwelling. The property must be one that is considered modest for the area, must not be designed for income producing purposes, have an in-ground swimming pool, or have a market value in excess of the applicable maximum loan limit, in accordance with § 3550.63.
- (b) Post-repair condition. Dwellings repaired with section 504 funds need not be brought to the agency development standards of 7 CFR part 1924, subpart A, nor must all existing hazards be removed. However, the dwelling may not continue to have major health or safety hazards.
- (c) Construction standards. All work must be completed in accordance with local construction codes and standards. When potentially hazardous equipment or materials are being installed, all materials and installations must be in accordance with the applicable standards in 7 CFR part 1924, subpart A.

### § 3550.107 Ownership requirements.

The applicant must have an acceptable ownership interest in the property as evidenced by one of the following:

- (a) Full fee ownership. Acceptable full fee ownership is evidenced by a fully marketable title with a deed vesting a fee interest in the property to the applicant.
- (b) Secure leasehold interest. A written lease is required. For loans, the unexpired portion of the lease must not be less than 2 years beyond the term of the promissory note. For grants, the remaining lease period must be at least 5 years. A leasehold for mutual help housing financed by U.S. Department of Housing and Urban Development (HUD) on Indian lands requires no minimum lease period and constitutes acceptable ownership.

(c) Life estate interest. To be acceptable, a life estate interest must provide the applicant with rights of present possession, control, and beneficial use of the property. For secured loans, generally persons with any remainder interests must be signatories to the mortgage. All of the remainder interests need not be included in the mortgage to the extent that one or more of the persons holding remainder interests are not legally competent (and there is no representative who can legally consent to the mortgage), cannot be located, or if the remainder interests are divided among such a large number of people that it is not practical to obtain the signatures of all of the remainder interests. In such cases, the loan may not exceed the value of the property interests owned by the persons executing the mortgage.

(d) Undivided interest. An undivided interest is acceptable if there is no reason to believe that the applicant's position as an owner-occupant will be jeopardized as a result of the improvements to be made, and:

(1) In the case of unsecured loans or grants, if any co-owners living or planning to live in the dwelling sign the repayment agreement.

(2) In the case of a secured loan, when one or more of the co-owners are not legally competent (and there is no representative who can legally consent to the mortgage), cannot be located, or the ownership interests are divided among so large a number of co-owners that it is not practical for all of their interests to be mortgaged, their interests not exceeding 50 percent may be excluded from the security requirements. In such cases, the loan may not exceed the value of the property interests owned by the persons executing the mortgage.

(e) Possessory rights. Acceptable forms of ownership include possessory right on an American Indian reservation or State-owned land and the interest of an American Indian in land held severally under trust patents or deeds containing restrictions against alienation, provided that land in trust or restricted status will remain in trust or restricted status.

(f) Land purchase contract. A land purchase contract is acceptable if the applicant is current on all payments, and there is a reasonable likelihood that the applicant will be able to continue meeting the financial obligations of the contract.

(g) Alternative evidence of ownership. If evidence, as described in paragraphs (a) through (e) of this section, is not available, RHS may accept any of the following as evidence of ownership:

(1) Records of the local taxing authority that show the applicant as owner and that demonstrate that real estate taxes for the property are paid by the applicant.

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(2) Affidavits by others in the community stating that the applicant has occupied the property as the apparent owner for a period of not less than 10 years, and is generally believed to be the owner.

(3) Any instrument, whether or not recorded, which is commonly accepted as evidence of ownership.

§ 3550.108 Security requirements (loans only).

When the total section 504 indebtedness is \$7,500 or more, the property will be secured by a mortgage on the property, leasehold interest, or land purchase contract.

(a) RHS does not require a first lien position, but the total of all debts on the secured property may not exceed the value of the security, except by the amount of any required contributions to an escrow account for taxes and insurance and any required appraisal fee.

(b) Title clearance and the use of legal services generally must be conducted in accordance with 7 CFR part 1927, subpart B. These requirements need not be followed for:

(1) Loans where the total RHS indebtedness is less than \$7,500; or

(2) Subsequent loans made for minimal essential repairs necessary to protect the Government's interest.

§ 3550.109 Escrow account (loans only).

RHS may require that borrowers deposit into an escrow account amounts necessary to ensure that the account will contain sufficient funds to pay real estate taxes, hazard and flood insurance premiums, and other related costs when they are due in accordance with the Real Estate Settlement and Procedures Act of 1974 (RESPA) and section 501(e) of the Housing Act of 1949, as amended.

§ 3550.110 Insurance (loans only).

(a) Borrower responsibility. Any borrower with a secured indebtedness in excess of \$15,000 at the time of loan approval must furnish and continually maintain hazard insurance on the security property, with companies, in amounts, and on terms and conditions acceptable to RHS including a "loss payable clause" payable to RHS to protect the Government's interest.

(b) Amount. The borrower is required to insure the dwelling and any other essential buildings in an amount equal to the insurable value of the dwelling and other essential buildings. However, in cases where the borrower's outstanding secured indebtedness is less than the insurable value of the dwelling and other essential buildings, the borrower may elect a lower coverage provided it is not less than the outstanding secured



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indebtedness. If the borrower fails, or is unable, to insure the secured property, RHS will force place insurance and charge the cost to the borrower's account. Force place insurance only provides insurance coverage to the Agency and does not provide any direct coverage or benefit to the borrower. The amount of the lender-placed coverage generally will be the property's last known insured value.

(c) Flood insurance. Flood insurance must be obtained and maintained for the life of the loan for all property located in Special Flood Hazard Areas (SFHA) as determined by the Federal Emergency Management Agency (FEMA). RHS actions will be consistent with RD Instruction 1970, Subpart F, 7 CFR part 1806, Subpart B, and RD Instruction 426.2 which address flood documentation and insurance requirements. If flood insurance through FEMA's National Flood Insurance Program is not available in a SFHA, if the lowest floor (including the basement) is not above the base flood elevation, or if there are viable alternative housing options outside of the floodplain, the property is not eligible for federal financial assistance.

(d) Losses.

(1) Loss deductible clauses for required insurance coverage may not exceed the generally accepted minimums based on current industry standards and local market conditions.

(2) Borrowers must immediately notify RHS of any loss or damage to insured property and collect the amount of the loss from the insurance company.

(3) RHS may require that loss payments be supervised. All repairs and replacements done by or under the direction of the borrower, or by contract, will be planned, performed, inspected, and paid for in accordance with 7 CFR part 1924, subpart A.

(4) When insurance funds remain after all repairs, replacements, and other authorized disbursements have been made, the funds will be applied in the following order:

(i) Prior liens, including delinquent property taxes.

