

U. S. Department of Housing and Urban Development  
Washington, D.C. 20410-8000

May 20, 1997

OFFICE OF THE ASSISTANT SECRETARY  
FOR HOUSING-FEDERAL HOUSING COMMISSIONER

MORTGAGEE LETTER 97-22

TO: ALL APPROVED MORTGAGEES

SUBJECT: Single Family Loan Production - FHA New Construction,  
Inspection, and Appraisal Requirements

The Department of Housing and Urban Development recently held two Roundtable discussions with our industry partners; one on new construction issues, and another on appraisal issues. The purpose of this mortgagee letter is to advise you of the practices and procedures being eliminated or modified to make FHA requirements less burdensome.

NEW CONSTRUCTION AND INSPECTION ISSUES:

HUD/VA/INDUSTRY LOCAL ADVISORY GROUPS

Maintaining open communication between our partners and the Department keeps both informed of changes, problems, and new issues. It helps eliminate possible program abuse, clarifies and helps resolve misinterpretation of specific program procedures, and assists us in developing simplified ways of delivering public services more efficiently and effectively. The Department, therefore, will reemphasize to its local HUD offices and the Homeownership Centers (HOCs) the importance of continuing and expanding the practice of meeting with builders, lenders, real estate professionals, VA and local government and community groups to communicate concerns and problems and to discuss solutions.

INSPECTIONS ON NEW CONSTRUCTION

Three inspections are required on new construction in order to get a high ratio insured mortgage. To expand the process of inspections, the Department will now permit the final inspection by the local authority to be accepted in lieu of HUD's third inspection in those jurisdictions where HUD now accepts the first two inspections by the local authority.

AFFIRMATIVE FAIR HOUSING MARKETING PLANS (AFHMP)

HUD and the National Association of Home Builders (NAHB) has a valid Voluntary Affirmative Marketing Agreement (VAMA). Therefore, any member of NAHB, or a builder who is not a member of NAHB but who has a contract with an NAHB member (a signatory

in good standing to a VAMA) to market their houses, is covered by the HUD/NAHB VAMA.

HUD and the National Association of Realtors (NAR) signed a Fair Housing Partnership Resolution, effective December 5, 1996. This is not a VAMA and it cannot be substituted for one. Builders who contract with real estate professionals to market their new houses must also complete and submit an AFHMP to the local HUD office or HOC in their area for approval prior to the issuance of a case number.

#### SWIFT ENFORCEMENT OF REGULATIONS

The Department is making it clear that it will not tolerate abuse of any single family program. Moving from pre-endorsement to post endorsement monitoring, more reliance is being placed on our lender partners to assure compliance with FHA requirements. To assure this, more staff is being added to our Lender Monitoring functions. Lenders are reminded that their quality control systems must be current and must be followed.

#### ENERGY EFFICIENT MORTGAGE (EEM) PROGRAM

This is to remind lenders that the Department is interested in promoting the use of the EEM program. We are currently working with Edison Electric to develop an EEM computer program which will assist in the required cost benefit analysis. EEM software and a user's guide will be available in the near future, and may be ordered through the HUD User Information System for a nominal fee. Interested persons may contact HUD User at 1-800-245-2691, fax 301-251-5767, or write: HUD User, P.O. Box 6091, Rockville, MD 20840. Note that the EEM program may now be used in conjunction with Section 203(h), Disaster Housing Mortgage Insurance. ( SEE ML 97-10, dated April 1, 1997. )

#### APPRAISER AND APPRAISAL ISSUES:

##### FHA ROSTER OF APPRAISERS

The Roster of Appraisers gives FHA a fast and effective way to stop a poorly performing appraiser from providing appraisals to lenders who are unfamiliar with their work. Additionally, the Department's policy on choosing appraisers states that there shall be no discrimination on the basis of race, color, religion, national origin, sex, age or disability. The roster is used to collect minority and gender information which is then used to measure one element of the lender's performance. No change, therefore, is being made to the FHA Roster of Appraisers.

Lenders are reminded that if the appraiser they selected provides a poor or even fraudulent appraisal which leads the Department to insure a mortgage at an inflated amount, the lender is held equally responsible with the appraiser for the violation. Therefore, it behooves the lender to assure they select appraisers that are knowledgeable and trustworthy and that the appraisals provided are accurate and justifiable. If they are not, the lender should report the appraiser to both the

Department and to the State Appraiser Licensing Board for action. While it may appear less troublesome to not select that appraiser in the future, lack of reporting allows that appraiser to be selected by other lenders, making it more likely that unsuspecting lenders will inadvertently choose a bad appraiser and be held liable for the poor results.