(ii) Delinquency on the account.

(iii) Advances due for recoverable cost items.

(iv) Released to the borrower if the RHS debt is adequately secured.

(5) If a loss occurs when insurance is not in force, the borrower is responsible for making the needed repairs or replacements and ensuring that the insurance is reinstated on the property.

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§ 3550.110 (d) (Con.)

(6) If the borrower is not financially able to make the repairs, RHS may take one of the following actions:

- (i) Make a subsequent loan for repairs.
- (ii) Subordinate the RHS lien to permit the borrower to obtain funds for needed repairs from another source.
- (iii) Permit the borrower to obtain funds secured by a junior lien from another source.
- (iv) Make a protective advance to protect the Government's interest.
- (v) Accelerate the account and demand payment in full.

§ 3550.111 Appraisals (loans only).

An appraisal is required when the section 504 debt to be secured exceeds \$15,000 or whenever RHS determines that it is necessary to establish the adequacy of the security. RHS may charge an appraisal fee. Appraisals must be made in accordance with the Uniform Standards of Professional Appraisal Practices. When other real estate is taken as additional security it will be appraised if it represents a substantial portion of the security for the loan.

§ 3550.112 Maximum loan and grant.

(a) Maximum loan permitted. The sum of all outstanding section 504 loans to 1 borrower or on 1 dwelling may not exceed \$20,000.

(1) Transferees who have assumed a section 504 loan and wish to obtain a subsequent section 504 loan are limited to the difference between the unpaid principal balance of the debt assumed and \$20,000.

(2) For a secured loan, the total of all debts on the secured property may not exceed the value of the security, except by the amount of any required appraisal and tax monitoring fees, and the contributions to an escrow account for taxes and insurance.

(b) Maximum loan based upon ability to pay. The maximum loan is limited to the principal balance that can be supported given the amount the applicant has available, as determined by RHS, to repay a loan at 1 percent interest with a 20-year term.

(c) Maximum grant. The lifetime total of the grant assistance to any recipient is \$7,500. No grant can be awarded unless the maximum level of loans, as supported by a budget, have been obtained.

§ 3550.113 Rates and terms (loans only).

- (a) Interest rate. The interest rate for all section 504 loans will be 1 percent.
- (b) Loan term. The repayment period for the loan should generally be as short as possible based on the applicant's repayment ability, and may never exceed 20 years; however loans made in combination with grants must have a term of 20 years.

§ 3550.114 Repayment agreement (grants only).

Grant recipients are required to sign a repayment agreement which specifies that the full amount of the grant must be repaid if the property is sold in less than 3 years from the date the grant agreement was signed.

§ 3550.115 WWD grant program objectives.

The objective of the WWD individual grant program is to facilitate the use of community water and waste disposal systems by the residents of colonias along the border between the U.S. and Mexico. WWD grants are processed the same as Section 504 grants, except as specified in this subpart.

§ 3550.116 Definitions applicable to WWD grants only.

- (a) Colonia. Any identifiable community designated in writing by the State or county in which it is located; determined to be a colonia on the basis of objective criteria including lack of a potable water supply, lack of adequate sewage systems, and lack of decent, safe, and sanitary housing, inadequate roads, and drainage; and existed and was generally recognized as a colonia before October 1, 1989.
- (b) Individual. Resident of a colonia located in a rural area.
- (c) Rural areas. Includes unincorporated areas and any city or town with a population not in excess of 10,000 inhabitants according to the most recent decennial census of the United States.
- (d) System. A community or central water supply or waste disposal system.
- (e) WWD. Water and Waste Disposal grants to individuals.

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§ 3550.117 WWD grant purposes.

Grant funds may be used to pay the reasonable costs for individuals to:

- (a) Extend service lines from the system to their residence.
- (b) Connect service lines to residence's plumbing.
- (c) Pay reasonable charges or fees for connecting to a system.
- (d) Pay for necessary installation of plumbing and related fixtures within dwellings lacking such facilities. This is limited to one bath tub, sink, commode, kitchen sink, water heater, and outside spigot.
- (e) Construction and/or parting off a portion of the dwelling for a bathroom, not to exceed 4.6 square meters (48 square feet) in size.
- (f) Pay reasonable costs for closing abandoned septic tanks and water wells when necessary to protect the health and safety of recipients of a grant for a purpose provided in paragraph (a) or (b) of this section and is required by local or State law.
- (g) Make improvements to individual's residence when needed to allow the use of the water and/or waste disposal system.

§ 3550.118 Grant restrictions.

(a) Maximum grant. Lifetime assistance to any individual for initial or subsequent Section 306C WWD grants may not exceed a cumulative total of \$5,000.

(b) Limitation on use of grant funds. WWD grant funds may not be used to:

- (1) Pay any debt or obligation of the grantees other than obligations incurred for purposes listed in § 3550.117.
- (2) Pay individuals for their own labor.

§ 3550.119 WWD eligibility requirements.

In addition to the eligibility requirements of § 3550.103, WWD applicants must meet the following requirements:

- (a) An applicant need not be 62 years of age or older.

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(b) Own and occupy a dwelling located in a colonia. Evidence of ownership will be presented as outlined in § 3550.107.

(c) Have a total taxable income from all individuals residing in the household that is below the most recent poverty income guidelines established by the Department of Health and Human Services.

(d) Must not be delinquent on any Federal debt.

(e) The household income must be verified at the time they apply for assistance through verification of employment and benefits. Federal tax returns are used as further verification of household income.

§§ 3550.120 - 3550.149 [Reserved]

§ 3550.150 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0172. Public reporting burden for this collection of information is estimated to vary from 5 minutes to 3 hours per response, with an average of 1 1/2 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. You are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Subpart D - Regular Servicing

§ 3550.151 Servicing goals.

This subpart sets forth the Rural Housing Service (RHS) policies for managing the repayment of loans made under sections 502 and 504 of the Housing Act of 1949, as amended.

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### § 3550.152 Loan payments.

(a) Payment terms. Unless the loan documents specify other loan repayment terms, borrowers are required to make monthly payments. Borrowers with existing loans specifying annual payments may request conversion to monthly payments, and must convert to a monthly payment schedule before any subsequent loan or new payment assistance is approved. Suitable forms of payment are: check, money order, or bank draft. Borrowers who make cash payments will be assessed a fee to cover the cost of conversion to a money order.

(b) Application of payments. If a borrower makes less than the scheduled payment, the payment is held in suspense and is not applied to the borrower's account. When subsequent payments are received in an amount sufficient to equal a scheduled payment, the amount will be applied in the following order:

- (1) Protective advances charged to the account.
- (2) Accrued interest due.
- (3) Principal due.
- (4) Escrow for taxes and insurance.

(c) Multiple loans. When a borrower with multiple loans for the same property makes less than the scheduled payment on all loans, the payment will be applied to the oldest loan and then in declining order of age. Future remittances will be applied beginning with the oldest unpaid installment.

(d) Application of excess payments. Borrowers can elect to make payments in excess of the scheduled amount to be applied to principal, provided there are no outstanding fees.

### § 3550.153 Fees.

RHS may assess reasonable fees including a tax service fee, fees for late payments, and fees for checks returned for insufficient funds.

### § 3550.154 Inspections.

RHS or its agent may make reasonable entries upon and inspections of any property used as security for an RHS loan as necessary to protect the interest of the Government. RHS will give the borrower notice at the time of or prior to an inspection.

§ 3550.155 Escrow account.

Escrow accounts will be administered in accordance with RESPA and section 501(e) of the Housing Act of 1949, as amended.

(a) Upon creation of the escrow account, RHS may require borrowers to deposit funds sufficient to pay taxes and insurance premiums applicable to the mortgage for the period since the last payments were made and to fund a cushion as permitted by RESPA.

(b) Borrowers may elect to escrow at any time during the terms of the loan if the outstanding RHS loan balance is over \$2,500.

(c) RHS may require borrowers to escrow in conjunction with any special servicing action.

§ 3550.156 Borrower obligations.

(a) After receiving a loan from RHS, borrowers are expected to meet a variety of obligations outlined in the loan documents. In addition to making timely payments, these obligations include:

(1) Maintaining the security property, and

(2) Maintaining an adequately funded escrow account, or paying real estate taxes, hazard and flood insurance, and other related costs when due.

(b) If a borrower fails to fulfill these obligations, RHS may obtain the needed service and charge the cost to the borrower's account.

§ 3550.157 Payment subsidy.

(a) Borrowers currently receiving payment subsidy.

(1) RHS will review annually each borrower's eligibility for continued payment subsidy and determine the appropriate level of assistance. To be eligible for payment subsidy renewal, the borrower must also occupy the property.

(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 RHS error caused the delay, or the next due date after the renewal is approved in all other cases.

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§ 3550.157 (a) (Con.)

(3) The borrower must notify RHS whenever an adult member of the household becomes employed or changes employment, there is a change in household composition, or if income increases by at least 10 percent. The household may also report decreases in income. If the change in the household's income will cause the payment for principal and interest to change by at least 10 percent, the household's payment subsidy may be adjusted for a new 12-month period. The new agreement will be effective the due date following the date the borrower's information is verified by RHS.

(b) Borrowers not currently receiving payment subsidy. Payment assistance may be granted to borrowers not currently receiving payment subsidy whose loans were approved on or after August 1, 1968, whose income does not exceed the applicable low-income limit for the area, are personally occupying the RHS financed property, and meet the requirements of § 3550.53 (b), (e), and (f). In general, to receive payment assistance the term of the loan at closing must have been at least 25 years. If an account has been reamortized and the initial term of the loan was at least 25 years, payment assistance may be granted even though the term of the reamortized loan is less than 25 years. Payment assistance may be granted on a subsequent loan for repairs with a term of less than 25 years.

(c) Cancellation of payment subsidy. RHS will cancel a payment subsidy if the borrower does not occupy the property, has sold or transferred title to the property, or is no longer eligible for payment subsidy.

§ 3550.158 Active military duty.

The Soldiers and Sailors Relief Act requires that the interest rate charged a borrower who enters full-time active military duty after a loan is closed not exceed six percent. Active military duty does not include participation in a military reserve or the National Guard unless the borrower is called to active duty.

(a) Amount of assistance. If a borrower qualifies for payment subsidy after reduction of the interest rate to six percent, the amount of payment subsidy received during the period of active military duty will be the difference between the amount due at the subsidized rate for principal and interest and the amount due at a six percent interest rate. The six percent interest rate will be effective with the first payment due after RHS confirms the active military status of the borrower.

(b) Change of active military status. The borrower must notify RHS when he or she is no longer on active military duty. RHS will cancel the six percent interest rate and resume use of the promissory note interest rate. A new payment subsidy agreement may be processed if the borrower is eligible.



§ 3550.159 Borrower actions requiring RHS approval.

(a) Mineral leases. Borrowers who wish to lease mineral rights to a security property must request authorization from RHS. RHS may consent to the lease of mineral rights and subordinate its liens to the lessee's rights and interests in the mineral activity if the security property will remain suitable as a residence and the Government's security interest will not be adversely affected. Subordination of RHS 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, RHS may consent to the lease only if the borrower assigns 100 percent of the income from the lease to RHS to be applied to reduce principal and the rent to be paid is at least equal to the estimated decrease in the market value of the security.

(2) If the proposed activity is not likely to decrease the value of the security property, RHS 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 RHS to be applied to reduce principal.

(b) Subordination. RHS may subordinate its interests to permit a borrower to defer recapture amounts and refinance the loan, or to obtain a subsequent loan with private credit.

(1) When it is in the best interest of the Government, subordination will be permitted if:

(i) The other lender will verify that the funds will be used for purposes for which an RHS loan could be made,

(ii) The prior lien debt will be on terms and conditions that the borrower can reasonably be expected to meet without jeopardizing repayment of the RHS indebtedness,

(iii) Any proposed development will be planned and performed in accordance with 7 CFR part 1924, subpart A or directed by the other lender in a manner which is consistent with that subpart, and

(iv) An agreement is obtained in writing from the prior lienholder providing that at least 30 days prior written notice will be given to RHS before action to foreclose on the prior lien is initiated.

(2) The total amount of debt permitted when RHS subordinates its interests depends on whether the borrower pays off the RHS loan.

(i) For situations in which the borrower is obtaining a subsequent loan from another source and will not pay off the RHS debt, the prior lien debt plus the unpaid balance of all RHS loans, exclusive of recapture, will not exceed the market value of the security.

(ii) For situations in which RHS is subordinating only a deferred recapture amount, the prior lien debt plus the deferred recapture amount will not exceed the market value of the security.

(c) Partial release of security. RHS may consent to transactions affecting the security, such as sale or exchange of security property or granting of a right-of-way across the security property, and grant a partial release provided:

(1) The compensation is:

(i) For sale of the security property, cash in an amount equal to the value of the security being disposed of or rights granted.

(ii) For exchange of security property, another parcel of property acquired in exchange with value equal to or greater than that being disposed of.

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

(2) An appraisal must be conducted if the latest appraisal is more than 1 year old or if it does not reflect market value and the amount of consideration exceeds \$5,000. The appraisal fee will be charged to the borrower.