#### FEES

FHA field offices will no longer establish maximum appraisal fees. However, a lender's charge to the borrower for an appraisal must be no more than the actual amount charged by and paid to the appraiser, subject to the fee being reasonable and customary for an appraisal in the area in which the property is located. That fee may be included in the closing costs upon which the mortgage is based. Lenders that utilize their own staff appraiser may charge a fee to the mortgagor which does not exceed that which is reasonable and customary in the area. Lenders utilizing management firms that secure the appraisal on behalf of the lender may only charge the mortgagor the actual amount paid to and received by the appraiser, subject to the reasonable and customary cap. Lenders dealing with service providers which charge reasonable and customary fees but pay the appraiser less than they charge the lender may only have the mortgagor pay what was charged by and paid to the appraiser.

#### COST APPROACH TO APPRAISING

The Department now places more reliance on the market approach, but there are instances when the cost and income approaches are required. For all new construction and existing properties less than one year old, both the cost and the market approaches must be used. If the property is a three or four unit building, the income approach must be used as well. However, the Department will rely on the appraiser's best supported final estimate of value obtained from any of these approaches. No longer will the appraiser's final estimate of value be restricted by the 3 percent difference between estimates. The appraiser's final estimate of value must be well explained and documented. If the appraiser does not have the plans, specifications and construction documents as well as the completed builder's certification at the time the appraisal is to be performed, the appraiser may not complete the appraisal until this documentation is made available.

When using the cost approach, the Marshall & Swift square foot method must be used by completing their form #1007. The pages from which the appraiser obtained the cost figures must be copied, the figures used in the calculations circled, and those pages attached to form #1007. (SEE HUD Handbook 4150.1 REV-1 for more instructions.)

#### VALUATION CONDITION (VC) SHEETS

The Department now requires the use of the same basic VC sheet nationwide with the exception of a FEW localized repair conditions established by the local HUD office. (Copy attached.)

FHA appraisals are done "AS REPAIRED" or as stated on the URAR, "subject to the repairs, alterations, inspections, or conditions...". This means the indicated value is reported as if all the repair items were completed. Since the lender selects the appraiser, the lender must inform the appraiser that the job is for an FHA case and that the appraiser is expected to use the VC sheet. If the appraiser is not familiar with the VC sheet, the lender is responsible for training the appraiser on its importance. Lenders, appraisers and FHA field offices must remember that required repairs are limited to those necessary to preserve the continued marketability of the property and to protect the health and safety of the occupants.

If there is a property condition disclosure statement, the appraiser should obtain a copy prior to performing the appraisal. (SEE ML 90-26 , dated July 26, 1990 for further information.)

If an appraisal report is field reviewed and repair items are discovered which were not reported, or reported to be completed when they are not, the lender and the appraiser will be subject to administrative sanctions.

#### APPRAISAL FORMS

Appraisals written on the Uniform Residential Appraisal Report form (URAR), the Federal National Mortgage Association's (FNMA) Individual Condominium Unit Appraisal Report form, or FNMA's Small Residential Income Property Appraisal Report form are acceptable to the Department. Currently, only these forms are acceptable for FHA cases. Other FNMA appraisal forms which are used for a streamlined appraisal or a qualitative sales comparison analysis are not acceptable at this time.

If you should have any questions concerning this Mortgagee Letter, please contact your local HUD Office.

Sincerely yours,

Nicolas P. Retsinas  
Assistant Secretary for Housing-  
Federal Housing Commissioner

Attachment  
Attachment to HUD Mortgagee Letter 97-22

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

NATIONAL VALUATION CONDITION (VC) SHEET

NOTE TO THE HOMEBUYER: THE VALUATION CONDITION (VC) SHEET IS FOR FHA USE ONLY AND NOT TO BE CONSIDERED AS AN FHA INSPECTION. IT IS NOT TO BE ASSUMED ALL PROBLEMATIC CONDITIONS WERE FOUND OR CORRECTED. FHA ENCOURAGES PURCHASERS TO HIRE A PRIVATE HOME INSPECTION SERVICE TO MAKE THE DETERMINATION THAT THE HOUSE IS ACCEPTABLE TO THEM.

FHA Case No \_\_\_\_\_

Date \_\_\_\_\_

Appraiser \_\_\_\_\_

State License No. \_\_\_\_\_

Property Street Address \_\_\_\_\_

City-State-Zip \_\_\_\_\_

LOCATION-PROPERTY ANALYSIS

\_\_\_ Location and Property Acceptable \_\_\_ Location Acceptable/property  
Rejected(See VC-12)  
\_\_\_ Location 223E/Property Acceptable \_\_\_ Location 223E/Property Rejected (See  
VC-12)  
\_\_\_ Location Rejected (See VC-12) \_\_\_ Location and Property Rejected (See VC-12)

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THE FOLLOWING CIRCLED CONDITIONS ARE HEREBY MADE A PART OF THE CAPTIONED  
DIRECT ENDORSEMENT STATEMENT OF VALUE. THE PURPOSE IS TO COMPLY WITH HUD  
HANDBOOK 4150.1 , REV-1 PARAGRAPHS 5-10 THROUGH 5-12, AND 4905.1, REV-1.