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

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

(5) Environmental requirements are met and environmental documentation is submitted in accordance with 7 CFR part 1970.

(6) When exchange of all or part of the security is involved, title clearance are obtained before release of the existing security.

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(7) 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 RHS 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 RHS indebtedness or used for improvements to the security property in keeping with purposes and limitations applicable for use of RHS loan funds. Proposed development will be planned and performed in accordance with 7 CFR part 1924, subpart A and supervised to ensure that the proceeds are used as planned.

(d) Lease of security property. A borrower must notify RHS if they lease the property. If the lease is for a term of more than 3 years or contains an option to purchase, RHS may liquidate the loan. During the period of any lease, the borrower is not eligible for a payment subsidy or special servicing benefits.

§ 3550.160 Refinancing with private credit.

(a) Objective. RHS direct loan programs are not intended to supplant or compete with private credit sources. Therefore, borrowers are required to refinance RHS loans with private credit sources when RHS determines that the borrower meets RHS criteria.

(b) Criteria for refinancing with private credit. Borrowers must refinance with private credit when RHS determines that the borrower has the ability to obtain other credit at reasonable rates and terms based on their income, assets, and credit history. Reasonable rates and terms are those commercial rates and terms that borrowers are expected to meet when borrowing for similar purposes. Differences in interest rates and terms between RHS and other lenders will not be an acceptable reason for a borrower to fail to refinance with private credit if the available rates and terms are within the borrower's ability to pay.

(c) Notice of requirement to refinance with private credit. The financial status of all borrowers may be reviewed periodically to determine their ability to refinance with private credit. A borrower's financial status may be reviewed at any time if information becomes available to RHS that indicates that the borrower's circumstances have changed.

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(1) A borrower undergoing review is required to supply, within 30 days of a request from RHS, sufficient financial information to enable RHS to determine the borrower's ability to refinance with private credit. Foreclosure action may be initiated against any borrower who fails to respond.

(2) When RHS determines that a borrower has the ability to refinance with private credit, the borrower will be required to refinance within 90 days.

(3) Within 30 days after being notified of the requirement to refinance with private credit, a borrower may contest the RHS decision and provide additional financial information to document an inability to refinance with private credit.

(d) Failure to refinance with private credit.

(1) If the borrower is unable to secure private credit, the borrower must submit written statements and documentation to RHS showing:

(i) The lenders contacted.

(ii) The amount of the loan requested by the borrower and the amount, if any, offered by the lenders.

(iii) The rates and terms offered by the lenders or the specific reasons why other credit is not available.

(iv) The information provided by the borrower to the lenders regarding the purpose of the loan.

(2) If RHS determines that the borrower's submission does not demonstrate the borrower's inability to refinance with private credit, or if the borrower fails to submit the required information, foreclosure may be initiated.

(e) Subordination of recapture amount. RHS may subordinate its interest in any deferred recapture amount to permit a borrower to refinance with private credit. The amount to which the RHS debt will be subordinated may include:

(1) The amount required to repay the RHS debt, exclusive of recapture,

(2) Reasonable closing costs,

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(3) Up to one percent of the loan amount for loan servicing costs, if required by the lender, and

(4) The cost of any necessary repairs or improvements to the security property.

(f) Application for additional credit. A borrower who has been asked to refinance with private credit will not be considered for additional credit until the refinancing issue is resolved unless such additional credit is necessary to protect the Government's interest.

§ 3550.161 Final payment.

(a) Payment in full. Full payment of a borrower's account includes repayment of principal and outstanding interest, unauthorized assistance, recapture amounts, and charges made to the borrower's account. Any supervised funds or funds remaining in a borrower's escrow account will be applied to the borrower's account or returned to the borrower.

(b) Release of security instruments. RHS may release security instruments when full payment of all amounts owed has been received and verified. If RHS and the borrower agree to settle the account for less than the full amount owed, the security instruments may be released when all agreed-upon amounts are received and verified. Security instruments will not be released until any deferred recapture amount has been paid in full.

(c) Payoff statements. At the borrower's request, RHS will provide a written statement indicating the amount required to pay the account in full. RHS may charge a fee for statements for the same account if more than 2 statements are requested in any 30 day period.

(d) Suitable forms of payment. Suitable forms of payment are: check, money order, or bank draft. Borrowers who make cash payments will be assessed a fee to cover conversion to a money order.

(e) Recording costs. Recording costs for the release of the mortgage will be the responsibility of the borrower, except where State law requires the mortgagee to record or file the satisfaction.

§ 3550.162 Recapture.

(a) Recapture policy. Borrowers with loans approved or assumed on or after October 1, 1979, will be required to repay subsidy amounts received through payment subsidy (including the former interest credit program) or deferred mortgage assistance in accordance with paragraph (b) of this section. Amounts to be recaptured are due and payable when the borrower transfers title or ceases to occupy the property, including but not limited to, in the event of foreclosure or deed in lieu of foreclosure.

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Such recapture will include the amount of principal reduction attributed to subsidy (for loans subject to recapture that were approved, and received interest credit, between October 1, 1979, and December 31, 1989), except in cases of foreclosure and deed in lieu of foreclosure.

(b) Amount to be recaptured.

(1) General. The amount to be recaptured is the amount of principal reduction attributed to subsidy plus the lesser of:

(i) The amount of subsidy received; or

(ii) A portion of the value appreciation of the property subject to recapture. In order for value appreciation to be calculated, the borrower will provide a current appraisal, including an appraisal for any capital improvements, or arm's length sales contract as evidence of market value upon Agency request. Appraisals must meet Agency standards under § 3550.62.

(2) Foreclosure or deed in lieu of foreclosure. Notwithstanding paragraph (b) (1) of this section, the amount to be recaptured in a foreclosure or deed in lieu of foreclosure is the amount of subsidy received, not including any principal reduction attributed to subsidy. Foreclosure actions will seek to recover such amounts only from the proceeds of the property. Liquidation proceeds (in the case of foreclosure) or the net recovery value (in the case of deed in lieu of foreclosure) will be applied or credited to the borrower's debt in accordance with the security agreement in the following order:

(i) Recoverable costs (e.g. protective advances, foreclosure costs, late charges).

(ii) Accrued interest.

(iii) Principal.

(iv) Subsidy.

(3) Value appreciation. The value appreciation of a property with a cross-collateralized loan is based on the market value of the dwelling and lot. If located on a farm, the lot size would be a typical lot for a single family housing property.

(4) Interest reduced from the promissory note rate to six percent under the Servicemembers Civil Relief Act (SCRA) is not subject to recapture.

(c) Deferral of recapture. If the borrower refinances or otherwise pays in full without transfer of title and continues to occupy the property, the amount of recapture will be calculated in accordance with paragraph (a) but payment of recapture may be deferred, interest free, until the property is sold or vacated. If the recapture amount is deferred, the Agency mortgage can be subordinated when in the Government's best interest but will not be released nor the promissory note satisfied until the Agency is paid in full. In situations where deferral of recapture is an option, recapture will be discounted if paid in full at the time of settlement or timely paid after Agency notification to the borrower that recapture is due.

(d) Assumed loans.

(1) When a loan subject to recapture is assumed under new rates and terms, the recapture amount may be paid in full by the seller or included in the principal amount assumed by the buyer.

(2) When a loan is assumed under the same rates and terms as the original promissory note, recapture amounts will not be due. When the new borrower transfers title or ceases to occupy the property, all subsidy subject to recapture before and after the assumption is due.

(3) When a borrower has deferred payment of recapture amounts, the deferred recapture amount may be included in the principal amount of the new loan.

§ 3550.163 Transfer of security and assumption of indebtedness.

(a) General policy. RHS mortgages contain due-on-sale clauses that generally require RHS consent before title to a security property can be transferred with an assumption of the indebtedness. If it is in the best interest of the Government, RHS will approve the transfer of title and assumption of indebtedness on program or nonprogram (NP) terms, depending on the transferee's eligibility and the property's characteristics.

(b) RHS approval of assumptions.

(1) A borrower with a loan on program terms who wishes to transfer a security property restricted by a due-on-sale clause to a purchaser who wishes to assume the debt must receive prior authorization from RHS. If RHS authorizes the transfer and assumption, the account will be serviced in the purchaser's name and the purchaser will be liable for the loan under the terms of the security instrument.

(2) If a borrower transfers title to the security property with a due-on-sale clause without obtaining RHS authorization, RHS will not approve assumption of the indebtedness, and the loan will be liquidated unless RHS determines that it is in the Government's best interest to continue the loan. If RHS decides to continue the loan, the account will be serviced in the original borrower's name and the original borrower will remain liable for the loan under the terms of the security instrument.

(c) Exceptions to due-on-sale clauses.

(1) Due-on-sale clauses 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.



§ 3550.163 (c)(1) (Con.)

(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.

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

(2) A transferee who obtains property through one of the types of transfer listed in paragraph (c)(1) of this section:

(i) Is not required to assume the loan, and RHS is not permitted to liquidate the loan, if the transferee continues to make scheduled payments and meet all other obligations of the loan. A transferee who does not assume the loan is not eligible for payment assistance or a moratorium.

(ii) May assume the loan on the rates and terms contained in the promissory note, with no down payment. If the account is past due at the time an assumption is executed, the account may be brought current by using any of the servicing methods discussed in subpart E of this part.

(iii) May assume the loan under new rates and terms if the transferee applies and is program-eligible.

(3) Any subsequent transfer of title, except upon death of the inheritor or between inheritors to consolidate title, will be treated as a sale.

(d) Requirements for an assumption.

(1) Loans secured by program-eligible properties to be assumed by program-eligible purchasers may be assumed on program terms. Loans secured by nonprogram properties and loans to be assumed by purchasers who are not eligible for program terms may be assumed on NP terms.

(2) The amount the transferee will assume will be either the current market value less any prior liens and any required down payment, or the indebtedness, whichever is less.

7 CFR Part 3550  
§ 3550.163 (d) (Con.)

(3) For loans assumed on program terms, the interest rate charged by RHS will be the rate in effect at loan approval or loan closing, whichever is lower. For loans assumed on nonprogram terms, the interest rate charged by RS will be the rate in effect at the time of loan approval.

(4) If additional financing is required to purchase the property or to make repairs, RHS may approve a subsequent loan under subparts B or C of this part.

(5) If an appraisal is required for an assumption on new terms, the purchaser is responsible for the appraisal fee.

(6) If all or a portion of the borrower's account balance is assumed, the borrower and cosigner, if any, will be released from liability on the amount of the indebtedness assumed. If an account balance remains after the assumption, RHS may pursue debt settlement in accordance with subpart F of this part.

(7) Unless it is in the Government's best interest, RHS will not approve an assumption of a secured loan if the seller fails to repay any unsecured RHS loan.

(8) If a loan is secured by a property with a dwelling situated on more than a minimum adequate site and the excess property cannot be sold separately as a minimum adequate site for another dwelling, RHS may approve a transfer of the entire property. If the excess property can be sold separately as a minimum adequate site, RHS will approve assumption of only the dwelling and the minimum adequate site. If the value of the dwelling on the minimum adequate site is less than the amount of the outstanding RHS debt, the remaining debt will be secured by the excess property. The outstanding debt will be converted to an NP loan and reamortized over a period not to exceed 10 years or the final due date of the original promissory note, whichever is sooner.

§ 3550.164 Unauthorized assistance.

(a) Definition. Unauthorized assistance includes any loan, payment subsidy, deferred mortgage payment, or grant for which the recipient was not eligible.

(b) Unauthorized assistance due to false information.

(1) False information includes information that the recipient knew was incorrect or should have known was incorrect that was provided or omitted for the purposes of obtaining assistance for which the recipient was not eligible.

## § 3550.164 (b) (Con.)

(2) If the recipient receives an unauthorized loan due to false information, RHS will adjust the account using the NP interest rate that was in effect when the loan was approved. The recipient must pay the account in full within 30 days.

(3) If the recipient receives unauthorized subsidy due to false information, RHS will require the recipient to repay it within 30 days. The account cannot be reamortized to include the unauthorized subsidy. If the recipient repays the unauthorized subsidy, the loan may be continued.

(c) Unauthorized assistance due to inaccurate information.

(1) Inaccurate information includes incorrect information inadvertently provided, used, or omitted without the intent to obtain benefits for which the recipient was not eligible.

(2) RHS will permit a recipient who receives an unauthorized loan due to inaccurate information to retain the loan under the following conditions.

(i) If the inaccurate information was related to the purpose of the loan or the recipient's eligibility, with the exception of income, or the income used was incorrect, but the recipient still qualified as income-eligible, RHS will allow the recipient to continue the loan on existing terms.

(ii) If a section 502 recipient's income was above the moderate-income level, RHS will convert the loan to an NP loan, using the nonprogram interest rate in effect on the date the loan was approved.

(iii) If a section 504 recipient's income was above the very low-income level, RHS will apply the applicable 502 or nonprogram interest rate in effect on the date the loan was approved.

(iv) If an incorrect interest rate was used, RHS will adjust the account using the correct interest rate.