ALL REPAIRS MUST BE COMPLETED IN A PROFESSIONAL MANNER, IN COMPLIANCE WITH  
HUD'S GUIDELINES AND SATISFIED PRIOR TO CLOSING.

VC-1 STRUCTURAL DEFECTS

Structural deficiencies noted in the \_\_\_ foundation \_\_\_ floor support system,  
\_\_\_ framing \_\_\_ roof. Provide a report from a registered engineer regarding  
the cause and proposed correction. When proposed corrective measures are  
completed, the engineer must certify that the recommended repairs have been  
completed and all deficiencies have been acceptably corrected.

VC-2 ATTIC - BASEMENT - CRAWL SPACE

- A. Provide \_\_\_ access \_\_\_ adequate ventilation to the \_\_\_ attic \_\_\_ crawl  
space. (After access has been provided additional repair items may be  
required)
- B. Submit evidence from a licensed waterproofing specialist or licensed home  
inspector that the condition(s) causing wet basement and/or crawl space  
has  
been corrected. Describe affected area:

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VC-3 GRADING AND DRAINAGE

Regrade the lot to provide positive drainage away from the perimeter walls of  
the house.

VC-4 MECHANICAL SYSTEMS

A. The following utilities were turned off at time of appraisal.

\_\_\_\_\_water    \_\_\_\_\_gas    \_\_\_\_\_electric

The appraiser is required to revisit the property after these utilities are connected. Additional conditions may be required at the time the appraiser revisits the property.

B. Submit evidence from a licensed home inspector that the \_\_\_\_\_ system(s) are in safe operating condition. This evidence is required because:

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

VC-5 PRIVATE ROAD ACCESS AND MAINTENANCE

Submit evidence that (name of road) \_\_\_\_\_ is protected by a permanent recorded easement (non-exclusive, non-revocable roadway, driveway easement without trespass from the property to a public street/road) and that there is an acceptable maintenance agreement recorded on the property.

VC-6 WELL, INDIVIDUAL WATER SUPPLY AND SEPTIC

A. Submit evidence that the subject property is connected to public \_\_\_\_\_water \_\_\_\_\_sewer.

NOTE: Connection must be made to public or community water/sewage disposal system whenever feasible, i.e., feasibility relates to the distance to connect not the cost.

B. Provide acceptable \_\_\_\_\_bacteriological test, \_\_\_\_\_organic test, or any other test required by the State or local HUD office/HOC to determine the acceptability of the private water system. See ML 95-34

C. Provide evidence that the private sewer system is acceptable to the local health department.

VC-7 LEAD BASE PAINT HAZARD

Correct all defective paint surfaces for homes built before 1978, all paint chips must be removed in accordance with 24 CFR, Part 35.

VC-8 ROOFING

Replace existing roof with appropriate roofing material. Installation must comply with local acceptable building practice, or local building codes.

VC-9 CONDOMINIUMS AND PLANNED UNIT DEVELOPMENTS (PUD)

(FHA and VA)

A. This project is on FHA's approval list or accepted through reciprocity. \_\_\_\_\_Condominium    \_\_\_\_\_PUD

B. The unit is a spot loan.

NOTE:For all condominiums, the lender shall submit certification from the Condominium Association or Management Firm that the condominium ownership is 51% or greater prior to closing the loan. The certification shall be dated within 60 days of the closing date. Also, spot loan binders must be documented in accordance with Mortgage Letter 96-41 .

VC-10 PROPOSED CONSTRUCTION/UNDER CONSTRUCTION OR PROPERTIES LESS THAN ONE-YEAR OLD.

A.If any portion of the property (everything within the legal boundaries of the site) is located in a FEMA 100-year floodplain, the property is not eligible for FHA insurance.

B.The covered multifamily dwelling is not in compliance with handicapped accessibility requirements under Section 804(f) (3) (c) of the Fair Housing Amendments Act of 1988.

NOTE:A covered multifamily dwelling is a unit in a building consisting of 4 or more dwelling units if such building has one or more elevators; and ground floor dwelling units in other buildings consisting of 4 or more dwelling units.

VC-11 WOOD INFESTATION AND SOIL POISONING

A. Structure is ground level, or is a total wood structure. A recognized termite control operator shall furnish certification using form NPCA-1, or State-mandated form, that the house and other structures within the legal boundaries of the property indicate no evidence of active termite infestation and any damage having resulted from previous infestation has been repaired.

B. Structure is not ground level. No inspection required.

C. Structure located in a geographic area with no active termite infestation. No inspection required.

VC-12 OTHER REPAIR/CONDITION ITEMS SEEN BY APPRAISER NOT PREVIOUSLY LISTED.

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Please give number of attached pages with further explanation  
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Appraiser's Signature \_\_\_\_\_

Date \_\_\_\_\_