(3) If the recipient receives unauthorized subsidy due to inaccurate information, RHS will require the recipient to repay it within 30 days. If the recipient cannot repay it within 30 days, the account may be reamortized. If the recipient repays the unauthorized subsidy or reamortizes the loan, the loan may be continued.

7 CFR Part 3550  
§ 3550.164 (c) (Con.)

(d) Unauthorized grants. Recipients may either repay the unauthorized assistance in a lump sum or execute a promissory note, regardless of whether the unauthorized assistance was due to false or inaccurate information. RHS may seek a judgment if the recipient refuses to repay the unauthorized assistance.

(e) Account servicing. RHS will adjust all accounts retroactively to establish the amount of unauthorized assistance. If the recipient does not repay the unauthorized assistance within 30 days, RHS may accelerate the loan. If the unauthorized assistance is due to inaccurate information and the recipient is unable to repay within 30 days, RHS may reamortize the loan.

(f) Accounts with no security. If an unauthorized loan or grant is unsecured, RHS may seek the best mortgage obtainable.

§§ 3550.165 - 3550.199 [Reserved]

§ 3550.200 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0172. Public reporting burden for this collection of information is estimated to vary from 5 minutes to 3 hours per response, with an average of 1 1/2 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. You are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Subpart E - Special Servicing

§ 3550.201 Purpose of special servicing actions.

The Rural Housing Service (RHS) may approve special servicing actions to reduce the number of borrower failures that result in liquidation. Borrowers who have difficulty keeping their accounts current may be eligible for one or more available servicing options including: payment assistance; delinquency workout agreements that temporarily modify payment terms; protective advances of funds for taxes, insurance, and other approved costs; and payment moratoriums.

§ 3550.202 Past due accounts.

An account is past due if the scheduled payment is not received by the due date.

(a) Late fee. A late fee will be assessed if the full scheduled payment is not received by the 15th day after the due date, or as authorized by State law.

(b) Liquidation.

(1) For borrowers with monthly payments. The account may be accelerated without further servicing when at least 3 scheduled payments are past due or an amount equal to at least 2 scheduled payments is past due for at least 3 consecutive months. In such cases RHS may pursue voluntary liquidation and foreclosure.

(2) For borrowers with annual payments. The account may be accelerated without further servicing when at least 3/12ths of 1 scheduled payment has not been received by its due date. In such cases, RHS may pursue voluntary liquidation and foreclosure.

(3) Subsidy recapture. Acceleration under this section will take into account any subsidy recapture due under § 3550.162.

§ 3550.203 General servicing actions.

Whenever any of the servicing actions described in this subpart result in reamortization of the account RHS may:

(a) Require a borrower who currently makes annual payments, but receives a monthly income, to convert to monthly payments.

(b) Require the creation and funding of an escrow account for real estate taxes and insurance, if one does not already exist for any borrower with monthly payments.

(c) Convert the method of calculating interest for any account being charged daily simple interest to an amortized payment schedule.

§ 3550.204 Payment assistance.

Borrowers who are eligible may be offered payment assistance in accordance with subpart B of this part. Borrowers who are not eligible for payment assistance because the loan was approved before August 1, 1968, or the loan was made on above-moderate or nonprogram (NP) terms, may refinance the loan in order to obtain payment assistance if:

(a) The borrower is eligible to receive a loan with payment assistance,

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§ 3550.204 (Con.)

(b) Due to circumstances beyond the borrower's control, the borrower is in danger of losing the property, and

(c) The property is program-eligible.

§ 3550.205 Delinquency workout agreements.

Borrowers with past due accounts may be offered the opportunity to avoid liquidation by entering into a delinquency workout agreement that specifies a plan for bringing the account current. To receive a delinquency workout agreement, the following requirements apply:

(a) A borrower who is able to do so will be required to pay the past-due amount in a single payment.

(b) A borrower who is unable to pay the past-due amount in a single payment must pay monthly all scheduled payments plus an agreed upon additional amount that brings the account current within 2 years or the remaining term of the loan, whichever is shorter.

(c) If a borrower becomes more than 30 days past due under the terms of a delinquency workout agreement, RHS may cancel the agreement.

§ 3550.206 Protective advances.

RHS may pay for fees or services and charge the cost against the borrower's account to protect the Government's interest.

(a) Advances for taxes and insurance. RHS may advance funds to pay real estate taxes, hazard and flood insurance premiums, and other related costs, as well as amounts needed to fund the current escrow cycle.

(b) Advances for costs other than taxes and insurance. Protective advances for costs other than taxes and insurance, such as emergency repairs, will be made only if the borrower cannot obtain a subsequent loan.

(c) Repayment arrangements.

(1) Advances for borrowers with multiple loans will be charged against the largest loan.

(2) Amounts advanced will be due with the next scheduled payment. RHS may schedule repayment consistent with the borrower's ability to repay or reamortize the loan.

(3) Advances will bear interest at the promissory note rate of the loan to which the advance was charged.

§ 3550.207 Payment moratorium.

RHS may defer a borrower's scheduled payments for up to 2 years. NP borrowers are not eligible for a payment moratorium.

(a) Borrower eligibility. For a borrower to be eligible for a moratorium, all of the following conditions must be met:

(1) Due to circumstances beyond the borrower's control, the borrower is temporarily unable to continue making scheduled payments because:

(i) The borrower's repayment income fell by at least 20 percent within the past 12 months,

(ii) The borrower must pay unexpected and unreimbursed expenses resulting from the illness, injury, or death of the borrower or a family member, or

(iii) The borrower must pay unexpected and unreimbursed expenses resulting from damage to the security property in cases where adequate hazard insurance was not available or was prohibitively expensive.

(2) The borrower occupies the dwelling, unless RHS determines that it is uninhabitable.

(3) The borrower's account is not currently accelerated.

(b) Reviews of borrower eligibility.

(1) Periodically RHS may require the borrower to submit financial information to demonstrate that the moratorium should be continued. The moratorium may be canceled if:

(i) The borrower does not respond to a request for financial information,

(ii) RHS receives information indicating that the moratorium is no longer required, or

(iii) In the case of a moratorium granted to pay unexpected or unreimbursed expenses, the borrower cannot show that an amount at least equal to the deferred payments has been applied toward the expenses.

7 CFR Part 3550  
§ 3550.207(b) (Con.)

(2) At least 30 days before the moratorium is scheduled to expire, RHS will require the borrower to provide financial information needed to determine whether the borrower is able to resume making scheduled payments.

(c) Resumption of scheduled payments. When the borrower is able to resume scheduled payments, the loan will be reamortized to include the amount deferred during the moratorium and the borrower will be required to escrow. If the new monthly payment, after consideration of the maximum amount of payment subsidy available to the borrower, exceeds the borrower's repayment ability, all or part of the interest that has accrued during the moratorium may be forgiven.

(d) Borrowers unable to resume scheduled payments. If even after all appropriate servicing actions have been taken the borrower is unable to resume making scheduled payments after 2 consecutive years of being on a moratorium, the account will be liquidated.

§ 3550.208 Reamortization using promissory note interest rate.

Reamortization using the promissory note interest rate may be authorized when RHS determines that reamortization is required to enable the borrower to meet scheduled obligations, and only if the Government's lien priority is not adversely affected.

(a) Permitted uses. Reamortization at the promissory note interest rate may be used to accomplish a variety of servicing actions, including to:

- (1) Repay unauthorized assistance due to inaccurate information.
- (2) Repay principal and interest accrued and advances made during a moratorium.
- (3) Bring current an account under a delinquency workout agreement after the borrower has demonstrated the willingness and ability to meet the terms of the loan and delinquency workout agreement and reamortization is in the borrower's and Government's best interests.
- (4) Bring a delinquent account current in the case of an assumption where the due on sale clause is not triggered as described in § 3550.163(c).
- (5) Cover the remaining debt when a portion of the security property is being transferred but the acquisition price does not cover the outstanding debt. The remaining balance will be reamortized for a period not to exceed 10 years or the final due date of the note being reamortized, whichever is sooner.



## § 3550.208 (a) (Con.)

(6) Bring an account current where the National Appeals Division (NAD) reverses an adverse action, the borrower has adequate repayment ability, and RHS determines the reamortization is in the best interests of the Government and the borrower.

(b) Payment term of reamortized loan. Except as noted in paragraph (a)(5) of this section, the term of the reamortized loan may be extended to the maximum term for which the borrower was eligible at the time the loan was originally made, less the number of years the loan has been outstanding. In all cases, the term must not exceed the remaining security life of the property.

## § 3550.209 [Reserved]

§ 3550.210 Offsets.

Any money that is or may become payable from the United States to an RHS borrower may be subject to administrative, salary, or Internal Revenue Service (IRS) offsets for the collection of a debt owed to RHS.

(a) IRS offset. RHS may take action to effect offset of claims due RHS against tax refunds due to RHS debtors under 31 U.S.C. 3720a and 31 CFR 285.2.

(b) Salary offset. Offset of claims due to RHS may be collected pursuant to the salary offset provisions in 7 CFR part 3, subpart C for a federal employee or other persons covered in that subpart.

(c) Administrative offset. RHS may take action to effect administrative offset to recover delinquent claims due to it in accordance with the procedures in 7 CFR part 3, subpart B.

(d) Offset by other federal agencies. Escrow funds and loan and grant funds held or payable by RHS are not subject to offset by other federal agencies.

§ 3550.211 Liquidation.

(a) Policy. When RHS determines that a borrower is unable or unwilling to meet loan obligations, RHS may accelerate the loan and, if necessary, acquire the security property. The borrower is responsible for all expenses associated with liquidation and acquisition. If the account is satisfied in full, the borrower will be released from liability. RHS may pursue any deficiency unless the borrower received a moratorium at any time during the life of the loan and faithfully tried to repay the loan.

7 CFR Part 3550  
§ 3550.211 (Con.)

(b) Tribal allotted or trust land. Liquidations involving a security interest in tribal allotted or trust land shall only be pursued after offering to transfer the account to an eligible tribal member, the tribe, or the Indian Housing Authority. Forced liquidation of RHS security interests in Indian trust lands or on tribal allotted land will be recommended only after the State Director has determined it is in the best interest of the Government.

(c) Acceleration and foreclosure. If RHS determines that foreclosure is in the best interest of the Government, RHS will send an acceleration notice to each borrower and any cosigner.

(d) Voluntary liquidation. After acceleration, borrowers may voluntarily liquidate through:

(1) Refinancing or sale. The borrower may refinance or sell the security property for at least net recovery value and apply the proceeds to the account.

(2) Deed in lieu of foreclosure. RHS may accept a deed in lieu of foreclosure to convey title to the security property only after the debt has been accelerated and when it is in the Government's best interest.

(3) Offer by third party. If a junior lienholder or cosigner makes an offer in the amount of at least the net recovery value, RHS may assign the note and mortgage.

(e) Bankruptcy.

(1) When a petition in bankruptcy is filed by a borrower after acceleration, collection actions and foreclosure actions are suspended in accordance with the provisions of the Bankruptcy Code.

(2) RHS may accept conveyance of security property by the trustee in bankruptcy if the Bankruptcy Court has approved the transaction, RHS determines the conveyance is in the best interest of the Government, and RHS will acquire title free of all liens and encumbrances except RHS liens.

(3) Whenever possible in a Chapter 7 Bankruptcy, a reaffirmation agreement will be signed by the borrower and approved by the court prior to discharge, if RHS decides to continue with the borrower.

(f) Junior lienholder foreclosure. When a junior lienholder foreclosure does not result in payment in full of the RHS debt but the property is sold subject to the RHS lien, RHS may liquidate the account unless the new owner is eligible to assume the RHS debt and actually assumes the RHS debt.

(g) Payment subsidy. If the borrower is receiving payment subsidy, the payment subsidy agreement will not be canceled when the debt is accelerated, but will not be renewed unless the account is reinstated.

7 CFR Part 3550  
§ 3550.211 (Con.)

(h) Eligibility for special servicing actions. A borrower is not eligible for special servicing actions once the account has been accelerated.

(i) Reporting. RHS may report to IRS and credit reporting agencies any debt settled through liquidation.

§§ 3550.212 - 3550.249 [Reserved]

§ 3550.250 OMB control number.

The information collection requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) and have been assigned OMB control number 0575-0172. Public reporting burden for this collection of information is estimated to vary from 5 minutes to 3 hours per response, with an average of 1 1/2 hours per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. You are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Subpart F - Post-Servicing Actions

§ 3550.251 Property management and disposition.

(a) Policy. Rural Housing Service (RHS) will manage custodial property and Real Estate Owned (REO) property to protect the Government's interest, and may dispose of REO property through direct sales, sealed bid, or auction. RHS will follow affirmative fair housing marketing policies.

(b) Custodial property. RHS may take custodial possession of security property that has been abandoned, or for other reasons necessary to protect the Government's security. After taking custodial possession of a security property, RHS may maintain and repair the security property as needed to protect the Government's interest, pay required real estate taxes and assessments, and secure personal property left on the premises. Expenses will be charged to the borrower's account. Custodial property may be leased when it is in the Government's best interest and in such cases the borrower's account will be credited for income from the security property.

(c) REO property.

(1) Classification. When RHS takes title to a security property, it is classified as either program or nonprogram (NP) property. An REO property that is eligible for financing under the section 502 program, or which could reasonably be repaired to be eligible, is classified as program property. An REO property that cannot reasonably be repaired to be eligible as section 502 property, and property that has been improved to a point that it will no longer qualify as modest under section 502, is classified as NP property.

(2) Disclosing decent, safe, and sanitary defects. When RHS determines that an REO property to be sold is not decent, safe, and sanitary, or does not meet cost-effective energy conservation standards, it will disclose the reasons why. The deed by which such an REO property is conveyed will contain a covenant restricting it from residential use until it is decent, safe, and sanitary and meets the RHS cost-effective energy conservation standards. RHS will also notify any potential purchaser of any known lead-based paint hazards.

(3) Property on Indian tribal allotted or trust land. REO property which is located on Indian tribal allotted or trust land, will be sold or otherwise disposed of only to a member of the particular tribe having jurisdiction over the allotted or tribal land, to the tribe, or to an Indian housing authority serving the tribe on a first-come, first-served basis.

(4) Reservation of program REO properties.

(i) Program REO properties are reserved for eligible direct or guaranteed single family housing loans under this part or part 1980, subpart D of this title and nonprofit organizations or public bodies providing transitional housing during the first 60 days after the date of the first notice of sale, and during the first 30 days following any reduction in price or any other change in credit terms or other sale terms. After the expiration of a reservation period, program REO properties can be bought by any buyer.

(ii) An offer on a program REO property from a buyer who does not qualify for a direct or guaranteed single family housing loan may be submitted during a reservation period, but is considered to have been received on the day after the reservation period ends.

(iii) No offer is considered until 3 business days after the date the property is offered for sale. An offer received during the 3-day holding period is not considered until the 4th day, and is evaluated with any other offers actually received on the 4th day.

§ 3550.251 (c) (Con.)

(5) Priority of offers received the same day.

(i) Offers received on the same business day are selected in the following order:

(A) Offers from eligible direct or guaranteed single family housing loan applicants, with a request for credit on program terms. All offers are evaluated as if they were submitted at the listed price, regardless of the offering price.

(B) Offers from nonprofits or public bodies for conversion to use as transitional housing or for other special purposes as specified in paragraph (d)(4) of this section.

(C) Cash offers, from highest to lowest.

(D) NP credit offers, from highest to lowest.

(ii) Acceptable offers of equal priority received on the same business day are selected by lot.

(iii) REO properties are not held off the market pending the outcome of an appeal of RHS rejection of a request for financing.

(6) Sale by sealed bid or auction. RHS may authorize the sale of an REO property by sealed bid or public auction when it is in the best interest of the Government. RHS will publicly solicit requests for sealed bids and publicize auctions. If a successful bidder is unable to settle the transaction under the terms of the offer, except for the financing contingency, any required bid deposit may be retained by RHS. If the highest bid is lower than the minimum acceptable bid established by RHS, or if no acceptable bids are received, RHS may negotiate a sale without further public notice.

(d) Special purposes.

(1) REO property may be purchased for conversion to multiple family housing.

7 CFR Part 3550  
§ 3550.251 (d)(Con.)

(2) When a nonprofit organization or public body notifies RHS in writing of its intent to buy an REO property to provide transitional housing for the homeless, RHS may withdraw the property from the market for up to 30 days to give the entity an opportunity to execute a purchase contract. The listed price may be discounted for offers on a nonprogram REO property at any time, and on a program REO property after the 60-day reservation period. No down payment is required, and the loan term will be for a maximum of 30 years. Until RHS executes a sales agreement, an offer from a program-eligible applicant will receive priority, regardless of a nonprofit's interest in purchasing the REO property for use as transitional housing.

(3) NP properties may be leased to a nonprofit organization or public body to provide transitional housing for the homeless at an annual cost of one dollar. When an REO property is to be leased as transitional housing, RHS will make repairs needed to put the property in decent, safe, and sanitary condition. The lessee is responsible for all future repairs and maintenance.

(4) REO property may be sold under special provisions to nonprofit organizations or public bodies for the purpose of providing affordable housing to very low- and low-income families.

§ 3550.252 Debt settlement policies.

(a) Applicability. Debt settlement procedures may be initiated to collect any amounts due to RHS including:

- (1) Balances remaining on loan accounts after all liquidation proceeds or credits have been applied,
- (2) Subsidy recapture or grant amounts due, and
- (3) Unauthorized assistance due.

(b) Judgment. RHS may seek a judgment whenever a judgment might enable RHS to collect all or a significant portion of an amount owed.

(c) Multiple loans. RHS does not settle debts for one loan while other RHS loans on the same security property remain active.

(d) Cosigners and claims against estates. RHS may use any and all remedies available under law to collect from any cosigner and from a deceased borrower's estate.

(e) Reporting. RHS will report to the Internal Revenue Service and credit reporting agencies any debt settled through cancellation, compromise, or adjustment.

## § 3550.252 (Con.)

(f) Settlement during legal or investigative action. Cases that are under investigation for fiscal irregularity or have been referred to the Office of the Inspector General, the Office of the General Counsel, or the U.S. Attorney will not be considered for debt settlement until final action by the investigating or prosecuting entity has been taken.

(g) Offsets. RHS may request offsets as described in § 3550.210 to collect amounts owed.

(h) Escrow funds. At liquidation all funds held in escrow or unapplied funds will be applied against the debt.

§ 3550.253 Settlement of a debt by compromise or adjustment.

Compromise or adjustment offers may be initiated by the debtor or by RHS. RHS will approve only those compromises and adjustments that are in the best interest of the Government.

(a) Compromise. A compromise is an agreement by RHS to release a debtor from liability upon receipt of a specified lump sum that is less than the total amount due.

(b) Adjustments. An adjustment is an agreement by RHS to release a debtor from liability generally upon receipt of an initial lump sum representing the maximum amount the debtor can afford to pay and periodic additional payments over a period of up to 5 years.

(c) Timing of offers.

(1) For a settlement offer to be considered, secured debts must be fully matured under the terms of the debt instrument or must have been accelerated by RHS.

(2) Unsecured debts owed after the sale of the security property may be proposed for compromise or adjustment at any time. Debts that were never secured may be proposed for compromise or adjustment when they are due and payable.

(d) Retention of security property. The debtor may retain the security property if the compromise payment is at least equal to the net recovery value, and it is in the best interest of the Government to allow the debtor to retain the security property.

7 CFR Part 3550

§§ 3550.254 - 3550.299 [Reserved]

§ 3550.300 OMB control number.

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